The extended governance of cooperative firms: inter-firm coordination and consistency of values.

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The extended governance of cooperative firms: inter-firm coordination and consistency of values

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Abstract

This work aims at providing a framework to help analyse governance in networks of cooperative firms. It builds on four bodies of literature: cooperation, transaction costs, monopoly capitalism, production networks. It considers four variables from transaction cost theory, which we use to interpret the governance of cooperative firms and their networks. These are: (1) values, (2) property rights, (3) control, (4) resource allocation. We associate the specific principles that define the identity of cooperative organisations (self-help, members' ownership, democratic control, financial participation, limited capital remuneration) alongside these dimensions. We then apply the same dimensions to production networks and propose a stylised networking model for cooperatives and identify two polarised types of networks: (1) heterarchical forms of coordination based on cooperation and mutual help, (2) hierarchical coordination based on exclusive direction.

Keywords: Cooperatives, Cooperative Principles, Control, Production Networks, Monopoly Capitalism, Democratic Governance

JEL classification codes: P13, L23

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[W]e are still very ignorant about institutions"

Williamson, 2000: 595

1. Introduction

There are 4.7 million people employed by cooperatives in Europe (Roelants, Dovgan, Eum & Terrasi, 2012). Cooperation is a prominent phenomenon in France, Italy, Spain and it is growing in the UK, where medium to small cooperatives represent an important part of the economy. The cooperative basic idea is centred on the specific aim of membership welfare to be reached by means of democratic governance. Albeit much has been written on the dispositions, practices and outcomes affecting economic sustainability, member welfare and - through this - community welfare, scholarly conversations on the impact of cooperative strategies on other stakeholders (besides members) need to be developed further (Sacchetti, 2013). Think in particular about production relationships. One of the most striking characteristics of the way today firms organise their production is in the richness of connections with other firms/organisations. The flourishing of an increasing number and variety of linkages has developed in parallel with globalisation, the progressive intensification of inter-firm relations across regions and countries. It became, therefore, very topical during the 1990s to be concerned with networking amongst firms whether, for instance, focusing on strategic alliances, or whether emphasising the relative strength and weaknesses of organising activities inside the firm or through inter-firm relationships.

This paper has been written with the specific aim of clarifying how cooperatives engage in production relations with other firms. An assessment of inter-firm relations, in our view, cannot isolate from the value-based nature of cooperatives. Our reasoning proceeds as follows. Cooperatives are embedded in a set of explicit values and principles which define their governance structure. Governance rules define who decides about what to produce, where and how. Production organisation has therefore important distributional implications, since by dividing labour it also distributes learning, innovation and surplus opportunities across the organisation and other firms (Kaplinsky, 2000). Whilst, however, cooperatives are explicit on internal governance rules, there is no explicit reference to the way they relate with other production stakeholders, how surplus and other opportunities are distributed and to what ends.

The vast literature on production democracy does not address inter-firm relations, albeit they constitute the essence of production organisation or of the way control over distributional issues is allocated. On the other hand value-chain literature has always focused on inter-firm division of labour amongst conventional for-profit firms (Cf. Kanter, 1989; Kaplinsky, 2000; Jarillo, 1988; Porter, 1990; Sacchetti and Sugden, 2003). Assessing production networks by cooperative firms requires therefore bridging these two streams of work. To this aim, we first need to disentangle democratic values and principles looking beyond the micro-level of internal incentives and employment, and even beyond the internal governance structure. The entire point of engaging in this effort is that if we challenge the values of cooperation at a fundamental ontological level, we can possibly understand whether these organisations may have a consistent and lasting grip on production governance beyond their legal borders.

To illustrate, consider the recent debate about worker cooperatives in times of crisis. The European Confederation of Worker Cooperatives, Social Cooperatives and Social and Participative Enterprises (CECOP) highlights subcontracting as an alternative or complementary solution (amongst others) to the use of cooperative reserves (CECOP, 2012). A perspective on inter-firm relations would suggest a more careful approach, as the stability of employment in worker cooperatives needs to be weighed against the implications of its external strategies, controlling in particular for the distribution of the positive and negative effects on for-profit subcontractors and subsidiaries.

Our double concern with values and with who controls production decisions reasserts that we are not addressing relationships amongst neutral agents. Rather we speak of the basic cell of production, the firm, its fundamental values, and the power that it can exert over other actors, such as employees, clients and other firms, although our analysis concentrates on the latter. Through this approach we substantially understand inter-firm relationships in terms of networks of forces (Sacchetti and Sugden, 2003). The general idea is to reach beyond the internal organisation of production and its democratic principles to understand how inter-firm coordination structures can impact on the welfare of connected actors, beside members. The relevance of our perspective is in the impacts that inter-firm relations involving cooperatives can have on the welfare of a multiplicity of organisations and the communities where these are located. This problem assumes particular relevance in the context of cooperative identity, which explicitly recognises cooperative autonomy, cooperation among cooperatives and community welfare as part of its constituent principles (ICA, 1995).

In order to concentrate on external production governance and its impacts we will assume that, internally, the cooperative is equipped with deliberative democracy processes that ensure a shared understanding of cooperative values and aims[i] and that internal governance and practices reflect the essential economic objective of promoting the welfare of members. Albeit this is a simplification of an evolving complex reality, it allows us to concentrate on the coherence of external governance with respect to the principles of cooperation.

