Unique Expectations of Co-operative Boards: taking on the challenges of the democratic enterprise

Arthur Sherwood and Keith Taylor

Abstract

The expectations for governing boards of co-operative enterprises continue to evolve and adapt in synch with various political crises seen across the globe. Take for example the banking crisis of 2008. Financial co-operatives were seen as a viable antidote to the excesses of the investor-owned financial institutions. But the economic crisis was so deep that it revealed a number of governance challenges embedded in robust co-operative sectors in Spain and the U.K.

Using the lens of the institutional logics perspective, we address the common and unique expectations of co-operative vs. investor owned corporate boards of directors. Building on prior governance literature, we discuss tensions created between various perspectives and identify and succinctly describe three common expectations including teaming, vigilance and strategic behaviors. Then, we take a deeper look at the unique co-operative expectation of being advocates for democracy and the challenges this poses including being played for suckers, tyranny of the majority (and minority), democratic despotism and pragmatism. We close with an exploration of co-operative democracy in practice and highlight resulting questions of interest to researchers and practitioners.

Keywords

Co-operative Boards, Co-operative Democracy, Co-operative Governance

Introduction

The world has experienced serious economic, social and political disruptions in the last decade. The ICA's Blueprint for a Co-operative decade states,

> *"in the second half of 2012, following five years of financial turbulence the more developed economies of the world remain in a state of crisis from which there is still no apparent exit, and the developing economies are being impeded in their pursuit of the Millennium Development Goals. In many nations, governments are in retreat, cutting their social and public spending, leaving citizens even more vulnerable to economic turmoil. In others, inequality continues to increase as economic power is shifting dramatically with consequential social impacts." (ICA, 2013, p2)*

The authors go on to say,

> *"In the midst of this uncertainty and suffering, co-operatives can provide some hope and clarity of direction for citizens around the world. Uniquely amongst models of enterprise, co-operatives bring economic resources under democratic control. The co-operative model is a commercially efficient and effective way of doing business that takes account of a wider range of human needs, of time horizons and of values in decision making." (ibid)*

In this "co-operative decade" the stated aim is to bring co-ops to the forefront as the acknowledged leader in economic, social and environmental sustainability, the institutional model preferred by people, growing faster than other forms of economic enterprise.

But, can democratically owned businesses actually make these differences? Are the elected governors just window dressing on what is really just another conventional business? These questions then beg a third: can democratically owned and controlled businesses really simultaneously deliver on the promise of enterprise performance and a robust and thriving democracy when the practice of democracy poses so many challenges, and faces persistent pressure and tension from the tradition of return on capital as the dominant priority in market-based enterprises?

Boards of co-operative organizations have a variety of expectations placed upon them that are unique to the co-op model. Cornforth identifies the tension between the management, board, and their democratic obligations to member-owners (2004); Spear, Cornforth and Aiken, (2009) point out the unique skills needed for competent governance; Birchall (2014) distinguishes the necessary governance differentials and adjustments needed between co-operatives of differing scales.

The logic of the institution will guide analysis about which of these tensions are in effect and how they should be managed. Our first contribution builds on this evolving discussion of tensions and challenges through a lens new to the literature on co-operative governance. We take a look at boards from an institutional logics perspective (Thornton, Ocasio and Lounsbury, 2012) in order to identify potentially paradoxical behavioral expectations held of these agents. We also draw from the broader governance literature to identify overlapping behavioral expectations of investor-owned corporation (IOC) and co-operative-owned corporation (COC) governors including teaming, vigilance, strategy and being advocates for democracy. We argue that the institutional logics of both IOC and COC indicate the first three are common expectations (although likely to have different flavors of implementation) while being advocates for democracy is unique to co-operatives.

These four expectations become the pillars that lead to a board's success, but the tensions created by the resulting paradoxes must be managed. Identifying the logics and related behavioral expectations is important as it takes our understanding one step closer to helping co-operative practitioners address the challenges and tensions arising from them.

Our second contribution is to address the challenges of democracy and the dangers the democratically controlled enterprise faces. Spear (2004) highlights that much of what a co-operative was designed to do has the potential to degenerate into what is essentially a managerially entrenched and powerfully controlled enterprise due to limited controls either from the market or the ownership. He states:

> *"This weakness in turn weakens the original market advantage of such enterprises in trust and collective goods, by reducing trust and reducing the incentives and controls for good performance. In the worst case the result is sleepy managers, cozy board relations and poorly performing social enterprises that eat into its asset base, often accumulated over generations, until it is taken over or fails, as markets become more competitive." (Spear, 2004, p.49)*

This is a concerning insight. The implication is that there is an expectation for boards to be effective in their democratic control, and if they are not, the results can be catastrophic. There is a point at which co-operatives may move toward isomorphic tendencies, standardizing into what looks like an IOC which in turn conceptualizes members instrumentally as mere consumers, producers or laborers, with governance becoming dominated by financial – not democratic-concerns (Malo and Vezina, 2004). This then leads to the downward spiral of diminishing market advantages (Spear 2004).

We will dig deeper into the potential vulnerabilities of democracies drawing from the work of Vincent Ostrom (1997). We will then argue that boards are critical to providing the countervailing measures called for by Spear (2004) including opportunities for protecting, perpetuating and practicing democracy.

