

# One Hundred Years: Co-operative Credit Societies Act in India – A Unique Experience of Legal Social Engineering

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*(In the context that the Indian Co-operative Movement is celebrating the century of co-operatives in the country, we felt that it is opportune to publish this article – Editor)*

## 1. Introduction

The author is working with legislation based on the Indian Co-operative Credit Societies Act of 1904 for more than 40 years, with first contacts in 1962/63, when meeting former Registrars of Co-operative Societies who had served during Colonial Government, like B. J. Surridge.

Marburg in September 2004 with participation of specialists from 8 countries (Australia, Cameroon, Canada, Finland, Germany, Sweden and the United Kingdom) to discuss the impact of this law on worldwide co-operative development<sup>1</sup>.

The Indian Co-operative Credit Societies Act and the government machinery devised for implementing this legislation became known as the “Classical British-Indian Pattern of Co-operation”<sup>1</sup> (CBIPC). It was tested first in India as experimental legislation, applied in South Asia (Burma/Myanmar, Ceylon/Sri Lanka), spread in Africa in the 1930s<sup>1</sup> and after the second world war it was recommended to the governments of all British dependencies as a Model Ordinance<sup>1</sup>, supplemented by Model Rules<sup>1</sup>. It even influenced the French colonial co-operative decree of 1955<sup>1</sup>. As a model, it became one of the first global laws.

In the following text, co-operatives are seen as social and economic institutions and organisations formed by a group of persons to promote their own economic and social needs by means of a jointly owned, controlled and used enterprise, or as defined in section 4 of the Indian Co-operative Societies Act of 1912:

To commemorate 100 years of the Indian Co-operative Credit Societies Act, a colloquium was held in “a society which has as its object the promotion of the economic interest of its members in accordance with co-operative principles”<sup>1</sup>.

The topic is dealt with in 9 steps. After a short presentation of the Indian Co-operative Credit Societies Act, the concept of state-sponsorship of co-operative societies is explained. The CBIPC is shown as a typical British piece of legislation without codification, with the characteristics of a “development law”, i.e. a law designed to promote development in a planned direction by education of co-operators and encouragement of co-operatives. The law follows a combination of public and private law approach, public law approach because a government machinery for the implementation of the law is created, private law approach because it is left to the citizens to make use of this new form of organisation and to avail themselves of the help, which government offers for its implementation. The Registrar of Co-operative Societies is presented as the special feature and main innovation of the CBIPC, in his original role as development entrepreneur, who always risks to become a supervisor and policeman, rather than to retain his originally intended role as guide, philosopher and friend of co-operators. It is discussed how such role can be played within a general civil service structure. Finally, examples are given how in practice the original design of

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<sup>1</sup> Calvert, H.: The Law and Principles of Co-operation, 5th Edition, Calcutta 1959, 109 f.

the Registrar as promoter and guide has turned into that of an administrator in charge of using co-operatives as instruments of the state for planned development rather than as a promoter encouraging co-operators to form co-operatives as self-help organisations working primarily for their own benefit.

## 2. The Indian Co-operative Credit Societies Act, 1904

The Indian Co-operative Credit Societies Act of 1904 was based on European ideas and experiences in the second half of the 19<sup>th</sup> century, the principles set by Friedrich Wilhelm Raiffeisen for agricultural co-operatives and by the Rochdale Pioneers (influenced by the ideas of Robert Owen) for consumer co-operatives.

Confronted with poverty, indebtedness of farmers, famine and social unrest, the Indian Colonial Government had sent officials to Europe to study, how similar problems had been overcome and one of their recommendations was to “find an Indian Raiffeisen”<sup>2</sup>.

As a programme to introduce co-operatives into India, the CBIPC consisted of promulgating a law and setting up a special government machinery for the implementation of that law: A Co-operative Department headed by a Registrar of Co-operative Societies (RCS).

The law was made to fit into the British legal system. The law-makers were guided by “co-operative principles” (Raiffeisen: self-help, self-administration, self-responsibility; the Rochdale Pioneers’ principles: open and voluntary membership, democratic management and control: one member - one vote, limited return on capital, political neutrality). These co-operative principles were later taken up by the International Co-operative Alliance (established in Manchester in 1895) and are followed by the world co-operative movement in a form last revised in 1995<sup>3</sup> up until today.