The paper proceeds as follows. We first consider four dimensions from transaction cost theory, which we use to interpret a layered model of cooperative governance and networks linkages thereof. These are: (1) values, (2) property rights, (3) control structure, (4) resource allocation. We interpret the values and principles that define the identity of cooperative organisations alongside these dimensions. We then apply the same dimensions to production networks and propose a stylised, value-based network model for cooperatives. Against this normative conceptualisation we consider inter-firm relations in practice injecting power in our analysis. Depending on its distribution across networked firms, we identify two polarised types of networks: (1) heterarchical forms of coordination based on cooperation and mutual help, (2) hierarchical coordination based on exclusive direction. For each network type the paper presents illustrations focusing on specific institutions and regional experiences. We compare both types with our stylised, normative framework. The last Section offers a concluding summary and recommendations.

2. The value-laden nature of cooperatives

New-institutionalism provides an explanation on why firms emerge and why they develop by "economising" on governance costs (Williamson, 1990). The governance institutions of the firm aim at minimising conflict, hazard and uncertainty over behaviours and outcomes. In a later contribution, Williamson (2000) positions new-institutionalism into a layered framework which grounds a) property rights, b) governance structures and c) economic incentives into informal socioeconomic institutions, e.g. habits, traditions, values, norms.

What Williamson seems to suggest with his framework is that formal institutions can be grounded on a variety of informal social institutions as long as they economise. This multi-layered approach is particularly relevant in our case, since cooperatives are defined by norms that reflect values such as “self-help, self-responsibility, democracy, equality, equity, solidarity, justice, mutual help” as well as “social responsibility and caring for others” (ICA, 1995). These values are implemented through the seven ICA principles: voluntary and open membership, democratic member control, members’ economic participation, autonomy and independence, education training and information, cooperation among cooperatives, concern for community. These are not, as a norm, emphasised within conventional business communities. Rather, they represent the niche culture,[ii] not typically rewarded in the market place.

Because compared with conventional firms’ values and aims, the economic efficiency principle is erroneously presented as a constraint that cooperative governance needs to meet,[iii] whilst overall the nature and objectives of cooperatives would be best understood as fulfilment of the ICA seven principles (Cf. Novkovic, Prokopowicz & Stocki, 2012). Rather, we would say that given the values, aims and principles that lead cooperative economic activity, the governance structure of cooperative firms is in fact economising. We can appreciate this observation by systematically interpreting the values and principles of cooperation in conjunction with the formal institutions of cooperation. We use Williamson’s layered framework and position values at the basis of all subsequent institutional formalisations (Level 1, Figure 1).

Figure 1 (bottom)

Ownership rights and governance structures work as constraining and enabling institutional mechanisms aimed at economic sustainability on the one hand, whilst pursuing fulfilment of basic cooperatives values on the other (Cf. Commons, 1934). At Level 2 we place those principles regarding the nature of property rights. In particular, the designation of *who* owns and control resources responds to principles of voluntary and open membership, joint ownership of members, and members’ economic participation. The general aim is to increase members’ welfare through self-help, self-responsibility, and mutuality. The definition of property rights in cooperatives has been brought to the fore by Hansman’s work. A strong interpretation of his argument (as in Borzaga and Tortia, 2010) is that cooperatives can be seen as substitutes of investor-owned organizations when the market fails, especially in the presence of asymmetric distribution of market power ex-ante (monopoly and monopsony power) and ex-post (contractual failures and lock-in into contractual relations). Failures are usually found when markets are either not competitive enough, or are not properly regulated (Hansmann, 1988, 1996, 2013). On the other hand, when established, cooperatives have been able to achieve sustainability and resilience since they are reported to last significantly longer than investor-owned firms (Burdín, 2013). In this interpretation, the relatively small number of cooperatives is not due to their inability to withstand market competition, but to a lower rate of creation, which can be explained if we acknowledge that cooperatives have an *explicit* value-laden nature and that such values are not dominant in current economic systems. Also, the weak interest of external investors in financing cooperatives[iv] (regarding mainly loans or to the purchase of cooperative bonds) places the obligation to fulfil economic, financial, and organisational requirements directly on the self-organised membership.

This brings us to the third Level, where principles define *how* control over the use of resources has to be implemented. Within the cooperative model, the principles of democratic member control and participation in the allocation of surplus define the internal governance structure. The purpose of these instruments, specifically, is to achieve procedural fairness, as per the values of democracy, equality and equity (Tyler & Blader, 2000; Tortia, 2008).The governance structure represents an effort to construct a democratic order, thereby eliminating conflict (between investors and other major patrons) and distributing decision-making power. However structural choices do not seem to be sufficient for mitigating ex-post conflict. Evidence of the difficulties of implementing democratic governance is subsumed by the three dimensions identified by Cornforth, Thomas, Lewis and Spear (1988). These are: a) “constitutional degeneration,” which occurs when decision-making power shifts from the members to a restricted group and turns into the exercise of power by an elite; b) “capitalist degeneration,” when cooperatives adopt financial instruments and practices that are typical of investor-controlled firms; c) “internal pressures” when misbehaviour and opportunism increase managerial control at the expenses of democratic and deliberative processes (Cf. Varman and Chakrabarti, 2004).

This last point takes us to Level 4, where incentives are aligned with the governance structure so as to match individual behaviours with firm’s objectives. In cooperatives, the rules underpinning the actual allocation of resources are defined by an internal incentive system which emphasises limited remuneration of capital as well as the reinvestment of residual income for mutualistic and communitarian purposes. These instruments are particularly oriented towards the pursuit of distributive fairness, long-term sustainability and the creation of societal value.

2.1. Heterarchical integration of stakeholders

The multi-stakeholder cooperative is a particular case of Level 2 and 3 institutions. Multi-stakeholder governance is the specific organisational solution designed to internalise the complexity of multiple stakeholders’ objectives (Sacchetti and Tortia, 2014). This solution is common when the aims of cooperatives are public, for example in the provision of social services. Through multi-stakeholdership the allocation of strategic control is shared amongst a multiplicity of patrons, who have voice also in decisions about the allocation of surplus. The identification of stakeholders and the allocation of strategic decision-making power is – as Bacchiega and Borzaga (2001) observe – “a consequence of the type of redistributional needs and market failures that characterise the production of a specific good or service.”