Review of three seminal co-operative governance papers

Past research has examined governance challenges and tensions from a variety of perspectives and approaches. While we do not provide an exhaustive review of this literature below, the three pieces we highlight lay a foundation for understanding the challenges and tensions co-operative boards face.

Cornforth (2004) reviewed a variety of theoretical perspectives that highlighted this tension including agency, stewardship, democratic, stakeholder, resource dependency and managerial hegemony theories. The author argued that a paradox perspective was needed in order to deal with these tensions, as using just one theoretical lens was too one-dimensional. In other words, we do not look at one facet, but a number of facets when identifying the various challenges facing a co-operative. The tensions identified included the question of who governs (representative vs. expert boards), the question of board roles (conformance vs. performance) and the question of relationships with management (controlling vs. supporting).

Spear, Cornforth and Aiken (2009) studied social enterprises in the UK identifying a variety of common challenges including: recruiting board members with the right skills and expertise, choosing appropriate legal and governance structures, managing the diversity of external stakeholder interests, managing membership, the power of boards to control management, managing the interdependencies between board and management and balancing social and financial goals. These challenges reveal multiple tensions including balancing stakeholder interests, organizational outcome expectations and how to be both supportive and controlling of management.

Finally, Birchall (2014) recently presented findings in a report for Co-operatives UK examining the governance of large consumer co-operatives. Two challenges noted by the author include ensuring expertise on the board and managing the cost of a participatory model of governance. He goes on to indicate that successful governance is all about effective distribution of various forms of authority. Again, it becomes apparent that these challenges create tensions. How can co-operatives develop the expertise to make decisions on behalf of their members and invest in a participatory model while keeping the financial and non-financial costs from going off the rails? How to have distributed authority that does not undermine successful board-management relations yet allows for appropriate control on behalf of members? Birchall states:

> *"In designing governance structures, we struggle to give some weight to each of four different types of authority: voice, representation, expertise and management. We have to listen to the voice of the members, to find an effective way of representing them, to find the expert help they need, and to find ways of encouraging and controlling managers. Only when all four types of authority are present can a co-operative be governed effectively" (Birchall, 2014 p22)*

Clearly getting these tensions balanced is a challenge to co-operative boards.

The challenges of being a co-operative enterprise

But why are these challenges? Why do these tensions exist at all? We argue that the tensions arise from two arenas: 1) the institutional logic of the co-operative enterprise and 2) the nature of the agency relationship. Approaching this from the institutional logics perspective allows us to explore behavioral expectations that develop for directors as agents in order to follow the logic of the organizational type.

The democratic governance expectation is particularly interesting because of unique importance placed upon it by co-operatives (democratic governance is a mandatory feature). This characteristic, while challenging, can also be the source of market advantage. Birchall (2012) discusses the comparative advantages of member-owned organizations derived from ownership, control and benefits. The set of 'comparative advantages' is directly derived from the nature of the member-owned business. In order to avoid degeneration of this co-operative advantage (due to the dangers noted earlier by Spear 2004), it is critical for boards to meet their behavioral expectations related to democracy.

We will go deeper into the democracy expectations and bring in the perspectives of noted political scientist, Vincent Ostrom. Linking to Ostrom's work (Ostrom, 1997) allows us to further understand the vulnerabilities of democratic representation and voice and the expectations that may arise for boards in order to counteract and/or avoid these vulnerabilities. We've structured our contribution into three components. First, we will frame the expectations of governing boards as agents informed by institutional logics. Although we look at both IOC and COC directors through a narrow - agency - lens, we seek to make the case that ideal type co-operative and investor owned corporations have different institutional logics that lead to particular expectations of board directors.

Second, we will identify the common expectations of co-operatively-owned and investor-owned corporations and briefly describe each including teaming, vigilance and strategic behaviors. Third, we take a deeper look at the unique expectations of co-operative boards to act as advocates of democracy, noting the special challenges this expectation poses to directors in structuring democracy as an asset rather than a liability.

We will use co-operatively owned corporations (COC) and investor owned corporations (IOC) for our discussion. When formed as a corporation, the two different ownership types typically will have boards of directors, separate legal existence, limited liability for owners and continuity of existence (i.e. existence that continues regardless of specific owners). The key point of departure lies in the breadth of stakeholder needs, with COC's typically having a more diverse set than IOC's (Spear et al, 2009). It is commonly understood that the primary interest of IOC shareholders is the maximization of wealth, whereas the primary interests of COC member-owners are diverse and subject to a one-member, one-vote democratic process. This understanding allows us to focus on the resulting overlapping and contrasting agent expectations stemming from their institutional logics.

Agency in the Institutional Logics of Co-operative vs. Investor Owned Corporations

Boards sit at an interesting place in the set of agency relationships of both COCs and IOCs that link to many of the aforementioned tensions. They are delegated an enormous amount of authority from owners while at the same time delegating nearly all this authority to management, often through a general manager such as a CEO. Making this even more interesting (and challenging) is that the number of owners is often high resulting in the inability to directly hear or represent all voices equally. Board directors are tasked to process the numerous voices and transmit interpretations of those desires within a complex organizational structure, while controlling for a dynamic market environment.

