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MAKING SENSE OF CO-OPERATIVE GOVERNANCE: COMPETING MODELS AND TENSIONS

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Introduction

This paper focuses on how co-operatives and mutual associations are governed. At the heart of these arrangements is an organisation's governing body or board. Paralleling developments in the private sector, the quality of governance of co-operatives has been questioned. Serious concerns have been raised both about the democratic legitimacy of boards and their effectiveness, for example the ability of lay board members to effectively supervise senior managers, ensure probity and protect the interests of members and other relevant stakeholdersⁱ.

These concerns have led to renewed professional and academic interest in organisational governance and a growing body of literature and advice. Much of this literature is prescriptive in nature and aimed at addressing the perceived shortcomings of governing bodies. However, it has been criticised for oversimplifying the problems, underestimating the conflicting demands and pressures that board members face, and presenting solutions that are difficult to implement in practice. These shortcomings point to the need for a greater understanding of the way boards work that is grounded in studies of board behaviour. This paper attempts to address this problem by presenting a new framework for understanding the governance of co-operatives in terms of multiple theoretical perspectives and a number of key paradoxes or tensions that boards face. The paper addresses two related problems.

First, the governance of co-operatives and mutuals is relatively under theorised. In contrast a variety of competing theories have been proposed to try to understand the role of boards in the private sector. The paper briefly reviews each of these theories and discusses how they can be usefully extended to throw light on the boards of co-operatives.

However, this raises a second related problem. Taken individually the different theories are rather one dimensional, only illuminating a particular aspect of the board's role. This has led to calls for a new framework that can help integrate the insights of these different perspectivesⁱⁱ. The paper argues that rather than choose between these different theories we need to find a way of drawing on the different insights they offer. It argues that, taken together, these theories are helpful in highlighting some of the important tensions and paradoxes that boards face, and which they must find ways of managing if they are to be successful. Based on this framework the paper outlines some of these key tensions:

- The tension between board members acting as *representatives* for particular stakeholder groups and '*experts*' charged with driving the performance of the organization forward.

- The tension between the board roles of driving organizational *performance* and ensuring *conformance* i.e. that the organisation behaves in an accountable and prudent manner.
- The tension between boards having to both *control* and *support* management.
- The tensions and conflicts that stem from accountabilities to multiple stakeholders.

Competing perspectives on boards

A variety of competing theories have been proposed to try to understand the role of boards in the private sector. Each implies a different model of how boards work and who should serve on them. Below each of these theoretical perspectives and associated models is briefly examined and how they can be usefully extended to throw light on the role of co-operative boards. However, we begin by looking at the democratic perspective on boards, which provides the dominant model on the role and practices of boards in co-operatives and mutual associations.

A democratic or association perspective – a democratic model

Democratic ideas and practices have been central to thinking about the governance of co-operatives and mutual associations. Democratic government is a central institution in Western societies. Key ideas and practices include: open elections on the basis of one person one vote; pluralism i.e. that representatives will represent different interests; accountability to the electorate; the separation of elected members, who make policy, from the executive, who implement policy decisions. Many of these ideas are embodied in principles underlying the governance of co-operatives.

A democratic perspective on governance suggests that the job of the board is to represent the interests of the co-operative's members. The role of board is to resolve or choose between the interests of different groups and set the overall policy of the organisation, which can then be implemented by staff. Central to this view is the idea of a lay or non-professional board, where any member can put himself or herself forward for election as a board member. Expertise is not a central requirement, as it is in the partnership model of the board we shall discuss below.

Agency theory – a compliance model

Agency theory has been the dominant theory of the corporation and corporate governance arrangements in the private sectorⁱⁱⁱ. It assumes that the owners of an enterprise and those that manage it (their agents) will have different interests. Hence the owners or shareholders of any enterprise face a problem that managers are likely to act in their own interests rather than to their benefit. While free markets are seen as the best restraint on managerial discretion, agency theory sees corporate governance arrangements as another means to ensure that management acts in the best interests of shareholders. This suggests that a majority of board members should be independent of management, and that their primary role is one of ensuring *managerial compliance* – i.e. to monitor and if necessary control the behaviour of management to ensure it acts in the shareholders best interests. This model can be quite easily extended to co-

operatives and suggests similarly that the main role of the board is to ensure managers act in the interests of the co-operative's members.