The internalisation of the network of stakeholders and their multiple interdependent interests increases complexity and requires, at Level 2, that stakeholders craft property rights and distributional rules that ensure mutuality, equality and democratic control. Deliberative praxis at Level 3 and incentive systems at Level 4 need to be shaped to include multiple perspectives, reduce potential conflicts and reach agreement in the long-run interests of all partners. Multi-stakeholdership is therefore meant to reduce the production of negative externalities whilst producing positive externalities for society. This shows a high consistency with the cooperative principles promoting self-help, self-responsibility and mutuality, equity and the production of societal value (Sacchetti and Tortia, 2014).

3. The cooperative governance of production linkages

Similarly to what has been argued about traditional for-profit firms, cooperatives do not work in isolation. Extending Coase’s warning cooperatives cannot be considered as “islands of economic planning” (Coase, 1937). Rather, they are businesses which operate in the market, interacting with its extent, structure and technologies, whilst being placed in a context often dominated by investor-owned firms, their for-profit nature and related incentives . Both large corporations and smaller firms rely for their activities upon a mesh of linkages and relations with other firms, which can be based in different localities. The theme of the division of labour amongst firms is not new, and Marshall (1921) already emphasised how production on a large scale could be undertaken by the co-ordination of activities of small production units. Not only can the scale of activities be augmented through networking. Through linkages, firms may benefit of a multiplicity of competencies and sources of experience that enlarge the scope of their production. Remarkably, one of the reasons which pushes firms to build external linkages is the need to find the synergies to solve specific production problems.

By virtue of their linkages, firms commit to various degrees to other external actors. Such commitment may be reciprocal and may represent a source of opportunities for the firm, or it can become the thread through which the firm that retains greater economic power directs the other. Take, for instance, the case of subcontracting relations. They might imply professional subordination and economic dependence of the subcontractor, conferring to quasi-vertical organisations a strong hierarchical character. Pyramidal structures of subcontracting relations, for instance, have been produced out of evidence from the automobile industry (Semlinger, 1993; Helper, 1993). Typically through contractual agreements, the large corporation exercises its control over other firms without having to internalise their activities (Cowling and Sugden, 1994). The result could be “strategic failure” (Cowling and Sugden, 1998): concentration of strategic decision-making power in the hands of a few might imply that production governance fails to effectively pursue the interests of the network of firms at large.

Being businesses with explicit values, cooperatives can have a purpose for building their networks differently from what described above. Cooperative networks can work as enablers and amplifiers of the values of cooperation, thus generating positive effects across societies at large. The idea being that networks that reproduce, in their praxis and outcomes, the values of cooperation can help in achieving a “critical mass” of cooperative attitudes, which would otherwise run the risk of being displaced by the prevailing values underpinning conventional economic aims and processes (Witt, 2003).

However, networking may not be synonymous with cooperation not even in the case of cooperative firms. Since the focus of cooperative principles is on internal membership, cooperatives construct formal and relational networks interpreting their values in different ways. Specifically, relations are formed in the market context, where performance is conventionally measured by pecuniary achievement (Veblen 1899/2003). The pervasiveness of the profit motivation and related practices, namely in terms of control allocation and distributional effects, becomes of concern when conventional business aims are placed before cooperative aims (Weisbrod, 1998).

These concerns offer a fertile terrain for an analysis that discriminates amongst the different modalities used by cooperatives to govern inter-firm relations.

3.1. A normative framework for networks

We associate the specific principles that define the identity of cooperative organisations alongside formal inter-firm network institutions, and propose a stylised networking model for cooperatives.

Figure 2 (bottom)

What would the institutions of a cooperative network be, if we accepted the validity of cooperative values and principles in defining inter-firm relations? From a normative perspective, the definition of formal network institutions may be exemplified by second level cooperatives, for example consortia or cooperative groups, which take the form of cooperatives of cooperatives (Level 2). This form of collaboration would be consistent with joint member ownership at Level 2 and democratic member control at Level 3 in our framework. Likewise other contracts (e.g. financial participation, partnerships, subcontracting) should be drafted so that the governance structure of the network is heterarchical, participatory and democratic. At Level 4 the allocation of surplus should follow similar rules to those of first level cooperatives. In the case of second level cooperatives distribution of material and immaterial surplus is defined through participatory and non-exclusive mechanisms, which take into account the objectives and the needs of all involved constituencies. Likewise, incentives should be drafted to achieve mutual benefit with no parties exploiting their competitive advantages against others' interests. For example, strategic decisions about division of labour or the possibility to upgrade knowledge and technology would aim at avoiding the concentration of rent opportunities across the network (Cf. Kaplinsky, 2000). The fairness of distributional outcomes would be a direct result of the democratic control at Level 3.

3.2. Network praxis and monopoly capitalism

Against the stylised normative idea of inter-firm coordination illustrated above, network praxis entails diverse approaches to formal and substantive control allocation, to membership, common resources, and their management.

Much has been written on networking of capitalist enterprises. The analysis of conventional corporations has emphasised that markets are not in general competitive and that control without ownership can be observed also between firms, not only internally as theorised by agency theory (Cowling, 1982; Cowling and Sugden, 1987). Under monopoly capitalism conventional firms would aim at maximising profits not only by pursuing monopoly power on the end-product market but also along the value chain by moving production activities across countries and by subcontracting production phases to dependent firms (ibid.).

Cowling and Sugden (ibid.), therefore, conceive the firm in terms of its strategic influence over other actors, such as governments, labour, clients, subcontractors. The firm, therefore, may be defined as the strategic planner and controller of an international network of production, which includes all those actors on which the strategic decision-making of the firm has a substantial influence.