This raises interesting questions about what might be the appropriate base assumptions of boards regarding their work expectations, and what the situations might be that influence or determine them. What might determine the base assumptions for COCs and IOCs and how might this impact directors' perceptions?

One perspective that is useful in exploring these questions is that of *institutional logics.*
The institutional logics perspective is a:

> *"Meta theoretical framework for analyzing the interrelationships among institutions, individuals, and organizations in social systems" (Thornton et al, 2012, p2)*

More specifically, institutional logic is defined as:

> *"the socially constructed, historical patterns of cultural symbols and material practices, including assumptions, values, and beliefs, by which individuals and organizations provide meaning to their daily activity, organize time and space, and reproduce their lives and experiences"(ibid).*

Theory related to agency often assumes bounded rationality (e.g. Eisenhardt, 1989). Because agent-actors can't know everything, they must rely on something to make decisions and act on behalf of their principals. Institutional logics can fulfill at least some of this role, ultimately impacting the perception of behavioral expectations placed upon agents through an understanding of key components in the above definition: historical patterns, cultural symbols, material practices, assumptions, values and beliefs of their organization. These expectations, laid upon and perceived by the governors will ultimately impact the governance systems/models employed by them. Furthermore, the logical orientation of an institution may impact the types of agents –and their concurrent motivations - which seek to participate in the governance systems of the firm.

If we assume that the specific logic of the institution influences actual and perceived expectations, we can assume that it both constrains and enables the actors in their level of agency, or ability to act. Agency is defined as an actor's ability to have some effect on the social world---such as altering the rules, relational ties or distribution of resources (Scott, 2008). Institutional logic argues that "agency, and the knowledge that makes agency possible, will vary by institutional order" and that "each institutional order has its own sense of rationality" (Thornton et al., 2012:pg. 4 and pg. 7). Thus, from an institutional logics perspective, we can anticipate that expectations placed upon and perceived by boards of differing institutional orders will also vary (as in this case, the logical differentiation between a COC and IOC).

Both COCs and IOCs must be profitable businesses in order to sustain themselves. They both have owners that invest equity, boards that act as agents of the owners and an enterprise. Thus, each has business, owners, and capital as part of their logic. At this point we can start to detect the departure of the two business models. Ownership in IOCs may be divided unevenly, with one shareholder able to hold multiple shares. The amount of shares determines the portion of the profit each owner may receive in dividends and the number of votes they have in electing the board of directors. This in turn leads to a widely held understanding that the primary value upon which the corporation should focus is maximization of shareholder wealth. IOCs are shareholder wealth *building mechanisms* and this is central to their institutional logic.

In contrast, ownership in COCs is evenly distributed with each owner having a single share. Each owner has one vote in the election of the board of directors. Rather than profits being distributed based on how many shares an owner has, it is distributed based upon patronage, or the value of economic transactions with the COC. This difference arose as a consequence of COCs being formed to meet the needs of their owners (Malo and Vezina, 2004; the scope of these needs may very well be wealth related but can start or evolve to be quite broad and diversified) and on the basis of democratic control by owners of the business. The widely held understanding is that COC's place primary value on meeting shareholder needs. COCs are needs meeting mechanisms and this is central to their institutional logic.

Maximizing shareholder wealth vs. satisfying owner needs as primary values likely impacts the institutional logics of IOCs and COCs, and in turn, the expectations held of directors' behavior for each rests on set of values that is quite different. Particularly interesting is the broader scope that COCs have in owner needs beyond creating monetary wealth for owners-members.

Many COCs around the world have embraced a set of broadly held values that are guided by a universal set of "Co-operative Principles." (ICA 1995). These principles and values are identified in Table 1.

Table 1:
CO-OPERATIVE PRINCIPLES AND VALUES

Seven Co-operative Principles	Co-operative Values
1. Voluntary and Open Membership* 2. Democratic Member Control 3. Member Economic Participation 4. Autonomy and Independence 5. Education, Training and Information 6. Cooperation among Co-operatives 7. Concern for Community *Membership assumes ownership in co-operatives, but it has a wider scope in democratic voice and patronage benefits.	• Self Help • Self-responsibility • Democracy • Equality • Equity • Solidarity • Honesty • Openness • Social Responsibility • Caring for others

It is interesting to note that only one of these addresses economic participation, and that the only one specifically articulated in both principles and values is that of democracy. The principles and values that sit aside economics should broaden the scope of the logic of this institutional type well beyond that of the IOC.

From this point forward, we assume that there are certain overlapping and distinguishing aspects of institutional logics that will lead to overlapping differentiated behavioral expectations held of, and perceived by, boards of directors.

Review of the literature on Directors' Behavioral Expectations

Multiple scholars, both from the traditional corporate and the co-operative arenas have identified contrasting perspectives on the role of boards (e.g. Cornforth, 2002; Finkelstein, Hambrick and Cannella, 2009). From this, the question arises as to what an agent is to do for the owners of the business and the impact they can ultimately have on the organization. Finkelstein et al (2007) indicate the key question to be "How do boards affect organizational choices, strategies and performance?" (229). This implies that directors are affecting those choices through their governing behaviors derived from their personal filters (mental models) of what they should do as governors.