Stewardship theory – a partnership model

Stewardship theory is grounded in a human relations perspective and starts from opposite assumptions to agency theory^{iv}. It assumes that managers want to do a good job and will act as effective stewards of an organisation's resources. As a result senior management and the 'owners' of the organisation are better seen as *partners*. Hence, the main function of the board is not to ensure managerial compliance or conformance, but to work with management to improve organisational performance. The role of the board is primarily strategic, to add value to top decisions. In this context it is not surprising that management ideas and practices should be applied to governance. From this perspective board members should be selected on the basis of their expertise and contacts so that they are in a position to add value to the organisation's decisions; boards and managers should receive proper induction and training; they should know how to operate effectively as a team etc. Ideas such as these are common in much of the 'how-to-do-it' literature on boards. For co-operatives this raises the question how can boards have the necessary expertise when their members are elected?

Resource dependency theory – a co-optation model

Resource dependency theory views organisations as interdependent with their environment^v. Organisations depend crucially for their survival on other organisations and actors for resources. As a result they need to find ways of managing this dependence and ensuring they get the resources and information they need. From this perspective the board is seen as one means of reducing uncertainty by creating influential links between organisations through for example interlocking directorates. The main functions of the board are to maintain good relations with key external stakeholders in order to ensure the flow of resources into and from the organisation, and to help the organisation respond to external change. Board members are selected for the important external links and knowledge they can bring to the organisation, and to try to *co-opt* potential external threats. Again this raises an issue for co-operatives when board members are elected.

Stakeholder theory – a stakeholder model

Stakeholder theory is based on the premise that organisations should be responsible to a range of groups (or stakeholders) in society other than just an organisation's owners, or in the case of a co-operative its members^{vi}. By incorporating different stakeholders on boards it is expected that organisations will be more likely to respond to broader social interests than the narrow interests of one group. This leads to a political role for boards negotiating and resolving the potentially conflicting interests of different stakeholder groups in order to determine the objectives of the organisation and set policy. For co-operatives this raises the question how should the interests of other important stakeholders besides members be represented.

Managerial hegemony theory – a ‘rubber stamp’ model

Managerial hegemony theory relates to the thesis that although shareholders may legally own and control large corporations they no longer effectively control them. Control having been effectively ceded to a new professional managerial class. From this perspective the board ends up as little more than a ‘rubber stamp’ for management’s decisions. Its function is essentially symbolic - to legitimise management’s actions. Although this theory was developed in the study of large business corporations, many of the processes it describes seem just as relevant to co-operatives: for example the separation of a co-operative’s members from those that manage it, and the increasing growth and professionalisation of management. This raises the question for all organisations including co-operatives what can be done to ensure boards are able to exercise real power and influence when required.

The paradoxes and tensions boards face

Taken individually these different theories are rather one dimensional, and can be criticised for only illuminating a particular aspect of the board’s work. This has led to calls for a new conceptual framework that can help integrate the insights of these different perspectives. A paradox perspective offers a promising approach to providing this new conceptual framework. Taken together these multiple theoretical perspectives are helpful in highlighting some of the important paradoxes and tensions that boards face.

Who governs -the tension between ‘lay’ and professional boards

The different models have different implications for who should serve on boards. The opposition is clearest between the partnership and democratic models. The partnership model stresses that board members should have expertise and experience that can add value to the performance of the organisation. The implication is that board members should be selected for their professional expertise and skills. In contrast the democratic model on which co-operatives are based stresses that board members are lay representatives there to serve members they represent. Other models suggest board members should be selected because of their contacts and experience or because they represent stakeholder interests.

Co-operatives need to consider how they can best manage these tensions. How can the expertise, experience or contacts of boards be increased without undermining democratic principles? A variety of options are available. For example, can more be done to encourage members with relevant expertise and experience to stand for election? Are there procedures to induct and develop new board members? Is training available for board members? Can co-options be used to bring missing skills, experience or contacts onto the board? Can other consultative forums be developed to make sure that other stakeholders’ views are considered?