## 3. A unique experience of legal social engineering

The CBIPC is a unique experience of legal social engineering for several reasons:

It has been applied in practice in all corners of the former British Empire.

Its application and modification is well documented from its beginnings up to today.

It is a mix of German and international co-operative principles or guidelines and elements of British organisation law moulded in a special design to meet the needs of the rural and urban poor with little knowledge of and access to written law and legal advice.

Following British tradition of law-making, the original Indian law was made on the basis of a report of a commission of enquiry, proposing to follow the Raiffeisen model. The purpose of this law and salient points of its contents were outlined in a detailed statement of objects and reasons<sup>4</sup>, presenting the concept underlying the draft law (bill) and describing the expected results.

The text of the law was based on written and unwritten assumptions. It was not a full codification but rather regulated only such matters considered important, leaving other matters to be governed by common law or specified later in the light of experience gained by practical application. For instance, in the revised version of the Act of 1912, the co-operative principles were mentioned in

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<sup>2</sup> Nicholson, F. A.: Report regarding the possibility of introducing land and agricultural banks into the Madras Presidency, Vol. I Madras 1895, Volume II Madras 1897; Ibbetson, Sir Denzil: Approach to Legislation on Co-operative Credit, 1904 in: National Co-operative Union of India: Anthology of Co-operative Thought, Vol. I, New Delhi 1975, pp. 99-109; Calvert, H. 1959, p. 5; Münkner, Hans-H.: Die Organisation der eingetragenen Genossenschaft in den zum englischen Rechtskreis gehörenden Ländern Schwarzafrikas, dargestellt am Beispiel Ghanas, Marburg 1971, pp. 6 f.

<sup>3</sup> ICA Statement on the Co-operative Identity, Review of International Co-operation, Vol. 88 No. 4, 1995, pp. 85-86.

<sup>4</sup> Report of the committee on the establishment of co-operative credit societies in India 1903; Ibbetson, Sir Denzil: Approach to Legislation on Co-operative Credit, 1904, op. cit.; Calvert 1959, p. 12.

the legal definition of the term “co-operative society”, but intentionally not defined in the law<sup>5</sup>. It was presumed that the co-operative principles were known by those applying the law and room was given for their interpretation according to needs and circumstances in an Indian environment.

The fact that in India at the turn of the 19<sup>th</sup> century already numerous autochthonous self-help organisations existed and on the one hand reflected the indigenous value system but on the other hand were flexible in adjusting to changing needs<sup>6</sup>, was mentioned for instance in a note by F. Nicholson on Madras Loan Funds and reproduced as part of the Report of the Committee on the establishment of co-operative credit societies in India, but not discussed in the law-making process, where this issue appeared to have been ignored or overlooked, possibly in the belief that development meant adjustment to imported values and new institutions were needed to replace the old ones.

#### 4. The Indian Co-operative Credit Societies Act as a “development law”

The Indian Co-operative Credit Societies Act can be classified as a “development law”<sup>7</sup>. It was not a mirror of social and economic reality prevailing in India, regulating the current state of affairs and providing for the resolution of potential conflicts, but rather a law meant to serve as an instrument for achieving or encouraging the achievement of an envisaged (planned) result, namely the formation of rural and urban co-operative societies of the Raiffeisen type, different from existing autochthonous self-help organisations in many ways:

- Co-operatives were meant to facilitate transition from subsistence farming and barter towards a market and money economy,
- The proposed model was based on European values like equality and democracy (one member – one vote), election of office-bearers for a limited term of office and under democratic control (as opposed to decision making by consensus and subtle forms of social control).
- The new law gave government a role in generating social cohesion and stimulating joint socio-economic action with some degree of autonomy and liberalism, while – under colonial government – private group activities with political objectives were strictly controlled or prohibited. However, autonomy of co-operatives was only granted with strict limitations. Later in East Africa, one of the Nordic advisers wrote: “Government wants us to be democratic, but we are left with little to be democratic about”.

During the first years (between 1904 and 1912) the law only allowed primary (local) co-operatives, without the right to federate and to form unions or federations. In 1912, when the law was amended for the first time, the need for co-operatives to form secondary (regional) and tertiary (national) organisations was recognised and authorised<sup>8</sup>.