McGinnis defines governance as:

> *"the process by which the repertoire of rules, norms, and strategies that guide behavior within a given realm of policy interactions are formed, applied, interpreted and reformed" (McGinnis, 2012, pg. 6).*

While there may be multiple levels of governance including that of operations in an institution, our focus here is that of the board of directors and their expected behaviors in the process defined by McGinnis.

COCs and IOCs have elected boards with certain common expectations of their governance duties as they act out their agency role. But as discussed in the previous section, there is a difference in who has the elector power and in the institutional logic each starts with, which then begins to separate and distinguish COCs from IOCs.

Figure 1 below illustrates a model of four board behavioral expectations that find their roots in the paradoxical theoretical perspectives. Each of the component expectations are labeled as behaviors. Because board governance is at least in part an act of agency, there are expectations that boards "do" something on behalf of those electing them to their positions.

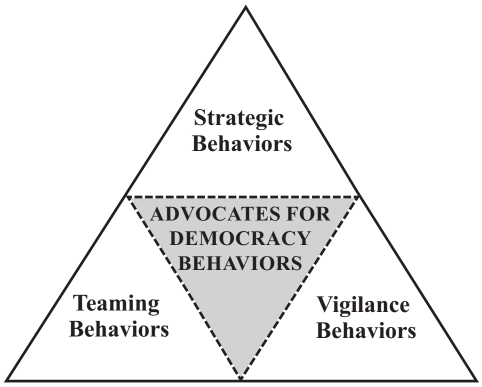

Figure 1: Components of Board Governance Expectations

The core expectation components of the framework are teaming, vigilance, strategic, and advocates for democracy behaviors. Democracy behaviors are in grey as these are considered to be the unique set of expectations of COC vs. IOC and may very well sit at the heart of the co-operative enterprise's comparative advantage. The next three sections define and describe each behavioral expectation component. We will treat teaming, vigilance and strategic behaviors succinctly and delve deeper into the unique challenges of being advocates for democracy for co-op boards.

Expectations of Board Teaming Behaviors

A team is "a specific type of group composed of members who are interdependent, who share common goals, and who must coordinate their activities to accomplish these goals" (Kogler Hill, 2013, p287). According to Finkelstein et al (2009) almost all theoretical framings related to boards identify two such common goals or roles that they work toward fulfilling on behalf of their owners. First, boards of directors have the common purpose of playing a role of linking the organization to its external environment. Second, they play an internal role related to control and administration. Each of the subsequent components of board governance expectations (vigilance, strategic, democracy) relate to one or both of these roles.

This of course can create tensions for boards as they try to understand if each director is a representative (e.g. democratic perspective) or to control vs. collaborate with management (e.g. agency vs. stewardship theory).The logic of either corporation type will establish that boards are expected to come together to accomplish a set of internal and external common purposes, although what this looks like and the degree to which the group is cohesive will surely vary.

Expectations of Vigilance Behaviors

Vigilance appears to have strong support as an expectation and the greatest overlap in expectations between co-operative and other forms of business. Vigilance behaviors can be considered acts of intentionally paying close and continuous attention to avoid risk.

Vigilance behaviors are observable as boards play their internally focused "role in administration and internal control, putatively (and legally) responsible for setting policy and monitoring management" (Finkelstein et al., 2009: p228) thus having a role focused on conformance (Cornforth, 2004).

Fama and Jensen (1983) point out that boards play the role of ratifying and monitoring top management decisions and that they are central in ensuring that shareholder best interests are served by management actions. The authors point out that this is the case for various types of organizations from corporations to financial mutual to not-for profits, akin to fiduciary responsibility (Joyal and Swansen 2011).

The key insight from the above is that board vigilance behaviors are expected from all types of board governed organizations. Not only are they expected by virtue of their logics, they are legally mandated to do so. Of course, which behaviors and how well these are carried out will vary from organization to organization resulting more or less effectiveness and more or less impact on an organization's ultimate performance as it relates to meeting shareholder/stakeholder/owner interests. Perhaps the words of Fama and Jensen (1983) summarize this well:

> *"Such boards always have the power to hire, fire, and compensate the top-level decision manager's and to ratify and monitor important decisions."(Fama and Jensen, 1983, p 311).*

Being highly vigilant can create tensions with both teaming and being part of the strategic process. Asking the difficult questions can place strains on the group (both in the board and with management) as well as be seen as obstructive to moving forward with strategy.

Expectations of Strategic Behaviors

Strategic behaviors are those acts that are part of the strategic process of the organization. Stewardship theory indicates that the board's role is to help improve performance and add value and support to management (Cornforth, 2004; Donaldson, 1990). Thus far, agency theorists have focused most of their attention on the monitoring role of boards and less on strategy and its formulation (Finkelstein et al., 2007).

While this may be the case, there has been growing pressure over time toward a higher level of board expectations, from the implementation of Sarbanes-Oxley act in the US to director liability issues, to directors wanting to play a primary role in advising and evaluating (Lorsch and Maclver, 1989). Yet, the literature also indicates that there are powerful norms not to question management, and penalties for boards and directors that do so (Westphal and Khanna, 2003).