Board roles - the tension between the conformance and performance

The different theories of governance put different emphasis on what are the main roles of the board. This is most apparent in the opposition between the agency and stewardship perspectives. What Garratt has called the ‘conformance’ versus ‘performance’ role of boards^{vii}. The compliance model emphasises the conformance role of the board to ensure that the organisation acts in the interests of its ‘owners’ and to be a careful steward of their resources. In contrast the partnership model emphasises the role of the board in driving forward organisational performance through adding value to the organisation’s strategy and top decisions.

Combining these roles can create difficult tensions for boards, as they demand very different kinds of attitudes and behaviour from board members. The conformance role demands careful monitoring and scrutiny of the organisation’s past performance and is risk averse. The performance role demands forward vision, an understanding of the organisation and its environment and perhaps a greater willingness to take risks. Strategies for dealing with this tension include separating out different aspects of the board role over time through an annual cycle of meeting, the careful management of board agendas and skilful chairing of meetings. In particular it is often wise for boards to set aside periodic meetings free from routine items of business to focus on longer term strategic issues with management.

Relationships with management - the tension between controlling and partnering

The agency and democratic perspectives stress the importance of the board monitoring and controlling the work of managers (the executive). In contrast stewardship theory stresses the role of the board as a partner to management, improving top management decision-making. The need to both control senior management and be their support and partner in decision making can be a source of role conflict and tension for board members. One way board members sometimes find it useful to think about their role is as a ‘critical friend’ to management.

Another related tension facing boards and management concerns the lack of a clear boundary between their respective roles. The complex and interdependent nature of management and board roles offers plenty of scope for different interpretations of the relationship and conflict. Boards are frequently accused of meddling in the organisation’s work or not being involved enough. An important means of helping to establish a productive working relationship with management is through regular discussion and negotiation over respective roles and responsibilities.

Multiple or ambiguous accountability

There may be tension concerning to whom board members are accountable. Formally co-operatives are accountable to their members. However, a stakeholder perspective suggests that there are likely to be other stakeholders who have a legitimate interest in what the organisation does, and should in some way be able to hold it to account. Board members may experience tension because they feel accountable to more than one group, or because they are unclear or differ over who they feel they are accountable to. An important exercise for any board and management team is to periodically review who it feels its main stakeholders are, and how their views are taken into account.

Conclusions

The paper has shown how existing theories of corporate governance can be extended to help understand the governance of co-operatives, but that by themselves each is too one-dimensional only highlighting particular aspects of the board's role. The paper argues that it is better to draw on the insights that each model offers rather than choose between them. As empirical research suggests governance is an inherently difficult and problematic activity. Taken together the different models highlight the important tensions and paradoxes boards face, which successful boards will need to learn how to manage.

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ⁱ See Review of International Co-operation, 89, 4, 1996, which examined corporate governance and control in co-operatives.

ⁱⁱ See Hung, H. (1998) 'A typology or theories of the roles of governing boards', *Corporate Governance*, 6, 2, 101-111, and Tricker, B. (2000) 'Editorial - Corporate Governance - the subject whose time has come', *Corporate Governance*, 8, 4, 289-296.

ⁱⁱⁱ Keasey, K., Thompson, S. and Wright, M. (1997) 'The Corporate Governance Problem - Competing Diagnoses and Solutions', in *Corporate Governance: Economic and Financial Issues*, Oxford: Oxford University Press

^{iv} Muth, M. M. and Donaldson, L. (1998) 'Stewardship Theory and Board Structure: a contingency approach', *Corporate Governance*, 6, 1, 5-28

^v Pfeffer, J. & Salancik, G. R. (1978) *The External Control of Organizations: a Resource Dependence Perspective*, New York: Harper & Row.

^{vi} Hutton, W. (1997) Stakeholding and its Critics, Choice in Welfare No.36, The Institute of Economic Affairs

^{vii} Garratt, B. (1996) *'The Fish Rots from the Head – the Crisis in our Boardrooms: Developing the Crucial Skills of the Competent Director'*, London: Harper Collins Pubs.