However, it soon became obvious that viable co-operative societies can only develop, if the environment in which they work is favourable or at least not totally hostile. To make written rules work, people must learn to read and write, to make production of cash crops interesting, there must be access to markets and reasonable prices must be offered. To transport produce to the market

<sup>5</sup> Co-operative Societies Act of 1912, section 4; Report of the committee on the establishment of co-operative credit societies in India 1903, p. 6 No. 5; Münkner 1971, pp. 61 f.

<sup>6</sup> Eden, Ake: Oriental Economic Thoughts and Co-operative Development on the Pre-colonial Indian Subcontinent, in: Münkner, Hans-H. (Ed.): 100 Years Indian Co-operative Credit Societies Act, 1904 – A worldwide applied model of co-operative legislation, Marburg 2004, in print.

<sup>7</sup> For details on „development law“ see for instance Münkner, General Report 1989, pp. 10-12, 102 f.; Münkner, Hans-H.: Law and Development, a new discipline of scientific research and teaching, in: Madlener, Kurt (Ed.): Year Book of African Law, Vol. 4 (1983), pp. 99-109; Münkner, Hans-H.: Practical Problems of Law Reform in Africa – with particular reference to co-operative Law, in: The Plunkett Foundation, Year Book of Agricultural Co-operation, 1982, pp. 61-62.

<sup>8</sup> Co-operative Societies Act, India, 1912, section 4; „a society established with the object of facilitation the operations of such societies“; Münkner, General Report 1989, p. 104.

there must be basic infrastructure. As a proverb suggests: “The lotus never rises above the level of the surrounding waters”.

When making the Indian Co-operative Credit Societies Act, government had no experience with this form of organisation in an Indian environment. The law-makers were aware of the fact that this lack of practical experience was a serious risk<sup>9</sup>.

## 5. The Registrar-System

The approach taken was to offer people access to a new form of organisation, choosing an experimental approach, leaving the RCS and future co-operators to determine, which way to go, without guarantee that the right choice would be made. Some parts of the law were deliberately left vague. Only after gaining experience it was planned to make adjustments of the law and of the methods of its application<sup>10</sup>.

The RCS was given a large margin of discretion for interpretation of the law and choosing his strategy. In a system with flexible rules and wide discretion, much depends on the actors. It is crucial to select and train people of the right calibre and to give them the chance to acquire experience before beginning their work as promoter, advisor or regulator.

The more discretion is given to the holder of a post, the more important it becomes to fill the post with a qualified, experienced and motivated person. When studying the application of the CBIPC over time it became evident that for successful work, the scheme of service for the RCS and staff could be more important than the law they had to apply<sup>11</sup>.

Promoting the development of co-operatives being self-help organisations leads to another general problem of technical assistance: Is aided self-help a viable concept or is it a contradiction in terms to help others to help themselves<sup>12</sup>.

Experience has shown that aided self-help can be successful, but the margin between under-promotion and over-promotion is extremely narrow and varies from case to case. This is another argument for careful selection and training of personnel in charge of promoting self-help organisations or acting as development entrepreneurs.

Sustainable self-help organisations can only develop at their members' own speed. When promoting self-help and enhancing co-operative development from outside, there is no short cut, especially not by offering financial incentives (buy the people).

Sustainable self-help organisations only develop, if they serve the interests of their members. If they are promoted for other purposes, e.g. to organise people under government control, to serve as channels for loans, to control production, to siphon off surplus or as Göran Hydén has put it “to capture an uncaptured peasantry”<sup>13</sup>, voluntary and active participation of members will be the exception rather than the rule.

On the other hand, self-help organisations including co-operatives can develop into lasting and viable institutions, if they enable people, to -

<sup>9</sup> Ibbetson 1904, pp. 101 f.; Calvert 1959, p. 1; Münkner, Hans-H.: New Trends of Co-operative Law in English-speaking Countries of Africa, Institute for Co-operation in Developing Countries, Papers and Reports No. 4, Marburg 1974, pp. 7-8; Münkner, General Report 1989, p. 101.

<sup>10</sup> Ibbetson 1904, pp. 101 f.; Calvert 1959, pp. 7, 12; Münkner 1971, pp. 8, 9, 13.; Münkner, General Report 1989, p. 101.