Tensions are created as boards work to determine how to balance strategic behaviors with those of vigilance (support vs. control). And it becomes even more challenging for directors of co-operatives as they have unique expectations placed upon them relating to democratic control.

Expectations for Advocates for Democratic Behaviors

To this point, we have briefly overviewed three behavioral expectations that are common to both COCs and IOCs. While each of these has inherent tensions between and within, behavioral expectations of board agents by principals are that they are to be fulfilled to the degree that it is consistent with their understanding of the institutional logic, as well as their own self interest (to paraphrase Tocqueville, "rightly understood").

The expectation of acting as democracy advocates is the point of COC distinction. The reasoning for this is quite simple; IOCs are not designed to be democracies and COCs hold democracy as core to their institutional logic and design. Co-operatives as democracies have long been the subject of scholarly attention (for example see Bernstein, 1976; Cornforth, 1995) with recent attention brought to how their unique nature brings comparative advantage to the enterprise (Birchall, 2012).

A long standing question is, what does it mean to be a co-operative democracy and how would impact upon owner expectations of the board? Isn't it basically about holding an election with each member-owner getting a vote, and check, democracy work is complete? To further address these questions, we turn to the writing of democracy scholar, Vincent Ostrom. Our intention from here forward it to use his thinking to go deeper into the challenges of democracy in general, and in co-operatives in particular, with the implications for boards as they fulfill yet another expectation, and act as advocates for democracy. This in turn helps take the countervailing steps called for by Spear (2004) and protects what may be the comparative advantage of COCs.

In addressing the reasons for crises of democracies around the world, Ostrom (1997) considers:

> *"Perhaps the answer is to be found in the superficial way we think about citizenship in our democratic societies. How people conduct themselves as they directly relate to one another in the ordinary exigencies of life is much more fundamental to a democratic way of life than the principle of 'one person, one vote, majority rule. Person-to-person, citizen-to-citizen relationships are what life in democratic societies is all about. Democratic ways of life turn on self-organizing and self-governing capabilities rather than presuming that something called 'the Government' governs".*
> *(Ostrom, 1997, p3).*

This is worth considering for the society of the co-operative as well. If being a democracy means more than "just one person, one vote, majority rules", then what are the implications of this to the institutional logic of the COC and the subsequent perceived expectations member-owners should have of elected boards?

Starting with the words of Ostrom, we can draw some parallels to COCs. The members make up the citizens of the COC democracy. They elect the board of directors. The board of directors is the elected part of the governing structure and the management is typically the appointed part of the governing structure. But from Ostrom's perspective, this is not what makes a democracy go beyond superficiality. The citizens retain governing power through this election and appointment approach having self-organized and developing, maintaining and utilizing self-governing capabilities. The citizen owners *delegate* authority and power, but do not abdicate authority and power to their agents.

In a robust and resilient COC democracy, member-owners have the capabilities for and are engaged in self-governance through participating in the processes of reflection and choice. Certainly they use agents to act on their behalf, but again the use of agents is an act of delegation to help the system work. Delegates are themselves members of the co-operative. In order to make good decisions on behalf of the majority of member-owners, having member-owners participate in the process of reflection that leads to choices appears critical.

Ostrom states that:

> *"democratic societies are necessarily placed at risk when people conceive of their relationships as being grounded on principles of command and control rather than on principles of self-responsibility in self-governing communities of relationships" (ibid, p4).*

If indeed the co-operative values and principles are taken as guidelines by COC boards, one can begin to see how fundamental this is to the institutional logic of COCs: democratic member control, self-help, self-responsibility, democracy. And to support a vibrant democracy: education, training and information, autonomy and independence, concern for community, caring for others, social responsibility, openness. The majority of the values and principles appear to be directly or indirectly about supporting a robust, self-governing democracy.

To have a robust and resilient democracy, Ostrom argues that it must be about *power with*, rather than power over. But this does not just spontaneously occur nor is it free from vulnerability. Multiple types of vulnerabilities have been identified including being played for suckers, tyranny of the majority, democratic despotism, and pragmatism. As democracies, co-operatives are vulnerable to each, and each presents a challenge to their boards.

Being Played for Suckers

Misaligned interests between principals (owners) and agents (board directors) is a core issue concern with agency theory (Eisenhardt, 1989).

This vulnerability is evident when after an election, whatever voiced alignment with the public evaporates in favor of hidden agendas and actions of winning coalitions (Ostrom, 1997). A COC is vulnerable if those on the board work to be elected based on one premise, with a hidden agenda upon which they base their actions. Owners-members can also be played for suckers if the elected board communicates one thing with the intention of acting in another. This manipulation and lack of candor breaks down trust, alienates members and disillusions them about the COC and how it connects to their values.

Tyranny of the Majority

Tocqueville (1835-40) and Madison (Hamilton, Jay and Madison, 1788) both identified this as a vulnerability via the majority vote mechanism. Ostrom (1997) refers to this vulnerability "as a sickness of government" where the majority decisions benefit the majority but leave the minority needs and interests behind. The vulnerability moves into a full on crisis when the majority restructures the co-op in such a manner that forces an abdication of authority, empowering the board to act on its interests alone.

