

## **THE ROLE OF LAW IN CO-OPERATIVE DEVELOPMENT**

### **The case of South Africa**

**By Jan Theron**

The first national legislation for co-operatives was introduced in South Africa in 1922. Since then entirely new legislation regulating co-operatives has been introduced on three occasions. However for my present purpose, I need only distinguish between the pre-democracy legislation and the post democracy legislation.

In terms of the pre-democracy legislation, there were two kind of co-operatives possible: an agricultural co-operative, and any other kind of co-operative apart from an agricultural co-operative. The latter were called trading co-operatives.<sup>1</sup> This legislation catered primarily for agricultural cooperatives, however, and the members of these co-operatives were white farmers on commercial farms.

Undoubtedly the fact that the legislation made detailed provision for agricultural co-operatives was one of their ingredients of their success. It would be impossible to separate this from other forms of support the state provided, both directly and indirectly over the years. Co-operatives, for example, were an integral part of the marketing boards through which government marketed agricultural products.

Other forms of co-operative did not receive the same legislative recognition or support. These included grassroots initiatives during the 1980s and 1990s by community organisations and trade unions to establish worker or producer cooperatives. Few of them proved sustainable, however, or provided a model of organisation that could be replicated, although it would be difficult to say how much this had to do with the legal or policy environment and how much had to do with the fact that these co-operatives were often established without any clear strategy as to how they were to operate as enterprises.

The 1990s in South Africa were about the transition to democracy and its integration into the global economy, which also necessitated the dismantling of agricultural marketing boards, in which co-operatives often played a central role. For this and other reasons many established co-operative converted to companies during this period.

---

<sup>1</sup> The Co-operatives Act of 1981( Act 91 of 1981) .

There was renewed interest in co-operatives on the part of government after 2000, and in about 2002, following a decision to transfer co-operatives from the Department of Agriculture to the Department of Trade and Industry (DTI), government embarked on a process of changing the legislative and policy environment. This process was influenced by the approach advocated by the International Labour Organisation (ILO) in terms of which legislation is informed by a formal policy, and the state exercises a light hand in regulating co-operatives.

Accordingly, in 2004 a Co-operative Development Policy (“the Policy”) was adopted, and in 2005 the new Co-operatives Act (“the Act”). It is, however, questionable to what extent the Act was informed by the Policy, since the approach adopted by the Act is in certain respects different from the Policy. A draft of what is now the Act was already in circulation prior to the adoption of the Policy, in the form of a draft Bill.

The Act set out to remedy some obvious deficiencies with its predecessor: the fact that the legislation did not adequately define a cooperative, or refer to the internationally accepted cooperative principles, for example. The 1981 Act had also to an extent departed from these principles, such as the principle that each member has one vote in a primary cooperative, regardless of the number of shares held.<sup>2</sup> The Act expressly seeks to promote other kinds of cooperative, as well as agricultural cooperatives. It also recognises the need for specific provisions relating to specific kinds of cooperative, namely housing cooperatives, worker cooperatives, agricultural cooperatives and financial services cooperatives, including SACCOs. These provisions are set out in a schedule to the Act<sup>3</sup>.

To obviate the need for SACCOs and other financial service cooperatives from having to be exempted in terms of Banks Act, National Treasury piloted the introduction of the Co-operative Banks Act (CBA) in 2007. This provides for the “registration of deposit-taking financial cooperatives as cooperative banks” whose scale of operations exceed the stipulated level.<sup>4</sup> A Cooperative Banks Development Agency (CBDA) was also established in terms of the CBA with the object of, amongst others, supporting, promoting and developing cooperative banking.<sup>5</sup> The CBDA is already operational.

In the meantime, in 2005, the transfer of co-operatives to DTI had been effected, and a new a Co-operatives Development Unit established.<sup>6</sup> The policy approach underlying the establishment of the Unit was to differentiate the development role and that of supervision. Supervision was now to be the sole function of the office of the Registrar of Co-operatives. This office was

---

<sup>2</sup> Section 3(1)(b). This refers to the second principle, of democratic member control.

‘Statement on the Cooperative Identity’, International Cooperative Alliance, Manchester, 1995.

<sup>3</sup> Schedule 1, Special provisions relating to certain kinds of cooperatives. Cooperatives Act, 14 of 2005.

<sup>4</sup> Section 2 (i), Act 40 of 2007. The Act only applies, in terms of section 3(1), to cooperatives with more than 200 members and holding deposits of members in excess of R1 million.

<sup>5</sup> Section 55 (1), Act 40 of 2007.

<sup>6</sup> The Cooperatives Act 14 of 2005. It was assented to on 18 August 2005.

located within DTI as a sub-division of the same office responsible for the registration of companies.

