

COOPERATIVE FOR THE FUTURE

Lada Rasmichová

Abstract

Cooperatives have had a long history on the territory of Czech Republic. Unfortunately, its reputation has been seriously damaged in the period after World War II when partly forced collectivization in agriculture and creation of hundreds agricultural cooperatives became one of the symbols of the establishment of communist power. That probably was why cooperatives were rejected as one of the methods of privatization on the end of the last century and why they have been ignored by both economic policy and theory in Czech Republic. At the same time, cooperatives can be a solution to the challenges of the sustainable development economy. Cooperative ownership leads to a different pattern of behavior from traditional ownership. From the point of view of economic theory, this different behavior can be explained in the different goal of the cooperative, which is to maximize profit per capita. The aim of this paper is to explain and justify this essential idea.

Key words: cooperative, self-management, employee ownership, economic democracy

JEL Code: A10, B50, D11

Introduction

Thirty years ago, the Czech Republic, together with other Central and Eastern European post-communist countries, found itself in a unique historic opportunity. This opportunity was to find one's own way to transformation of real socialism characterized by a non-market and dysfunctional economic system to a modern market economy. On that way we could use all experience, either the good or the bad ones which the surrounding developed part of the world, lucky enough developing in the post-war period in a democratic environment, not under the domination of the Soviet Union and the Stalinist distorted communist ideology, had gained and was willing to pass on to us.

Unfortunately, those who were designing this „own path“ to a market economy and trying to create it through various initiatives stayed alone. The majority science and political opinion led to the same mistake that the Czechs (as part of Czechoslovakia) had made once before in the 1950s when they were the most radical of the radical while deciding to uncompromisingly eliminate any form of private property. In the 1990s, we decided for equally radical and uncompromising return to capitalism of the first half of the twentieth century. The all-encompassing privatization, which was again unparalleled in our neighbors, led, among other things, to the extremely rapid creation of the modern Czech financial oligarchy, simultaneously and subsequently to the sale of “family silver” to foreign capital, and above all to new injustice and property and social inequalities which have had nothing in common with constantly proclaimed democracy. Obviously, the opinion has not been changed over the past thirty years. On the contrary, the privatization process culminated couple of years ago in the incredible restitution of property to the churches, which further shifted ownership structure in the Czech Republic from the twentieth even to the eighteenth century.

1 Self-management and Cooperative

Figuratively meaning, the Czech economy has been repainted from red to gold or to gold violet over the past thirty years. But colorfulness (plurality) should be part of democracy. Nevertheless, any proposals to provide space for other forms of ownership than "traditional" in the context of privatization were rejected by political decisions in the 1990s. For large state-owned enterprises, the ESOP method ¹ was seen the good alternative. It was a well-known and proven plan of worker ownership creation through a bank loan (Menke, Buxton, 2010)). For medium-sized and smaller companies, cooperative ownership was proposed, which, like the ESOP, would create owners from the existing employees of the then state-owned companies. Unlike the ESOPs, the cooperative brings economic democracy not only in the distribution of the generated profit, but also in ownership and management.

From evolutionary economics point of view, I understand, as I explain in this paper, this kind of microeconomic democracy not only as an inevitable outcome of the process of democratization of society, but above all as the only (complete) solution to the current conflict

¹The Employee Stock Ownership plan (ESOP) is an American type of benefit plan authorized by the Employee Retirement Income Security Act of 1974 and it is the most important and perspective form of employee ownership in The U.S. (Menke, 2010)

between the inherent capitalist orientation to growth on the one hand and the increasingly disturbing issues of sustainable development accompanied by post-industrial revolution 4.0.

When we mention a self-managed firm we mean clearly democratically organized company in which, in accordance with the definition of the ICA Group ², all its employees (management, officials, workers own the majority of shares. Three basic characteristics can be applied to such a company:

1 / All employees are owners, the team is not divided into those who own and other secondary employees.

2 / Ownership is common or collective as well as the responsibility for the use of this ownership.

3 / Employees own the majority of their company (its shares), which gives them real decision-making powers.

If we reformulate the third condition to the condition of 100% ownership, we obtain the most general definition of a fully self-managed enterprise = cooperative, as a form of full economic democracy (Vanek 1970). This kind of a self-managed company creates preconditions for a microeconomic solution of the current state of the economy. This kind of self-managed firm will be treated in the paper.

2 Cooperative and ownership

The cooperative is a form of return to truly private property. Small family-type companies which have survived in contemporary corporate capitalism are ideal self-governing companies. However, their significance is negligible in terms of their share of GDP as the condition for their existence is only small capital ownership therefore their importance in the current character of production is very limited.