We would argue that if cooperatives mimic the strategy of conventional firms under monopoly capitalism and pursue exclusive direction over production linkages, not only network governance will not be economizing, but the cooperative will dilute its identity and fail to produce the positive externalities of cooperation.

Building on monopoly capitalism literature, we focus on the distribution of control power and rent across the network and operate a fundamental differentiation amongst cooperative firms. For each of its external linkages a cooperative firm can be considered as:

(a) An *inter*-actor, or an active participant which relates with another firm on a mutual and reciprocal basis. This relational form conforms with the cooperative ideal described in Figure 2, as it emphasises heterarchical relations based on deliberation, reciprocity, and mutual dependence in strategic decision-making, such as on the allocation of control and rent distribution (Sacchetti & Sugden 2003, 2009).

(b) The *recipient* of another organisation's strategic choices, or an organisation which is mostly subject to production decisions taken elsewhere and which impact on what is produced and how, what it is learned and rent distribution. Here the recipient firm assumes a passive role and control is *de facto* external to the firm.

(c) A *director*. The cooperative is an external source of control and direction for another firm. Reflecting monopoly capitalism critiques, the active role of the director carries the potential of being exerted at the expenses of the recipient, who is excluded from strategic decisions of interest. The alienation of control rights impacts also on other strategic decisions, such as the production of a residual income and its allocation. The director-recipient relation would not be consistent with the general principles of mutual-help, autonomy and independence of cooperatives since it would detach some of the cooperative principles from actual strategic behaviour.

We use the heterarchical/hierarchical criterion to increase our understanding of the nature and implications of specific solutions, such as non-profit consortia, the network contract, public-private partnerships, social capital networks, financial linkages, subcontracting, and market relations through and by relating this to cooperative principles.

Figure 3 about here

4. Heterarchical coordination via external linkages

We talk of heterarchical coordination when strategic production decisions are not exclusively taken from one major centre and then enforced on others, but self-managed with the aim of recognising reciprocal interests and mutual dependence around shared common activities. Across the heterarchical network, cooperatives keep their autonomy whilst identifying common activities around which labour is coordinated by means of shared common rules. The norms applied throughout the network define also how the benefits of shared activities are distributed. In heterarchical networks these norms are designed to increase the opportunities of each and every network member.

4.1. Non-profit consortia of small and medium cooperatives (SMCs)

Small and medium size cooperatives (SMCs) are likely to be subject to dependence on their main contractors, whether those are conventional firms, larger cooperatives or public administrations. Consider for example the provision of social services, where social cooperatives currently play a large role (in Italy and in various other countries). Typically the public sector would work as the main contractor of local social cooperatives. In this case we can talk of *public-sector-anchored cooperatives* whose objectives, methods and sustainability are mostly influenced by the welfare policy and standards set alongside public administrators' decision to externalise public services.

In the case of public-sector-anchored cooperatives, consistency – and in particular the principle of cooperative autonomy and independence – needs to be tested in practice, as dependence on the public sector is generally high and can expose the cooperative to the dangers of public failure. Consider, for example, inefficiencies in public administrations causing delays that make social cooperatives insolvent, eventually bankrupt, and service beneficiaries uncovered. Consider also the tendency of the public sector to prefer the delivery of standardized and easily controllable services, to the experimentation of innovative, but more effective and creative solutions. Again, where the decision-making power of the membership is subordinated to the strategies of third parties, the principles of the cooperative may be at risk, and likewise member rights.

As a response, SMCs can resort to consortia to foster mutual-help. The consortium can be conceived as an instrument to achieve a critical mass of cooperative values and define the identity of cooperative organisations, normally through a shared code of practice. They are typically backed by network statutes, aims and values declarations, as well as by common assets which can be used to pursue objectives common to the participating organizations. Through consortia, cooperatives aim at accessing and creating business opportunities, innovation and knowledge transfer, capacity building and scale economies. Common assets at the same time support cooperative start-ups and buffer financial needs. The governance of consortia is not strictly regulated by law, but is intended to be horizontal and prevalently democratic, since decision making power needs to be shared among all involved organizations.

Consortia of this sort are not-for-profit collective organisations, grounded on peer-support and peer-control, entrusting behaviours and practices that characterise social capital and that privilege inclusion, communication, mutuality and trust. Control rights in consortia indicate how common reserves are managed by cooperating organisations, and provide guidance on the incentives operating across the network. Relationships typically involve a plurality of inter-actors with diverse and evolving interests and do not allow for direct control over production choices of firms in the consortium.

4.1.1. The case of the CGM and its evolution

A notable example of this kind of network is, in Italy, CGM (Consorzio Gino Mattarelli), formed by one national consortia, 78 local consortia, 1,000 associate social cooperatives, about 7,000 operational units throughout Italy (in 70 Provinces out of 107 and in all of 20 Italian Regions), and about 45,000 workers (including both worker-members in cooperatives and employees).[v] In 2012 CGM turnover was higher than 1.1 billion Euro. CGM is a second level consortia founded in 1987 (Borzaga and Ianes, 2006; Ianes and Tortia, 2009). Within its national network many cooperatives are characterized by cross financial participation, whereby financial members part take the patrimony of the organization and are granted the right to elect their representatives in the Board of Directors, though they can never reach a controlling position.

In 2005 CGM was constituted as a Cooperative Group.[vi] With this new structure CGM becomes the core organization directing the whole network. The Group flanks the original national consortium, which keeps its coordination role at an operational, executive level.