In 2010 the DTI adopted amendments to the Policy, and in 2012 it adopted a strategy document, with the object of implementing the Policy.<sup>7</sup> In the interim, there had been an exponential growth in the number of co-operatives registered with DTI. Whereas in 2002 there were 1 444 cooperatives, and the number was falling, by 2005/06 this trend had been reversed, and the number stood at 7 355, a massive increase. By 2011/12, according to the strategy document, the number was 43 062, and continues to grow. I am advised that there are now over 60,000 co-operatives on the books of the Registrar.<sup>8</sup>

If 60, 000 co-operatives were operating as such, and provided on average employment to ten people (five is the minimum number of persons that may form a co-operative, in terms of the Act) then co-operatives would be making a substantial contribution to South Africa's unemployment problem. The employment co-operatives generate is also at a minimal cost, since co-operatives subscribe to the value of self-reliance. The number of jobs that government's controversial youth employment subsidy hopes to generate, by way of comparison, is 423,000.

My topic here, however, is not the potential of co-operatives in creating employment. The question I would like to explore is to what extent this exponential growth of co-operatives is attributable to the new legislative and policy environment, and what general lessons can be learned from the case of South Africa. The conclusion I arrive at is that notwithstanding the exponential growth of co-operatives, or perhaps because of it, there are more negative than positive lessons to be drawn from the South African case, for reasons I will explain.

### **The positive and the negative about the South African experience**

The positive lesson to be learned, I think, concerns the initial "massive" increase in the number of co-operatives. It would be difficult to explain such an increase if these co-operatives were not responding to a real need, expressed by people on the ground, in the poorest communities, for enterprises based on the notion of human solidarity rather than the individual pursuit of profit. The fact that many of these co-operatives were located in the poorest parts of the country, Limpopo, Eastern Cape and rural Kwazulu Natal, confirms this analysis.

The only external factor that could explain this increase is the policy and legislative changes in the environment in which co-operatives operated, coupled with the fact that government had signalled its intention to support co-operative development. Even though the Act was not yet operational, government's intention to adopt new legislation had been publicised through a

---

<sup>7</sup> DTI, 2012. Integrated Strategy on the Development and Promotion of Cooperatives : Promoting an integrated Cooperative Sector in South Africa, 2012-2022.

<sup>8</sup> Unless otherwise stated, data provided by Ursula Titus, DTI.

series of road-shows, and a process of consultation with stakeholders, including NEDLAC.<sup>9</sup>

However, even at this stage, questions were beginning to emerge as to how much of this growth represented genuine co-operatives and how much represented an opportunistic response by sharp operators to the possibility of enriching themselves. The province where the most co-operatives were formed, Kwa-Zulu Natal, was where the provincial government was most proactive in promoting co-operatives. Support took the form of the establishment of a co-operative lending programme operated by a provincial development bank.<sup>10</sup> There is quite a lot of anecdotal evidence of “co-operatives” being established simply to access loans, and never functioning

Soon afterwards, “having identified co-operatives as one of its flagship projects”, the DTI established its own incentive scheme. This incentive scheme entails the payment of a once-off grant to cooperatives, subject to certain conditions, including the requirement that the cooperative concerned have a business plan (which is not a requirement of the Act).<sup>11</sup> Initially the co-operative concerned was required to provide a “matching” amount equivalent to ten percent of the approved costs of a project. Even then, there was anecdotal evidence of co-operatives being formed in order to access these grants, but never functioning as such. Subsequently DTI has dropped the requirement of a matching amount.

The sad truth is that no-one really knows how many of the co-operatives on the books of the Registrar are functional, and there is also no agreement as to what the criteria for a functional co-operative should be. The requirement that a co-operative should have submitted an audited financial statement to the Registrar, as they are required to do in terms of the Act, would certainly exclude some genuine co-operatives that are unable to afford the costs of producing audited financial statements.

The DTI itself regard most of the new co-operatives that have been established as worker co-operatives. It is understandable that many worker co-operatives would have been formed, given the economic needs that lead people to form co-operatives. But this may also be because “job creation” is one of the criteria to qualify for a grant or loan. Moreover, even though the Act clearly identifies co-operatives as a distinct form, requiring a specific kind constitution, the DTI used to provide all groups wishing to register a co-operative with the same model constitution.

Although the DTI now has different model constitutions for different kinds of co-operatives the problem of how to classify some kinds of co-operative remains. This can be illustrated with the example of a collective farm, which could be categorised as a worker co-operative which happens to be in the agricultural sector, or an agricultural co-operative. Consequently, although the

---

<sup>9</sup> The National Economic Development and Labour Advisory Council is a body made up of government representatives, representatives of organised labour and employers, and a fourth “chamber” supposedly representing “the community”.

<sup>10</sup> Ithala Development Finance Corporation. See [www.thala.co.za](http://www.thala.co.za)

<sup>11</sup> Cooperative Incentive Scheme Operational Guidelines, DTI.

DTI does distinguish between different kinds of co-operatives, the reliability of this data is questionable.

The importance of distinguishing between worker co-operatives and other co-operatives relates to the vexed issue of the applicability of labour legislation. The reason this issue arises is because labour legislation applies to a relationship between an employer and employee(s), and regulates the exercise of power by the employer over the employees. However in a genuine worker co-operative there should be no such power relationship, because the workers that are members are at the same time the joint-owners. Perhaps the easiest way to understand the relationship between members and their co-operative is as collective self-employment.