Cooperative is a way of combining large capital ownership of a given stage of technology development with individual ownership, which, in contrast to public ownership, creates a motivation for profit and allows full operation of market mechanisms. The basis for the effective rationality of self-governing companies (cooperatives) is that they extend the ideal motivation from self-employment to companies with many employees which create in common working and managing team. (Ellerman, 1975)

² The ICA Group „is a leading expert on worker ownership and the oldest national organization dedicated to the development of worker cooperatives“ <https://icagroup.org/>

The cooperative is created by the union of capital ownership of several individuals for the purpose of business. The workers' cooperative is a business company in which the ownership of business assets is entrusted to members, the members are sovereign subjects and each of them has one vote. In a worker cooperative all employees are its members. At the same time nobody else that employees are members of the firm, it means all owners are employees and all employees are owners at the same time.

The defining condition of a self-governing cooperative, as we understand it here, is the non-existence of an employment contract. The wage labor ends here.

As has been said, there are no owners in the cooperative who are not members of the team. Any external financing of the company does not take place through the sale of shares to foreign shareholders. If one of the members leaves a cooperative, the company settles its property relations with him by repurchasing his share and the ownership of this member expires.

From the point of view of economic theory, such an arrangement of property rights has a deeper impact than it might seem at first glance. Ellerman distinguishes between self-ownership (characteristic of companies with partial ownership of workers - workers' shares, ESOP, etc.) and self-partnership defining cooperatives. (Ellerman, 2019). The cooperative is not defined by its ownership. Ownership loses its importance because ownership does not in itself create a right to an income. People come together here for business purposes, and the only source of income is the result of their common efforts.

Ownership loses its meaning but does not disappear. The members of the cooperative have a collective right to use the company's assets, but they are not their full owners in the sense that they could sell or spoil their share of ownership. In a pure theoretical model of cooperation, all physical and monetary assets of the company are leased (Vanek, 1977). The capital owner's claims are paid through interest, rent or annuities. The members of the cooperative are the owners of the work and they hire capital. The situation is thus quite the opposite of that of a traditional capitalist enterprise, where the owner of capital hires work. In the cooperative, labor becomes a source of profits and capital is a deductible item. Consequently, the resulting income is a return on labor, not capital.

Leasing capital does not always have to be a condition for the functioning of a self-governing company. The experience of Mondragon ³ proves that the activities of the cooperative can be funded from its own resources and that in this case the collective of the self-governing company can be both the owner of labor and capital.

3 Cooperative and organization

Adherence to some basic organizational principles is essential for the proper functioning of the cooperative.

The main one is the already mentioned principle one man - one vote. For participation in decision-making and management of the company, it is not the size of the capital contribution of a member of the cooperative that is important, but its inclusion in the work team.

The entire collective of a self-governing company always decides on major issues, operational management is performed by professional management. The daily job of managers is no different from the job of the management of a classical capitalist firm, but its interests are fundamentally different. Managers must logically be members of the cooperative, and therefore their interests are the same as those of all other members. Management control is performed by the board of directors, whose members are also members of the cooperative and are elected by the general meeting of the cooperative according to the principle of one person - one vote.

4 Cooperative and its Goal

There are, therefore, two arguments for a thesis that a self-governing firm overcomes the separation of ownership from business, which I consider a fundamental problem of contemporary capitalism. The first of them is that managers who are members of the work team and at the same time the owners, identify with the other participants of the firm (Zelený, 1997) Secondly, the control of managers, which is aimed solely at the control of their abilities, not the promotion of their own interests, is carried out continuously, immediately and informally by other members of cooperative who, unlike external shareholders in a public joint stock company, are perfectly informed.

³ Mondragon is Spanish corporation (since 1956, with over 80000 owners-employee) based fully on cooperative principles, which is seen a „laboratory of self-management and cooperative“ <https://www.mondragon-corporation.com>

There is a match of interests within the self-governing company. However, the match of interest is not enough to claim that the behavior of a self-governing firm is different from that of a traditional capitalist firm. We must first ask a question what is interest of employees-owners.

Owners who are managers of their company at the same time are interested in profit, regardless of whether it is a traditional capitalist company or a self-governing company. The company's employees are interested in the salary, again completely regardless of whether it is a traditional company or a cooperative. It logically follows that owners who are also employees are interested in profit and wages at the same time. Because wages are no longer a deductible item, as explained above, we can say that wages and profits form the newly created value of a self-governing enterprise, which we call the total income of a company. The self-governing company is interested in its total income.

In a schematic representation, the difference in the motivation of a classical (or perhaps rather neoclassical) capitalist firm and a self-governing enterprise is as follows:

In a neoclassical concept, an owner in the role of entrepreneur and capitalist, calculates his profit as the difference between total revenue and the cost of production factors – labor and capital or in other words human and material capital:

$$z = TR - (TC_L + TC_K)$$

In a cooperative, an owner in the role of entrepreneur and employee calculates his income as the difference between total revenue and the cost of only material capital:

$$d = TR - TC_K$$

Wages, which are a cost to the capital owner, are part of the income of the self-governing collective.

Although the theory of self-governing economy commonly uses the term profit in connection with this income, it should be noted that cooperative profit is fundamentally different from capitalist profit. A self-governing enterprise thus relieves ninety percent of humanity from the obligation to live with a negative sign and to act in the market system as a deductible item (Vanek 1975).

Let's continue with our thoughts: A self-governing company is interested in its total income, but not in its total size. She is interested in the size of the income in relation to the number of employees or in other words, the goal of the self-governing company is to maximize the income per employee (Ward, 1958)

Income growth can be achieved in two ways: by increasing the scale of production or by reducing costs. The first case is uninteresting for a self-governing company. From a short-run point of view, the growth in the scale of production means the involvement of additional production factors, it also means the employment of additional work. Thus, for the cooperative, the expansion of production means an increase in the volume of income (profit), but at the same time an increase in the number of employee-owners who claim their share in this profit. From the point of view of the "old" members of the self-government, who would decide about such an expansion of production, the increase of income in this way will have no effect.

Therefore, a self-managed company will grow only if its growth will be accompanied by cost savings, so it will grow exactly to the point of minimum average costs, it means maximum production efficiency (Bowles, 1993). Exactly at this scale of production the company maximizes income (profit) per employee-owner. Thus, a self-governing firm will naturally tend to be smaller than a capitalist firm whose economic security is largely based on its size.

Self-management through a total income creates a company's immediate interest in cost savings and ensures that the size of the company contributes to production efficiency (Pencavel, 2012). Self-government thus returns to the market its function of ensuring allocation and production efficiency, which the market has lost with its previous development of capitalism to its corporate form based on the separation of ownership and business and on the growth of companies as a source of certainty.

5 Cooperative and certainty

For a capitalist enterprise, growth is a fundamental source of certainty. Does this mean that a self-governing company, if it does not strive for growth, does not strive for certainty for its employee-owners? No, certainty is a natural goal of every economic individual, including those who are associated in a self-managed enterprise. Efforts to achieve security are maintained, but the source of security is changing.

In general, a firm operating on the principle of employee total income maintains a higher employment, better performance than a capitalist firm and is more able survive economic crises (Guzman, 2020). The evidence is not only the experience of Spain's Mondragon and the US majority ESOP, but also the millions of economic entities "paid"

directly from profits: farmers, lawyers, doctors and others who are statistically much more immune to crises than those involved in the production process through employment relationship.

The root cause of this phenomenon is clear. Profit sharing tends to reduce wages as soon as economic problems occur. For a capitalist firm, redundancy is the first solution to economic problems and the only way to reduce the wage costs. In a profit-sharing company, labor costs fall automatically as the total income decreases. Using macroeconomic terminology, we could say that they act as a built-in stabilizer. The pressure to reduce employment is therefore not so important.

For a self-managed company that makes democratic decisions, this phenomenon continues to be supported by the efforts of the owners to achieve certainty. The certainty in this case is not the profit or the dividend, but just the preservation of the job (Krimerman 1999). Therefore, in the case of economic difficulties, not only profit shares but also basic wages may decrease. In such a case, collective decision is aimed at overcoming economic difficulties and preserving jobs. The will to survive is much greater in a self-managed company than in the case of a classic joint-stock company, in which any economic difficulties manifest themselves as a decrease in the value of shares further aggravating these difficulties. The will to survive the cooperative together with the downward flexibility of wages, is the basic source of security for the individuals that associate in the cooperative.