This governance evolution can be interpreted in terms of hybridization of the basic mutualistic structure (Spear, 2012). The new governance structure was in fact accompanied by the creation of 70 transversal organizations, which may, but need not, be cooperatives. These organizations are in charge of producing specialized services for the associated grass-root cooperatives. They support entry into new sectors, especially capital intensive ones, with high entry barriers (and potentially higher rents) such as healthcare, which has not been addressed by social cooperation to date. By supporting entry in markets with high entry barriers, the new organizations in CGM are functional also to the achievement of scale and competence pools against market failure, which address the specific inefficiencies originated by monopolistic/monopsonistic positions of service suppliers and buyers, such as the public sector or other conventional private firms. These strategies may be absent or ineffective when the cooperative acts in isolation. Peer networking and monitoring through consortia has, therefore, the potential to distance cooperatives from practices and incentive systems that are functional to conventional for-profit organisations whilst, at the same time, protecting them from subordination to monopoly power.

Overall, CGM emerged as formalized horizontal and multi-layered network of small grass-root organizations. The founding structure is still in place. On its pillars, new elements (heterarchical and hierarchical, operational and strategic) have been added to improve efficiency in terms of market opportunities and coordination.

4.1.2. The case of credit cooperatives in the Trentino Alto-Adige Region

The case of credit cooperatives (BCC, Banche di Credito Cooperative) in Trentino – Alto-Adige is a successful experience of heterarchical coordination by means of consortia. Trentino – Alto-Adige borders with Austria in North Eastern Italy and is an autonomous region since 1972. It is populated by about one million people, across the two Provinces of Trento and Bolzano. The latter is the capital of South Tyrol, the only German speaking area in Italy. Informed by the social doctrine of the Catholic Church, the first cooperative bank in Trentino was started by Father Lorenzo Guetti in 1892 on the model of the German Raiffeisen cooperative bank, shortly after the publication of the encyclical letter *Rerum Novarun* by Pope Leone XIII in 1991. Cooperatives credit banks where created by farmers through the institute of unlimited responsibility to overcome usury and credit rationing by large commercial banks. Following a historical trend of ever increasing economic and social relevance, today 40 credit cooperatives with about 400 branches are embedded in the Province of Trento and manage about 60 per cent of the total amount of credit in the area. There are 124,000 members and 3,000 employees. Credit cooperatives in Trentino, like in the rest of Italy, are small to medium size local banks, whose territorial reach is limited and regulated by law. They are configured as a tightly knit collaborative Federation. The degree of formalization and complexity of the network is high, similarly to the Federal Association of Co-operative Banks (*Volksbanken* and *Raiffeisenbanken*) in Germany. The Federation has functions of representation, fiscal and legal assistance, consulting, training and communication. The extensive network of local cooperatives (in several peripheral municipalities in Trentino the cooperative bank is the only existing bank) is now centred around a second level consortia, the Central Cooperative Bank (*Cassa Centrale Banca*), which was created in 1974 and delivers products and services exclusively to the federated banks. Among other notable structures, a Guarantee Fund *(Fondo di Garanzia Istituzionale)* was created by the Federation in 2008 to contrast the systemic risk coming from the global financial crisis. Also, the Federation created and runs a number of 'system' companies that deliver specialized services, such as asset management, information systems, insurance contracts and training.

This structure of inter-firm cooperation has allowed promoting cooperative principles in several ways. Specifically it has allowed overcoming monopolistic power on the credit market and usury. At the same time it has supported peripheral small and medium enterprises and the economies in which these are embedded. The ability of cooperatives to operate effectively in peripheral areas without exploiting their local monopoly power is noteworthy and shows the economic potential of this kind of organization.

4.2. The "network contract"

An interesting example of institutional innovation that supports network creation and governance is the "network contract", instituted in Italy in 2009 to favour the creation of new, collaborative networks and to increase the stability of existing networks. Its introduction was part of the policy measures towards the economic downturn to enhance innovation and competitiveness. The network contract is intended to have definite scope: it is created to reach an objective common to the networked organizations and lasts (when not renewed) until the aim is achieved. This is one of the main aspects differentiating the network contract from consortia, which are instead stable open-ended coordination structures for common functions and services. Because of its venture nature, the network contract is recognized in public tenders as a viable form of aggregation of a plurality of organizations (Cf. Iamiceli, 2006).

Each networked organization keeps its legal independence, whilst interdependencies attached to shared production activities are recognised by the effort of each and every firm to pursue the common interests of all partners (Cf. Sacchetti and Sugden 2003 on networks of mutual dependence).[vii] Albeit the network contract is not incompatible with hierarchical control by a larger or contractually stronger organization, it leaves wide room to cooperatives to shape the agreement consistently with cooperative values and aims. Specifically the institution of the board and of a common capital asset can reflect mutuality and democratic decision-making principles amongst the partners, whilst avoiding to create concentration of control and decision-making power. Cafaggi, Iamiceli and Mosco (2013) analyse 333 network contracts underwritten in Italy before 2012.[viii] They evidence that, albeit not required by law, most contracts provide for the presence of a common fund and of a common governing body in charge of the utilization of financial resources.

4.3. Public-private partnerships

Public-private partnerships are developed through dedicated policies aimed at promoting community welfare by means of public procurement. Take as an example the Community Benefit Clause (CBC) used in public procurement in the UK and specifically in Scotland. CBCs were conceived by the Scottish Government to foster "sustainable procurement," "a process whereby organisations meet their needs for goods, services, works and utilities in a way that achieves value for money on a whole life basis in terms of generating benefits to society and the economy, whilst minimising damage to the environment" (Sustainable Procurement Task Force 2006: 10; Scottish Government 2008). The community development aim provides a strong incentive to contractors to conform to the principle of community care and to contract out activities to those organisations that best serve the procurement broader objectives. For example contracting out the delivery of specific services to social enterprises would represent, for the main contractor, a strategy for fulfilling the required social objectives, such as creating local jobs and increasing the work integration of the disadvantaged.