Democratic Despotism

Tocqueville (1835-40) identified this vulnerability to arise when things are good, and the people are kept happy.

This leads to a sort of benevolent autocracy where, "power is absolute, minute, regular, provident and mild. It would be like the authority of a parent if, like that authority, its object was to prepare men for manhood; but it seeks, on the contrary, to keep them in perpetual childhood: it is well content that the people should rejoice, provided they think of nothing but rejoicing. For their happiness such a government willingly labors, but it chooses to be the sole agent and the sole arbiter of that happiness; it provides for their security, foresees and supplies their necessities, facilitates their pleasure, manages their principal concerns, directs their industry, regulates the descent of property, and subdivides their inheritances: what remains, but to spare them all the care of thinking and all the trouble of living?" (Ostrom, 1997,p 16).

Ostrom identifies this as a "sickness of the people" and states:

> *"Democracies are in serious difficulties when a sickness of the people creates a dependency, a form of servitude, in which the people no longer possess the autonomous capabilities to modify their constitutional arrangement and reform their system of government in appropriate ways" (ibid, p17).*

But can this possibly apply to COCs? Arguably, COC businesses are especially vulnerable as there is considerable attention paid to customer service and member-owner needs. If needs are not met, complaining and working to change the system are expected. But what if people are satisfied for a significant period of time? Why bother to know how to actively participate in the democracy? It is not hard to imagine member-owners saying to themselves *the* board *will do* it and even more so, the *excellent management will take care of us.* Perhaps a member-owner does have a concern but things are generally just fine, right?

This long term member satisfaction may in fact lead to democratic muscle atrophy. And when a need to engage does arise, the skills no longer exist within the membership and even within the board and management. This atrophy can lead to a vicious cycle of a fear of democracy, with actors working to stifle participation of voice, representation and information sharing through indirect action of ignoring member-owners to active stifling through manipulating process (the aforementioned problem of coerced abdication).

Pragmatism

The pragmatic paradigm originates from the presidential administration of Woodrow Wilson (Ostrom, 1997). Participatory mechanisms of governance are perceived as cumbersome, and prone to engagement of sub-optimal agents. Instead, knowledge leaders or experts are elevated to leadership positions, and elite-labeled amateurs are excluded from participatory governance processes. As globalization and business competition intensifies, the deference to pragmatic governance threatens to weaken democracy. Under such a system, the users of crucial public goods are kept from informing elite agents working on their behalf - what Aligica and Boettke (2009) refer to as a public service paradox. The agents then exhibit a cloistered worldview, informed by a shallow knowledge pool of information dissemination. Pragmatic governance opens channels for exploitation in that it obscures participation in reflection and choice by the public (owners) as it may interfere with the "necessary" business at hand and create distractions by introducing the challenges the COC principles and values bring (again, the delegation authority is abdicated).Ostrom (1997) states of Wilson's pragmatic thinking:

> *"Governments could presumably govern in democratic societies without regard for the processes of crafting and re-crafting the common knowledge, shared communities of understanding, patterns of social accountability, and mutual trust necessary for self-governing society (ibid, p 20)".*

Wilson essentially argued that the original intentions –institutional design and structure- and future desired states were not of importance; rather, the pragmatic situation of today is what matters most. The government had grown up and those original values were nice, but not practical. Clearly, this is an argument that professional management of COCs may be tempted to make and thus move closer toward what Spear (2004) cautioned against. They might argue democracy is hard and messy and dealing with all those members reduces our agility in the marketplace and our capacity to respond to competitive pressures. And these things are likely true; this is why pragmatic governance is such a dangerous vulnerability of COC democracies. Practical business needs as identified by professional management can potentially trump all else. The COC loses its value edge, and ultimately its comparative advantage.

Each of these vulnerabilities is real, and unfortunately, they are often not well understood by members of COC democracies. Avoiding becoming victim to these vulnerabilities implies both defensive and proactive behaviors. Thus boards must become the champions of democracy, and have the consequent expectation to be *advocates for democracy.*

Avoiding Vulnerabilities, Strengthening "Self Governing" Democracy

What might these advocacy behaviors be? Here, we do not propose any grand scheme, but instead choose to highlight some examples, with the intent that this will lead into a body of research on best practices for individuals in board governance positions.

Board governors (directors) must be explicitly aware of their responsibilities as advocates of democracy; at the same time, they must also build a self-regulating system that keeps them in check as well. Simply put, the membership body has delegated certain responsibilities and rights to the elected members who serve on the board of directors; at no time should this be perceived as the membership at large partaking in a wholesale abdication of their fundamental constitutive rights over the co-op.

Practice Democracy

Co-ops are common resource regimes, meaning they are owned collectively, with major decision-making authority being vested in the best interest of the collective. Any democratically governed institution requires optimal access by its members, owners, or citizenry (optimization being quite subjective, dependent on the habits, self-reflection, and reasoning of the citizenry). And yet paradoxically, boundaries and rules are of critical importance for co-operatives to offer the degree of participation demanded by the member-owners (some co-operatives may prefer direct participation, whereas others desire strong representation in a top-down management team). Processes should be put into place that reinforce predictable, concise, understandable avenues by which member-owners might engage in their co-operative. One such example is in the U.S. food co-operative sector, in which a sizable share of the co-operatives are implementing Carver's highly conceptualized Policy Governance® model; this then allows co-ops to follow a common, structured framework, and improve upon it. Concurrently, co-operative directors from across the country can share their experiences in interacting within that framework.