The approach taken by the Act to this issue is to provide that certain labour laws do not apply to worker co-operatives, notably those regulating unfair dismissal and basic conditions of employment. However, for the purposes of laws providing certain forms of social protection (unemployment insurance and compensation for occupational injuries) members will be deemed to be employees. The number of persons a worker co-operative may employ without their being members is also strictly limited, to prevent the misuse of worker co-operative.

Notwithstanding these provisions, firms in the clothing industry in Kwazulu Natal have converted to “cooperatives” with the objective of evading the provisions of a collective agreement entered into between the trade union and employers in that industry. If these firms were indeed worker co-operatives there would have been a change in control, and they would now be managed subject to the direction of workers. All indications are that the “co-operatives” are bogus, and the alleged conversions a sham.

As if to confirm it, workers at one of the “co-operatives” came out on strike while a researcher for the project I co-ordinate was conducting interviews on this question in the town of Newcastle. The workers demand was an interesting: either they be made members of the co-operative, and be entitled to the benefits of working for an enterprise they control, or their bosses comply with the collective agreement in question.

### **Lessons to be learned**

Co-operatives represents an alternative both to the for-profit form of enterprise, exemplified by the company, and the non-profit organisation, which does not have an economic objective. For this reason, the odds will always be stacked against a co-operative movement becoming established. Any abuse of the co-operative form, but especially widespread abuse, is bound to make the task of establishing a viable movement in South Africa that much more difficult. How did this situation come about, and were there legal steps that could have been taken to prevent it?

At the risk of stating the obvious, I think the following points can be made with regard to the South African experience:

1. The Policy and the Act are obviously not without flaws, but all they can aspire to do is provide a framework within which co-operatives can emerge, given the right leadership. I refer here to the leadership of the co-operative movement itself. I refer more broadly, also, to the leadership role the DTI should be playing, as the government department responsible for co-operatives, and within political organisations and civil society.

Where, however, there is on the one hand a corrupt leadership, concerned with self-enrichment and individual advancement, or, on the other hand, a leadership that believes that the only solution to the problems of unemployment and under-employment is the pursuit of economic policies that are supposed to stimulate economic growth, it is very unlikely that co-operatives will become anything more than a panacea.

It is clear from both the provisions of the Act and the accompanying memorandum, that the drafters were mindful of the danger that co-operatives might be abused, and had taken specific steps to prevent abuse. The fact that abuse has nevertheless occurred can be laid squarely at the door of DTI, and co-operative movement itself for allowing it to happen.

However to blame the co-operative movement (ie the genuine, as distinct from bogus co-operatives) is to blame the victim. So too, it is not entirely helpful to blame DTI, when the relevant departments have from the outset been the denied resources they would have required to carry out their functions. The Co-operatives Development Unit was from the outset hopelessly under-resourced. The office of the Registrar simply has not had the personnel to evaluate applications, let alone monitor compliance with co-operative principles. At root and base the political argument as to why we need to promote co-operatives has not been made out.

2. One manifestation of the lack of political leadership displayed is the extent to which government continues to work in silos. A good example is the failure of the Department of Agriculture to promote co-operatives, ever since it surrendered the competency to DTI, while at the same it claims to support small-farmers. It is inconceivable that any policy to promote small-farmers could be successful in the current economic climate unless it were coupled with a policy to promote small-farmer co-operatives.

Misguided efforts to promote co-operatives can be no less damaging. In some provinces, people have been encouraged by government to form co-operatives in order to tender for school feeding schemes, without any consideration as to how such entities would be able to operate as co-operatives, or be sustainable.

3. Incentives for co-operatives are justified, but direct financial incentives in the form of grants or loans are obviously open to abuse. They can also be the kiss of death for co-operatives that have not yet come to grips with how precisely they propose to function as a co-operative, and what their objective is. As a form of enterprise that is supposed to be founded on self-reliance, incentives should be targeted at co-operatives with a proven track record, and that have demonstrated the capacity to utilise such loans or grants properly.
4. The adoption of a policy, and the introduction of legislation, in and of itself does not create a legal environment that is less hostile to co-operatives. What is needed is people who are willing to assert the rights co-operatives have in terms of the legislation, and to challenge the disregard of the legislation that makes the abuse of co-operatives possible.

The DTI is now proposing to amend the Act. In terms of a draft Bill that still has to be tabled in Parliament, it is proposing to institute a Cooperatives Advisory Council instead of the Cooperatives Advisory Board that the current Act mooted, to advise government on policy issues and matters related to the application of the Act. (The proposal of a Board was never implemented, for reasons that are not apparent).<sup>12</sup> It is also proposing to introduce a Cooperative Development Agency, a training academy and a Cooperative Tribunal, as well as other amendments of a more technical nature.

It is not certain at the time of writing whether these proposed amendments will be adopted. Even if they are, it will depend on what resources they are allocated whether they will be able to contribute meaningfully to co-operative development. However legislation will not overcome the more fundamental problem, the absence of leadership and the weakness of co-operatives on the ground.

---

<sup>12</sup> Chapter 12, Act 14 of 2005.