4.4. Social Capital Networks

Social capital networks (SCNs) are described in Campbell and Sacchetti (2013). They can be defined as heterarchical coordination mechanisms, which encompass essentially the same set of values that are applied by participant organisations. SCNs reflect the main aims of consortia, albeit without using a formal organisation. They are based on informal ties and kept together by a coordinator (typically a third sector organisation, not necessarily a cooperative), periodic meetings, and by use of social media. This practice is enabled also by the small dimension of the networks. The main asset in SCNs is relational rather than financial, offering linkages not only amongst organisations that are close and alike (bonding social capital), but also with other types of businesses other than cooperative organisations (bridging social capital) and at higher institutional levels, e.g. to access procurement opportunities (linking social capital) (Cf. Putnam 2002; Szreter and Woolcock 2004). For these reasons, social capital networks represent the humus that facilitates the creation of more formal relations, and are therefore to be seen as a backbone for developing types of heterarchical networks of the sort described in the above sections (e.g. consortia, network contracts, public-private partnerships).

The case of the development of Social Enterprise Networks in Scotland illustrates the development model followed in the creation of the networks. The founder used his understanding of social capital theory, centred on the value of cooperation and community welfare, to introduce a network form of peer support that would take social entrepreneurs out of isolation and provide them with specific voice and specialised support. Through these networks, thematic and geographic, social entrepreneurs have formed communities of practice and have started to collectively act in order to establish and reinforce the norms of behaviour shared by social enterprises in Scotland. One of the main aims that social entrepreneurs shared was to become independent and autonomous from external influences, hence to move away from grant dependence. The fact that participants in the network shared the same values provided a basis for furthering communication, sharing experiences, and identifying multiple perspectives and mutually beneficial opportunities. The modality of interaction chosen was that of a heterarchical network, which encompassed essentially the same set of preferences on aims and processes that social entrepreneurs already applied to their own organisations. This model could be imitated also by cooperatives with which social enterprises share a variety of intents.

5. Hierarchical coordination via external linkages

We can talk of hierarchical coordination when production decisions are orchestrated from one major centre, a hub cooperative, which plays the most prominent role in deciding how production and knowledge creation should be divided along the value chain. Since the distribution of income across networked firms depends on the way production is divided, the principles applied by the governing firm define also how benefits are distributed across the network (Kaplinsky, 2000; Sacchetti 2004). The hub cooperative could therefore promote cooperative principles through its coordinating function, designing a network system that redistributes incomes through the production network. Oppositely it could strategically allocate production across the network to increase its economic power.

5.1. Cooperative hub-led coordination

In the first case, we can talk of a *cooperative hub-led coordination***.** Through cooperative hub-led coordination the core organisation applies cooperative principles also to external governance, actively searching for mutually beneficial opportunities, for compatibility between the objectives of members and the interests of other stakeholders. The application of the cooperative principles to other firms would add consistency to the organisation also internally, although this may increase the tensions between those who perceive the cooperative as being essentially about the welfare of members and those who would regard strategic behaviour towards others outside the cooperative as subject to similar principles. When the cooperative coordinates its different sets of relations on the ground of cooperative values and principles more generally, external coordination would endorse (through appropriate mixes of financial participation, contractual arrangements, networking and other substantive practices) participatory governance processes and mutually beneficial incentive structures (Sacchetti, 2013).

5.2. Exclusive hub-led coordination

In the opposite case, we talk of *exclusive hub-led coordination*, when cooperative values are confined within the cooperative organisational borders of the core firm. Relations with subsidiaries through financial integration or contract-based relationships such as ventures, subcontracting arrangements or shorter-term market relations are, in this stylised form of coordination, functional to the objectives of the core cooperative or particular groups within it, even despite the welfare of suppliers, partner companies or subcontractors. In line with recent monopoly power critiques (Cowling & Sugden, 1998; Sacchetti & Sugden 2003) we suggest that when the hub cooperative uses its power advantage to take strategic decisions despite the long-term sustainability of the 'recipients', consistency between mutualistic principles of cooperatives and the wider principles of cooperation is undermined.

As an illustration, consider a hub cooperative acting as the 'director' of the supply chain, the cooperative may manage relations in different ways. In fact, the greater the distance from the perfectly competitive market benchmark, the higher the relevance of firm behaviour and, therefore, strategic choice on coordination mechanisms. Despite its non-for profit nature, the cooperative could, as a possibility, seek monopoly power or collusive agreements with other producers, or exert its market power against suppliers. Where the competitive element is more incisive, strategy may focus further on permanent cost minimisation by stimulating arm's length market competition among substitutable producers, typically for low knowledge content production types.

In summary, we talk about exclusive hub-led coordination when the modalities of the interaction resemble governance by exclusive direction, where relationships are administered strategically without integrating in strategic choice the interest of related firms. This is a case of coordination without cooperation.