From this line of thinking questions arise such as, do various co-operative sectors (i.e. electric, food, etc.) across ownership models (worker, consumer, producer) adhere to specific governance practices? If so, how did they evolve and adapt? Could co-operatives optimize their governance through inter co-operative linkages (cross-pollination)?

Protect Democracy

Co-operatives must guard against capture, atrophy, and mal-intent. The practice of democracy helps to "bake-in" democratic culture, and adherence to the co-operative principles generates additional incentives which drive member-owner participation (specifically the return of patronage dividends). But what about those co-operatives that are currently captured by a small faction, or are under threat of demutualization? Proper laws and regulatory regimes can help guard co-operative democracy against such self-serving behavior as is the case with a New Mexico electric co-op whose management refused to grant its member-owners access to the co-op's by laws, thereby creating a power differential (one group is left with an upper-hand, having privileged knowledge of the rule of the game of their co-operative). But so too can mobilized co-operative advocates guard against such behavior. Credit unions are always under threat of demutualization, particularly when such a process can line the pockets of the sitting CEO. The US-based Credit Union National Association and other member credit unions have banded together to prevent select credit unions from demutualization by organizing public opinion against the demutualization effort, thereby preserving the co-op for future members.

Interesting questions arise from this including, what can we learn from demutualization –and counter demutualization- drives? Perhaps such cases may provide insight as to how co-op democracies atrophy? How do we identify an optimal regulatory framework that enhances co-op competitiveness and entrepreneurship? Do "model-laws" exist which might inform such ends?

Promote Democracy

Robert Putnam in his book Bowling Alone (2000) documented the declining arenas for civic participation. Fewer venues for civic engagement and governance result in fewer individuals with self-governing capabilities. Co-operatives are then tasked to not only promote internal venues for participatory democratic governance, but to do so in a challenging market environment. Boards will need to seek to create opportunities for participation in democracies that simultaneously strengthen democratic skills and lend toward market advantage. Examples may include activities such as building community conversations as seen in food co-operatives in Wisconsin (Sherwood, 2014) and multi-layered governance opportunities as seen in Affinity Credit

Union in Saskatoon (ibid). Internal organizational processes are demystified, and member-owners are made to feel empowered to participate. These are intentional, proactive steps boards can take, but there are other avenues created through required operations to build opportunities to participate in the process of reflection and change in the organization turning member feedback into an act of democratic participation.

Questions arising include, what are the avenues available to promote democracy? How can boards influence the entire co-operative to build and provide these opportunities for democratic participation and help members take advantage of these opportunities? What skills do members need in order to do so effectively? What are the results of these efforts in terms of performance and comparative advantage?

Perpetuate Democracy

The practice of democracy is a practice of applied education. It follows that the more democracies that exist, the greater the likelihood that individuals will be capable to engage in democratic self-governance. Therefore, the proliferation of co-ops is one strategy toward this end.

Another strategy is the continued development of robust participatory mechanisms within the co-op in an effort to engage as many member-owners as possible and thus build a pool of democratic leaders to take the co-op forward. Take for example the North Carolina State Employee's Credit Union (SECU; 2014). The $30 billion co-op has a location in every county of the state, and each location has a member advisory council serving as the locality's de facto board. These board members then can access the larger co-op structure. But of greater interest to the topic of perpetuation, this then creates a more engaged member-ownership and a pool of people capable of effective democratic governance within and outside SECU. In this manner, democratic self-governing tendencies are perpetuated throughout the organization and in the community.

Interesting questions arise including, do nations or regions with higher/lower densities of co-operative enterprises create more/fewer new co-operative start-ups? Do they have fewer/greater instances of demutualization? What are the mechanisms (policy, example, training etc.) through which boards can take action now that bolsters the likelihood that democracy will continue into the future?

Conclusions

Clearly there are many questions ahead with which practitioners will continue to grapple and researchers will continue to build understanding. Our paper has argued that co-operative boards share some of the same tensions and challenges of investor owned boards, but appear to have an even greater challenge to their logic of needing to meet diverse member needs through a democratic enterprise.The democratic nature brings a variety of unique vulnerabilities that must be attended to through actions such as practice, protection, promotion and perpetuation by governing boards. As the Blueprint points out, the external challenges are great. The related need is great for the research community to continue their efforts to understand effective governance of co-operatives in a way that deals with the paradoxical tensions and challenges faced by directors, as they work to live up to their expectations framed by their institutional logics.

Notes

[1]This paper approaches directors in their role as agents, although the literature on co-operative governance highlights the importance of the stewardship role, as directors are typically also members of the co-operative.

[2]We use this term to create distinction between the two models in order to help compare and contrast. In reality, individual corporations vary from this ideal type where we find co-ops having a narrower set of stakeholder needs to address, and IOCs focusing on more than simply maximizing shareholder wealth.