<sup>11</sup> SurrIDGE, B. J., 1953, pp. 175 f.; Colonial Office: Circular Despatch dated 20th March, 1946, from the Secretary of State for the Colonies to the Colonial Governments, Col. No. 199, London 1946, Enclosure 1, Memorandum on Recruitment and Training of Co-operative Staff.

<sup>12</sup> Münkner, Hans-H.: Consequences of consequent self-help promotion for development policy, in: Hedlund, Hans (Ed.): Co-operatives Revisited, Seminar Proceedings No. 21, Scandinavian Institute of African Studies, London-Ibadan-Nairobi 1980, pp. 187 f., 193; FAO: Strategies for the promotion of self-help organizations of the rural poor, Rome 1992.

<sup>13</sup> Hydén, Göran: Beyond Ujamaa in Tanzania, Underdevelopment and an uncaptured peasantry, Uppsala 1988.

- elect and control their own leaders,
- gain access to knowledge, markets and credit,
- pool resources and to build up countervailing power against traders and financial service providers, and
- initiate processes of mutual learning, knowledge sharing with promoters and innovation at peoples' own speed.

## 6. Contents of the Law

The Indian Co-operative Credit Societies Act has the usual contents of a law governing business organisations<sup>14</sup>:

- Establishment of the regulatory authority (the RCS),
- Formation procedures, requirements for registration and registration,
- Power to make by-laws and necessary contents of the by-laws,
- Membership, acquisition and termination, rights and obligations of members,
- Organisation and management,
- Financing
- Audit, supervision, inquiry,
- Dissolution and liquidation,
- Penal clauses, protection of members and customers/business partners

In case of the Indian Co-operative Credit Societies Act of 1904, the innovation was that the state acted as initiator and promoter of co-operative societies by offering a government machinery for the implementation of the law, not in term of administering the law, but with a RCS as a "development entrepreneur"<sup>15</sup>.

The RCS with his wide discretionary powers has been described as the creator and destroyer of co-operatives or as the very foundation of the movement<sup>16</sup>.

In some countries following the CBIPC the fact that co-operatives were originally initiated by government during colonial times has been a negative birthmark up until today.

## 7. Special Features of the RCS

The RCS was perceived as a high ranking officer, recruited for a term of office of five or more years after having undergone special training and having gained experience with co-operative work by visiting co-operative organisations in other countries<sup>17</sup>.

Unlike ordinary government departments, the co-operative department under the RCS was called upon to work by persuasion and to mobilise voluntary co-operation. Originally, the RCS had no

<sup>14</sup> Münkner, General Report 1989, pp. 111 f.

<sup>15</sup> Münkner, General Report 1989, p. 103; On „development entrepreneurs“ see Röpke, Jochen: Co-operative entrepreneurship, Marburg Consult for Self-help Promotion, Series A 7, Marburg 1992, pp. 75 f.: Catalytic Entrepreneurs; Münkner, General Report 1989, pp. 87 f.

<sup>16</sup> Madane, Madhav V.: Patterns of Future Relationship between the Government and the Cooperative Movement, in: International Co-operative Alliance, State and Co-operative Development, New Delhi 1971, p. 66; Calvert 1959, p. 105.

<sup>17</sup> Ibbetson 1903, pp. 107; Calvert 1959, p. 108, footnote 1; Colonial Office, Despatch dated 20<sup>th</sup> March 1946, pp. 4 f., Enclosure 1 Memorandum on recruitment and training of co-operative staff.

power to coerce or to punish. His task and the task of his staff was to open access to a new legal framework and to new economic group activities by offering information, education and advice<sup>18</sup>.

The law gave the RCS some skeleton powers: To register new societies, to audit existing societies, to carry out enquiries in case of irregularities discovered during the course of audit, to dissolve and liquidate societies either on demand of co-operators or ex-officio and to settle disputes within and among co-operatives, touching the business of a co-operative society (excluding access to court)<sup>19</sup>.

In addition, the RCS had the overall responsibility for sound development of co-operatives. For this purpose he developed non-statutory powers<sup>20</sup> supplementing his statutory powers, implied and deemed to be covered by the law. The most important non-statutory powers were to carry out inspections outside audit (surprise inspections, routine inspections), to attend meetings of co-operatives and to influence the agenda, to make potentially dangerous decisions of co-operative office-bearers subject to his prior approval and to remove unfit officers.

After some time, many of these extraordinary non-statutory powers of the RCS and his staff (meant to be used only in extraordinary circumstances) became routine, were written into the co-operative law and turned into statutory powers.<sup>21</sup>

## 8. Pros and cons of a special scheme of service

The functions of “development entrepreneur” did not fit into the career structure of the civil service, in which promotion depended on age and years of service, and usually meant to be promoted from positions as fieldworkers to office and paper work. In a closed department<sup>22</sup>, i.e. a department of a specialised ministry requiring special training and skills from its officers, promotion within the department depended on vacancies. In a small closed department this meant few or no chances of promotion within reasonable time.

To have a well trained, experienced and motivated team of co-operative fieldworkers and to retain them in service, new methods had to be developed and a special scheme of service had to be developed (against the objections of the Public Service Commission) to prevent young and dynamic field workers from leaving the co-operative department in search of greener pastures. It had to be avoided that co-operative departments turned into a reservoir of low graded and low paid inspectors or even sub-inspectors (Pakistan), who had to work during odd hours, travel on local transport to remote areas, sleep in villages and stay far from their families – and were still expected to remain enthusiastic co-operative promoters<sup>23</sup>.

The mechanism of ordinary public service, which usually allows to promote a good fieldworker by transferring him/her to the head office and making him/her an office worker in charge of paper

<sup>18</sup> Calvert 1959, pp. 106 f.; Münkner 1971, pp. 7 f., 218 f.; Münkner, General Report, 1989, p. 103.

<sup>19</sup> Münkner 1971, pp. 8 f.

<sup>20</sup> Münkner 1974, pp. 9 f.

<sup>21</sup> E.g. in the case of Malaysia, of which Soedjono, Ibnoe and Cordero, Mariano in their Critical Study on Co-operative Legislation and Competitive Strength, ICA Regional Office for Asia and the Pacific, New Delhi 1997, p. 54, say that the Registrar has too much power that encroaches on the autonomy of co-operatives, i.e.: Compulsory amendment of by-laws (section 10A, Co-op. Soc. Act, 1948, added by section 10 the Co-op. Soc. (Amendment and Extension) Act, 1976); calling of general meetings (rule 11 Co-op. Soc. Rules 1949); power of government officers to attend meetings of registered co-operative societies (section 11A Co-op. Soc. Act 1948); rescission of decisions of general meetings (rule 28 Co-op. Soc. Rules 1949); dismissal of unfit officers (section 37A (6), Co-op. Soc. Act 1948, amended by section 23 the Co-op. Soc. (Amendment and Extension) Act, 1976); Removal of committee/board of a registered society and appointment of a caretaker committee or administrator (section 37 A Co-op. Soc. Act 1948); suspension of activities of registered society (section 37 A (1) (a) Co-op. Soc. Act 1948).

<sup>22</sup> See Münkner General Report 1989, pp. 87 f.

<sup>23</sup> Cf. Hydén, Göran: Efficiency versus Distribution in East African Co-operatives, a study of organisational conflicts, Nairobi-Kampala-Dar es Salaam 1973, pp. 148 f.; Münkner, Hans-H.: Problems of Co-operative Management in Africa, in: ILO Co-operative Information 3/77, pp. 41-58.

work, did not encourage good fieldwork as a life career. The payment schedules of civil service did not allow to raise the pay for successful fieldworkers on the job apart from “field allowances”. What would have been needed to keep good fieldworkers in the field – payment in accordance to performance and to the difficulty of the task - was against civil service rules.

Without career prospects and incentive pay, it was easy to become a frustrated administrator, using his/her powers as a representative of the state to have things done rather than to become a dynamic promoter of self-help organisations, acting as guide, philosopher and friend of co-operators, helping people to help themselves, protecting them against unfair practices and unfair competition.

Experience has shown that the Registrar-system only works, if the RCS -

- is an experienced specialist in promoting development,
- has a relatively independent position outside the common hierarchy of the civil service, as far as his professional work is concerned,
- is not obliged to pursue a political agenda and
- is not directly involved in matters of indoor management of co-operative societies he is supposed to guide.

Furthermore, co-operative officers doing field work have to be well trained, convinced of the importance of their task, highly motivated and with room for own initiatives. Without reasonable pay and career prospects the best officers may leave and the remaining staff will be a negative selection of persons accepting the bad service conditions because they have no alternatives<sup>24</sup>.

If the RCS and his staff interfere with the organisation and management of societies under their supervision, e.g. by implementing government programs or by insisting that advice be followed, their neutrality as advisers, auditors and arbitrators is lost. In this case, advice becomes an order. Where the RCS is called upon to settle a dispute arising from acts done according to advice given by co-operative officers, the RCS would practically be a party to the dispute and it would be a misnomer to call such proceedings arbitration proceedings.

All these preconditions for the functioning of the Registrar-System were contained in the original statement of objects and reasons when presenting the Bill in 1904 to the Indian legislative assembly<sup>25</sup>. However, regarding the law, these assumptions remained unwritten, were often ignored and finally forgotten.

In the following it will be shown how the special mission of the RCS as development entrepreneur gradually turned into that of an ordinary administrator, and how his statutory powers in dealing with co-operatives increased and his work was approximated to that of ordinary civil servants.

## 9. From state-sponsorship to state-control

Out of the many examples that could be quoted to demonstrate this trend from state-sponsorship to state-control, some amendments of the original Indian Co-operative Credit Societies Act of 1904 will be discussed with regard to five issues:

- Formation of co-operatives,
- Autonomy to make by-laws,
- Organisation and management,
- Financing and
- Auditing

<sup>24</sup> Strickland, in *International Labour Review* of 1938, quoted by Surrige, J. B. 1952, pp. 175, 176 on neglecting the training of co-operative department staff: “the ignorant had been sent to lead the ignorant, the blind to guide the blind and the result has naturally been disastrous”.

<sup>25</sup> Ibbetson 1904, pp. 101 f.; Münkner, *General Report* 1989, pp. 101 f.

### 9.1. Formation of co-operatives,

Originally, the RCS had full autonomy to decide whether a new society should be registered or not. “The Registrar may, if he thinks fit, register the society and its by-laws”<sup>26</sup>.

Except for a prescribed minimum number of members (10), it was left to the RCS with his expert knowledge to define the conditions to be met before registration.

This vast margin of discretion gave the RCS the necessary flexibility to react to conditions and circumstances. But it also opened venues for political interference and manipulations. The RCS could be ordered by politicians or high ranking government officials to register societies for convenience, even if the requirements were not met.

Later, in the light of experience, formation procedures and conditions to be met before registration were written into the law, e.g. conduct of a socio-economic survey by co-operative officers or co-operative federations, submission of a feasibility study or a trial balance for the first year<sup>27</sup>.

In East Africa in the 1960s, provisional registration was introduced. It was meant to provide a learner phase for new co-operatives, which had to prove their viability during a probation period of one or two years before full registration<sup>28</sup>.

### 9.2. By-laws

Originally, the members were given the task and autonomy to make the by-laws of their society, if necessary, with the help of co-operative officers. The law prescribed the minimum contents of the by-laws and a list of matters to be regulated in the Rules made under the Act<sup>29</sup>. As Calvert puts it: “The Act itself does not empower a society to make by-laws. It must have them before it is registered”<sup>30</sup>. The RCS had to make sure that the by-laws were not contrary to the Act and the Rules<sup>31</sup>.

The local government (later the Minister) in charge of co-operative development could use the powers given under the law to make regulations for the application of the law to regulate in detail what societies should have in their by-laws. In this way, the executive took away the autonomy given to co-operators by the law-makers and left co-operators to repeat in the by-laws, what was laid down as necessary contents in the rules or regulations made under the law. The main purpose of granting autonomy to make by-laws, namely to empower co-operators adjust the general provisions of the law to the special needs of the individual society and to give people the feeling that they were working according to their own rules, was defeated.

The next step was to prescribe that model by-laws made by the RCS or by co-operative federations had to be adopted by the societies as a requirement before registration<sup>32</sup>. In this way, only very few issues of the by-laws were left to be decided by the individual society and all had to follow uniform rules. The power of the RCS to amend the by-laws of registered co-operative societies ex-officio, if

<sup>26</sup> Co-operative Credit Societies Act, India, 1904, sections 6 (2) and 8 (3); Calvert 1959, pp. 101, 131 f.

<sup>27</sup> For Tanzania and Zambia see Münkner, Hans-H.: The Legal Status of Pre-Co-operatives, Friedrich-Ebert-Stiftung, Bonn 1979, pp. 60 f.

<sup>28</sup> