

Co-operative Group Governance Reform Proposals and Co-operative Principles

This paper summarises my view on the compatibility of the proposed Co-operative Group Governance Reforms with the Society's status as a bona fide co-operative in line with the ICA Principles. It should be read alongside the overview of the proposed new governance structure circulated as part of this pack.

Since early June this year, I have been involved in developing these proposals and in the extensive consultation with members that has been a key part of that process. There has been a serious and, in my view, successful attempt by all concerned to co-operate in balancing member voice, member representation, business expertise, and effective management to meet the current needs of the Society and its members. The resulting governance model should allow a new start and pave the way for a successful co-operative future.

Governance and Bona Fide Co-operatives: The Key Elements of Co-operative Governance

The ICA deals with governance in its second Principle:

“Co-operatives are democratic organisations controlled by their members, who actively participate in setting their policies and making decisions. Men and women serving as elected representatives are accountable to the membership. In primary cooperatives members have equal voting rights (one member, one vote) and cooperatives at other levels are organized in a democratic manner.”¹

That principle is applied by the UK registrar of co-operatives, the Financial Conduct Authority, in applying the statutory “bona fide co-operative” test to society registrations and the registration of rule amendments. It seems clear to me that the proposed structure meets both of those tests.

Scholars have developed certain key elements that are needed in the governance of large co-operatives so that they can operate effectively in the market place and also maintain their co-operative identity.

Four key governance elements have been identified as appropriate for large co-operatives²:

- member voice,
- member representation,
- expertise and
- effective management.

How do the proposed governance reforms of the Co-operative Group deal with these key elements of co-operative governance?

The purpose of a co-operative is to serve its members and in accordance with the ICA's Second Principle members must have ultimate control and be able to actively participate in its governance. Under these proposals, democratic member control and voice are secured in the ways set out below.

Direct Member Voice

The members of the Co-operative Group will have greatly increased direct control and participation in governance. This is a dramatic extension of member control.

¹<http://ica.coop/en/whats-co-op/co-operative-identity-values-principles>

²Prof. Johnston Birchall, *The Governance of Large Co-operatives: A Research Study for Co-operatives UK*, Manchester 2014, p 77

Members have direct control of all major constitutional decisions, they can requisition general meetings and submit resolutions. They can remove directors. They elect part of the Board on the basis of contested elections and can approve or reject the independent non-executive directors. They have to approve surplus distributions, they consider accounts and annual reports, they vote on rule changes and any other resolutions proposed to or by them (either directly or through the Council they elect) in general meetings or in a referendum. This provides direct member control of all major decisions and election of a board – subject to the candidates for the Board meeting objective requirements of competence and experience established to ensure effective decision-making on the members' behalf.

Member Representation

The direct constitutional power of ordinary co-operative members will be supplemented by direct communication with all levels of the organisation. That is facilitated by direct engagement with the full use of social media and other digital communication and through local committees and the Council as well as community activities important to people as members. Member engagement can be “informal” but in these proposed reforms it is linked to clear constitutional rights.

The Members' Council represents members and is directly elected by and from them. It guards the constitution, has direct links to the Board and can influence policy and strategy and decide certain matters reserved to it.

This body will maintain active member involvement and develop wider member engagement. It can express members' views, bring motions to general meetings and represent constituencies of members through those functions and by direct dialogue with the Board. In particular, it is a further check on the Board as it will receive reports from the Board and have its own secretariat.

There is a commitment to provide suitable training and education to Council members and the Council and Senate may choose to request internal or external advice, including commissioning research, within any budgetary constraints determined by the Group Board.

In order to independently scrutinise and effectively challenge on any area of concern, the Council is entitled to any information it requires on any matter in connection with or concerning the Society's affairs from any officer, employee or advisor of the Group, subject to any legal or regulatory constraints (e.g. in relation to price sensitive information and confidentiality in the light of the Group's listed securities).

The Council and Senate publish an annual statement to the members of the Group about their own activities and, in the event of any unresolved disagreement with the Board, on where the Board has not followed the Council's advice or recommendations. In holding the Board to account the Council has various sanctions available to it, including recommendations to members not to re-elect individual Directors who are retiring by rotation and the power to propose a motion at a Society General Meeting to remove a Director before the expiry of his or her term of office. In practice, this will give the Council and Senate considerable influence in their discussions with the Board.

Expertise and Effective Management

In the proposed Co-operative Group reform, the key is that the whole membership elect and can remove Board members but that nomination depends on passing a threshold developed and applied by the Nomination Committee (NomCo). The threshold concerns competence to run a business of the Group's size, membership of the society and a commitment to its co-operative nature and the service of its consumer members. Every Board member has to be approved by the whole membership. If they refuse approval, the person must leave the Board. The serving CEO and one other executive are a minority on the Board and are there ex officio, having been appointed to their role by the whole Board. Up to three of the directors, having passed the

threshold applied by the Nomination Committee, are elected in contested elections rather than on the basis of being approved or rejected.

The process of ensuring that directors provide the range of skills and experience that is needed involves the NomCo. However, proposals from that committee to the Board must be unanimous and the NomCo is composed of the Council President plus two Member Nominated Directors and the Group Chair plus two independent non-executive directors. That ensures member involvement in the Nomination process.

The complexity of the Group's business and its recent history demonstrate the importance of holding executives to account and also show that, without relevant experience and expertise balanced across the Board, that is unlikely to be done effectively. The question is how business decisions and strategies can be tested in open and transparent team discussion and, when necessary, executives removed without a divisive or adversarial boardroom atmosphere. A team of executives and non-executives with the skills and experience to advise and assist is a tried and tested formula in the UK. The directors' clear roles and responsibilities ensure the continued independence of the majority of directors and their ability to challenge the executives.

At the operational level, the CEO and the executive team will be responsible for management. The Board will have a majority of independent non-executive directors and up to three member nominated directors. They will all meet, individually and as a group, objective criteria set to ensure appropriate skills and expertise. The Board deals with strategic decision making in consultation with the Council. It also both supports and challenges the executive in business and co-operative terms.

The competence of all Board members, and the independent perspective brought by the independent non-executive directors, is intended to ensure effective business strategy and execution and to support the executive in its work. The roles of the risk & audit committee, the remuneration committee, the scrutiny committee, the senior independent non-executive, and of the internal and external auditors should equip the Board to make good decisions. The whole structure is focused on pursuing the interests of the Society and its members. It is designed to give the best possible chance of effective member centred management.

The independent directors will be subject to approval by the whole membership and up to three member nominated directors will be chosen by contested elections, having first satisfied the objective criteria in respect of skills and expertise.

Conclusion

This analysis suggests that the current proposals meet a number of tests.

First, they provide members of the co-operative group with greater powers than they have ever previously enjoyed. That is achieved by the direct constitutional powers they will have to elect and remove directors and the right to fully participate in decisions at meetings or through referenda. There is also provision for two way communication between members and the Board and Council who work for them. That should provide real and substantial engagement for members who want it. The local and regional structures to be designed by the Transitional Council will provide involvement for members in community campaigning and the development of activities. They also facilitate member input to express and develop co-operative values and principles.

Second, the proposals provide, in the Council, a representative structure to balance the power of the Board by consultation, analysis, access to the membership and the power to gather information, raise issues and to provide input on strategy. It is important as a guardian of the constitution and of co-operative values and principles. There will be direct dialogue between the Senate, the Council President and the Board. The Council reports to members.

Third, the proposed board structure addresses the problem of combining effective and focused

management with the necessary independent input and scrutiny in line with governance best practice as adopted in the UK context. The reputational risk to both executives and independent non-executive directors give every incentive to perform well. It also ensures that both those directly engaged in management and those who provide independent input and accountability have the level of experience, competence and expertise that the organisation needs.

In addition, all directors will be elected by members, although some without a contested election, and all will be open to removal by members either at the end of their two year term or during it. The annual report of the independent Council provides a concrete method for debate and accountability to members.

To achieve all of this, the factors found in these proposals draw on UK governance experience and best practice and also borrow from many particular aspects of international co-operative governance. The members' Council is found in a number of contexts and the use of the expertise of independent outside directors is increasingly common.

The current proposals represent a major improvement in the level of control available to Co-operative Group members compared with the existing system. They also provide an innovative and creative example for other large co-operatives faced by the perennial problems of combining expertise with member control in a diverse business.

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