[3]Interestingly, in a co-operative that holds a diversity of values that at times appear to be in conflict, it may be possible for the democracy to suffer from a *Tyranny of the Minority*. This occurs when a small group forces their ideology to the forefront, attempting to bypass the democratic

process and the agents in place. This is done using the priority the co-operative places on a related value and then leveraging this to make their squeaky wheel gain attention. This is worth further exploration as, if a minority indeed is able to circumvent the processes used, the resilience of the democracy may be questionable.

[4]For further details of the events around the Socorro electric co-operative, see this article: http://www.informedcynic.com /SEC/sec-docs-jan-2010-dec-2010/081810-SEC_Investigates_Financial_Irregularities.pdf

References

Books

Aligica, P.D. and Boettke, P.J. (2009). *Challenging Institutional Analysis and Development:* The Bloomington School. New York City, NY: Routledge

Bernstein, P. (1976). *Workplace Democratization: Its Internal Dynamics.* New Jersey: Transaction Books.

Finkelstein, S. F., Hambrick, D. C., & Cannella Jr., A. A. (2009). *Strategic Leadership: Theory and Research on Executives, Top Management Teams and Boards.* Oxford: Oxford University Press.

Hamilton, A., Jay, J., & Madison, J. (1788). *The Federalist.* Ed. Edward M. Earle. New York: Modern Library

Kogler Hill, Susan E in Northouse, Peter. (2013). *Leadership: Theory and Practice*, 6th Edition. Los Angeles: Sage.

Lorsch, J. W, &Maclver, E. (1989). *Pawns or potentates: The reality of America's boards.* Boston, MA: Harvard Business School Press.

Ostrom, V. (1997). T*he meaning of democracy and the vulnerability of democracies: a response to Tocqueville's challenge.* USA: University of Michigan Press.

Putnam, R. D. (2000). *Bowling alone: The collapse and revival of American communities.* New York: Simon and Schuster.

Scott, R. (2008). *Institutions and Organizations: Ideas and Interests*. Los Angeles: Sage

Thornton, P. H, Ocasio, W., &Lounsbury, M. (2012). *The institutional logics perspective*. Oxford: Oxford University Press.

Tocqueville, A. (1945). *Democracy in America.*2 vols. Ed. Phillips Bradley. New York: Alfred A. Knopf.

Journals

Birchall, J. (2012). The comparative advantages of member-owned businesses. *Review of Social Economy*, LXX, 3: 263-294.

Cornforth, C. The governance of cooperatives and mutual associations: A paradox perspective. *Annals of Public and Cooperative Economies*, 75, 1: 11-32.

Donaldson, L. (1990). The ethereal hand: Organizational economics and management theory. *Academy of Management Review*, 15(3), 369-381
.

Eisenhardt, K. M. (1989). Agency theory: An assessment and review. *Academy of Management Review*, 14(1), 57-74.

Fama, E. F. & Jensen, M. C. (1983).Separation of ownership and control. *Journal of Law and Economics,* 26, 301-325.

Joyal, T. & Swanson, D. (2011, March-April). Precautions and protections: Summarizing legal responsibilities of cooperative boards. *Cooperative Grocer*, 26-30.

Malo, M-C. and Vezina, M. (2004). Governance and management of collective user-based enterprises: Value-creation strategies and organizational configurations. *Annals of Public and Cooperative Economics*, 75 (1): 113-137

Sherwood, A. L. (2014). Strategic leadership is a cooperative effort: Making co-op ends come alive in your community. *Cooperative Grocer*, May-June: 24-26.

Spear, R. (2004).Governance in democratic member-based organizations. *Annals of Public and Cooperative Economics*, 75:1: 33-59.

Spear, R., Cornforth, C., and Aiken, M. (2009). The governance challenges of social enterprises: Evidence from a UK empirical study. *Annals of Public and Cooperative Economics*, 80(2): 247-273.

Westphal, J. D. & Khanna, P.(2003). Keeping directors in line: Social distancing as a control mechanism in the corporate elite. *Administrative Science Quarterly*, 45: 366-398.

Miscellaneous

Affinity Credit Union. (2014, May 26). Retrieved from https://www.affinitycu.ca/YourCreditUnion/About/GovernStruct/Pages/default.aspx

Birchall, J. (2014). The governance of large cooperatives. *A research study for Cooperatives UK*. Retrieved May 15, 2014 http://www.uk.coop/sites/storage/public/downloads/the_governance_of_large_cooperatives_0.pdf

International Co-operative Alliance (1995). 1995 *Statement of Identity*.

International Co-operative Alliance (2013). *Blueprint for a Co-operative Decade*. Retrieved May 25, 2014 from http://ica.coop/sites/default/files/media_items/ICA%20Blueprint%20-%20Final%20-%20Feb%2013%20EN.pdf

McGinnis, M. D. (2012). *Updated guide to IAD and the language of the Ostrom Workshop*: A simplified overview of a complex framework for the analysis of institutions and their development. http://php.indiana.edu/~mcginnis/iad_guide.pdf.

Move Your Money Project. (n.d.). Retrieved June 26, 2014, from http://moveyourmoneyproject.org/

State Employees Credit Union. (2014, May 26). Retrieved from https://www.ncsecu.org/AboutSECU/Governance.html