5.3. The evolving nature of coordination. An illustration from the Mondragon Group

In practice cooperatives, and those of large size in particular, coordinate with other firms through a variety of mechanisms, and can resort to both exclusive or cooperative hub-led coordination. To illustrate, consider the expansion and internationalisation of the Mondragon Cooperative Corporation, which, in 2012, associated 257 organisations (110 cooperatives and 147 subsidiaries), employed over 80,000, of which 66,418 in Spain (Mondragon Corp., 2013) and about 32 thousand are members of the cooperatives.[ix] Despite its shared values, internal and international growth has not occurred without tensions. In particular, the expansion of retailing in Spain (the Eroski retail chain employs 45,000) and manufacturing overseas involving 65 production plants and 14.601 employees in 2006 (Monasterio, Telleria & Etxebarria, 2009) has been shaped by a strategy of acquisitions and green-field investments for the creation of subsidiaries, without worker membership. Overseas the Mondragon group has adopted a strategy towards internationalisation similar, in some respects, to those of traditional transnational corporations (Errasti, Heras, Bakaikoa, & Elgoibar, 2003; Errasti, 2013). FDIs have reflected, in part, a strategy of cost minimisation, but also risk reduction in the face of diverse workers attitudes regarding employee ownership across countries, and different legal and juridical frameworks.[x] Overall, the growth strategy of Mondragon has raised an issue around their actual values, where the pursuit of members' welfare becomes a cost for other workers inside controlled or otherwise affiliated companies. The challenges to the idea of membership presented by growth across sectors and regions, through internationalisation, are currently unresolved, but likely to change again the architecture of rules at Mondragon. These challenges are mixing with the backlash of the economic crisis, which led the oldest and largest Mondragon industrial cooperative, Fagor, to file for bankruptcy protection at the end of 2013, while the retail chain store of the group, Eroski - one of the largest in Europe - is facing difficulties as well. The likely lay–off of many non-member workers in subsidiaries and stores outside Spain will require a deep reshaping of the policies towards membership and employed labour, and towards networking inside and outside Spain. Against changing contextual conditions, the development of the group's internal and external governance requires complex operations of social reconstruction, building "the road while travelling" (Morrison, 1991). Because explicit on its values, cooperative development has shown to be strongly connected with institutional development, reinforcing the need for a constant appraisal and elaboration of strategies and practices that are coherent with cooperative values and identity (Arando, Freundlich, Gago, Jones et al. 2010; Jones & Kalmi, 2012; Morrison, 1991; Stikkers, 2011; Turnbull, 1995).

6. Concluding remarks

We have started this contribution by considering the extent to which the nature of inter-firm coordination can be deemed consistent with the nature of cooperation and its principles. Our analysis has emphasised that heterarchical networks and cooperative hub-led networks, more than the large cooperative corporation, can spread cooperative values. Following our analysis and examples, the invitation to scholars working on the democratic governance of production organisations is to appreciate the impacts of cooperatives also through their extended production governance, focusing on how cooperative principles features differently across inter-firm relations and on how formal institutions can be improved to reflect cooperation at all governance levels.

The implications for practitioners would be in terms of developing inter-firm relations around an extended notion of mutuality, by acknowledging, through appropriate rules and processes, multiple perspectives and interests. To support this process, managers in cooperative organisations can resort to the legal frameworks that best reflect cooperative principles, such as consortia and the network contract. From a substantive point of view, they can improve means of communication and deliberation, not least to achieve an inter-subjective understanding of practices consistent with the meaning and value of cooperation. This on-going dialogue can lead to the possibility to collectively evolve intermediate governance structures and non-exploitative contracts. We have pointed in particular at cooperative hub-led coordination and heterarchical networks as institutional solutions that embed peer-support and democratic governance by means of formal or customary rules.

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Figure 1

Internal Institutional Levels

LEVEL	COOPERATIVE NICHE CULTURE	PURPOSE
I. INFORMAL INSTITUTIONS Individual values and believes, culture on the organisation of economic activities	Self-help, self-responsibility, democracy, equality, equity, solidarity, justice, mutual help, social responsibility and caring for others	Fulfilment of needs and desires
II. FORMAL INSTITUTIONS Property rights: who controls and appropriates resources	Voluntary and open membership Ownership of members	To increase members' welfare
III. GOVERNANCE STRUCTURE How control is implemented	Democratic member control. Participation in the finance and in the allocation of surplus. Autonomy.	Procedural fairness
IV. RESOURCE ALLOCATION Incentive structure	Limited remuneration of capital Reinvestment for mutualistic and communitarian purposes	Distributive fairness Long term sustainability Creation of societal value