Another reason why a self-managed company is better able to withstand market fluctuations is probably due to another circumstances. In a self-managed enterprise, conflicts in relations between employers and employees disappear. This gives cooperative extraordinary flexibility in decision-making processes. At the same time, the members of the cooperative have immediate and complete control over the results of the company's activities. In contrast, capital market signals to which the owners of a classical joint stock company respond can often be inaccurate and always arrive with a time delay. Management control by shareholders is therefore not only limited due to incomplete information, but it is also lengthy and cumbersome. The self-managed working team always has a perfect overview of the economic situation. This allows him to react faster and make decisions that will help overcome any economic difficulties. Greater flexibility and a quick response to market signals is another source of certainty and the basis for greater stability. Flexible responses to market signals are being replaced by diversification of investment and endless growth, which is a

source of certainty for companies in corporate capitalism (Krimerman, 1992). Contemporary capitalism limits the effects of market forces by reducing ownership from management by reducing market motives. The relationship of corporate owners to real business is highly mediated to nil, and their motives are not business motives, the income their ownership brings is not real business income (Ellerman, 1975).

Conclusion

Here stated theses concerning the functioning of the cooperative lead us to believe that in a market where self-ownership would prevail, we could expect not only economic democratization and fairness in distribution, but also the restoration of market competition and the creation of preconditions for better efficiency through an invisible hand of market with the need for significantly less macroeconomic intervention.

From my point of view, the most important attribute of a self-governing economy is that it is not growth oriented. Goal of self-managed firms leads them to effectiveness, market stability and to preserve jobs. The self-governing economy thus can respond to the new historical situation of postindustrial society, to the fact that society is able to satisfy its real material needs in a very short time, and further growth of material consumption based on consumer persuasion has catastrophic effects on the planet. The self-governing economy creates the preconditions for society to shift the focus of its life to happiness and security of its members on one hand, and to the non-productive area - to use only the time and reserves of natural resources and energy it really needs to do so on other hand. It creates preconditions for a change in social rationality.

In the future, we should be grateful to capitalism for the fact that it is its natural focus on growth that has achieved such labor productivity that enables this new social rationality.

References

Bowles, S., Gintis, H. A Political and Economic Case for the Democratic Enterprise. *Economics and Philosophy*, Vol. 9, No.1, 1993, (pp.75-100.)

Ellerman, D. The "Ownership of the Firm" is a Myth. *Administration and Society*. Vol. 7, No. 1, May, 1975 (pp. 27-42)

Ellerman, D. Worker Ownership and the Current Crisis, in *Conflicts. Stability. Democracy? The 2019 Serbian Political Science Association Annual Conference Proceedings*, September, 2019 Belgrade, ISBN 978-86-6425-067-2

<https://ellerman.org/wp-content/uploads/2020/03/WorkerOwnershipAndCurrentCrisis.pdf>

Guzmán, G., Santos, F.J., Barroso, M. Analyzing the Links between Cooperative Principles, Entrepreneurial Orientation and Performance, Small Business Economics. Vol 55, No. 5 December, 2020. DOI:[10.1007/s11187-019-00174-5](https://doi.org/10.1007/s11187-019-00174-5)

Krimerman, L., Lindenfield, L. When Workers Decide. New Society Publishers. Philadelphia, 1992

Kruse, D. L., Freeman, R.B., Blasi J.R. Shared Capitalism at Work. University of Chicago Press. Chicago, 2010 ISBN: 0-226-05695-3

Menke, J. D., Buxton, D. C. The Origin and History of the ESOP and Its Future Role as a Business Succession Tool. Journal of Financial Service. Vol.74. May 2010. <https://cleo.rutgers.edu/articles/the-origin-and-history-of-the-esop-and-its-future-role-as-a-business-succession-tool/>

Pencavel, John, Worker Cooperatives and Democratic Governance. IZA Discussion Papers 6932. Institute of Labor Economics (IZA), 2012

Vanek, J. General Theory of Labor-managed Market Economies. Cornell University Press. 1970 <https://www.questia.com/library/1442620/the-general-theory-of-labor-managed-market-economy>

Vanek, J. Some Fundamental Considerations on Financing and the Form of Ownership under Labor Management, In: The Labor-Managed Economy: Essays by J. Vanek. Cornell University Press. Ithaca, 1977

Ward, B. The Firm in Illyria: Market Syndicalism. The American Economic Review. Vol. 48, No. 4, Sep., 1958 (pp. 566-589)

Zelený, M. Insider Ownership and LBO performance. Human Systems Management. Vol. 16, No. 4, pp. 243-245, 1997 DOI: [10.3233/HSM-1997-16401](https://doi.org/10.3233/HSM-1997-16401)

Contact

Lada Rusmichová

Prague University of Economics and Business

W. Churchill Sq. 1938/4, 130 67 Prague 3 – Žižkov, Czech Republic

rusmichl@vse.cz