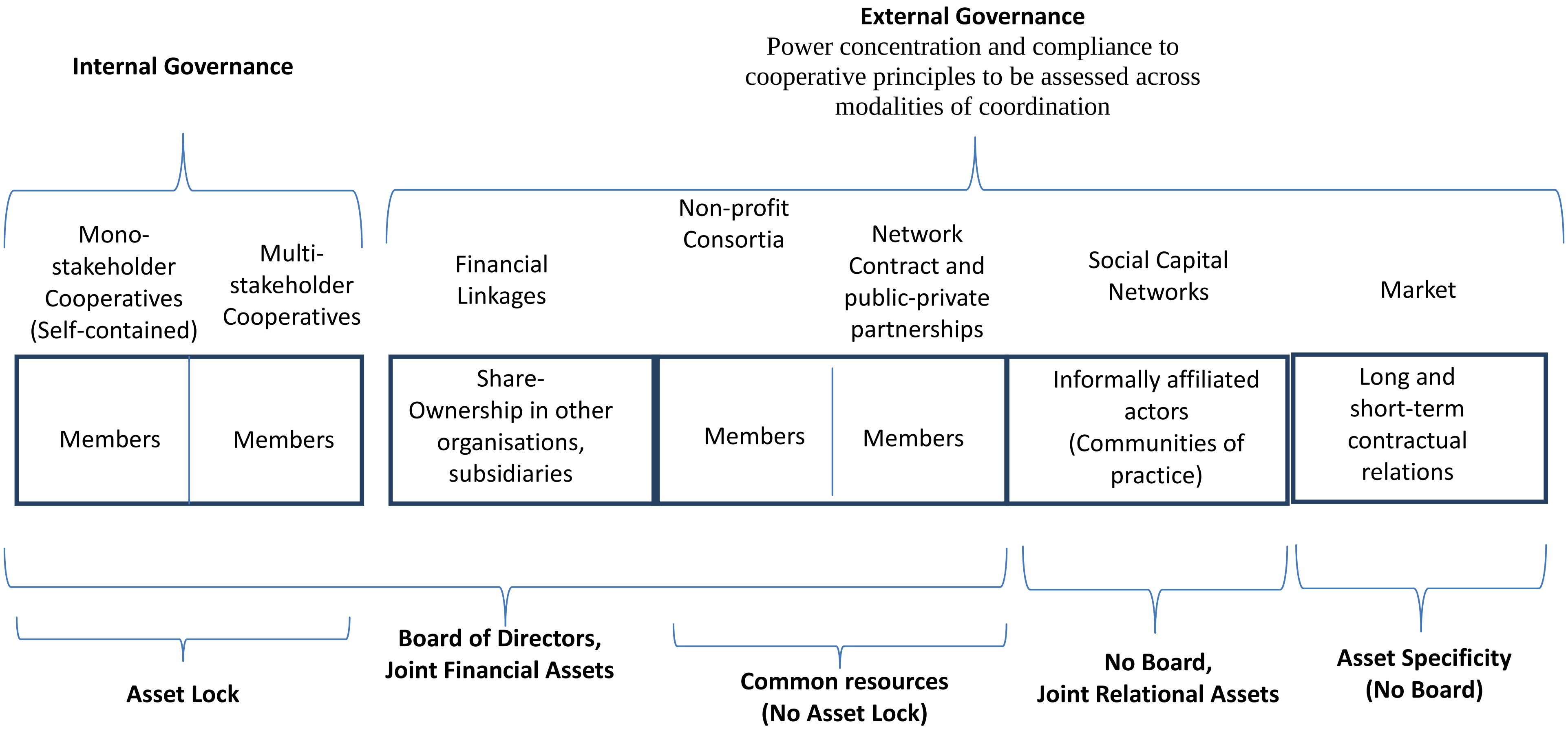
FIGURE 2

External Institutional Levels

LEVEL	COOPVERATIVE NICHE CULTURE	PURPOSE
I. INFORMAL INSTITUTIONS Individual values and believes, culture on the organisation of economic activities	Self-help, self-responsibility, democracy, equality, equity, solidarity, justice, mutual help, social responsibility and caring for others	Fulfilment of needs and desires
II. FORMAL INSTITUTIONS Property rights: who controls and appropriates resources	Cooperatives of cooperatives, consortia, cooperative groups, network contract, short and long-term collaboration contacts	To increase stakeholders' welfare across multiple communities and localities
III. GOVERNANCE STRUCTURE How control is implemented	Contracts promote heterarchical relations	Procedural fairness
IV. RESOURCE ALLOCATION Incentive structure	Mutual benefit; non-exploitative contractual conditions	Distributive fairness Long term sustainability Creation of societal value

FIGURE 3

The governance of cooperatives and their networks



[i] Such understanding is inter-subjective and context dependent. We can expect therefore different interpretations and implementations across localities and organisations, more or less in line with the seven ICA principles. A more general stakeholder perspective would allow a tailored application of our framework and further specifications regarding the nature of coordination and value consistency. For example, within producer cooperatives issues of worker welfare may be disregarded by a more standard focus on member welfare.

[ii] We use niche-culture rather than the more widespread term of sub-culture because the latter creates a hierarchy amongst values which fails to recognise equal dignity to different expressions of values.

[iii] The points of contact between new-institutionalism and ICA's approach are only in some respects straightforward. For example, ICA requires cooperatives to be economically sustainable and independent, finding compatibility with the neo-institutional criterion of cost minimization. However, ICA also requires cooperatives to be democratically run by their members, and this aspect is in contrast with the alleged inefficiency of democratic governance which, for neo-institutionalism, inflates decision-making costs as well as the risk of internal contrasts, the more so when the membership is characterized by heterogeneous preferences (Hansmann, 1996). Similarly, the community-care principle emphasised by the ICA seems to recognise the multiplicity of interests to be taken into account in decision-making processes, in contrast with what neo-institutionalist arguments would support.

[iv] Given their non-profit nature, external financiers have limited incentives to invest and to organise production in cooperatives, both because private returns on investment on specific assets are lower than in for-profit firms, and because – in terms of conventional economic approaches to property rights – cooperative control rights increase the risks of losses and of morally hazardous behaviours.

[v] Almost all social cooperatives work in the social service sector. At the end of 2008 13,938 active social cooperatives employing 317,399 workers were recorded in Italy. In 2011 the turnover of social cooperatives overcame 7 billion of Euro.

[vi] This is a new contract introduced in the Italian Civil Code by the 2003 reform of Corporate Law.

[vii] Amongst others, an interesting example of its application by cooperatives is the Conesco cooperation network, a permanent collaborative network amongst energy service companies that develop renewable energy in Southern Italy (Cf. Roelants et al., 2012).

[viii] One year later the number of such contracts grew to 707.

[ix] Total employment in the Mondragon Cooperative Corporation decreased to 80,321 in 2012 from 83,568 in 2011 due to the crisis of the economy and of the sovereign debt in Spain. To date, lay-offs have exclusively hit short term and other non-member employees, while all worker members are reported to have reserved their jobs.

[x] From the corporate website: "All our companies abroad are organised as Limited Companies. There are several reasons for this: most of the countries do not have the appropriate legislation of a cooperative nature that we have here; in many cases we incorporate these companies as a joint-venture with other partners and, thirdly ... the setting-up of cooperatives requires cooperative members who are used to working within a cooperative culture, and this is a process that takes time." www.mondragon-corporation.com/language/en-US/ENG/Frequently-askedquestions/Business-Strategy.aspx (accessed 23 October 2012).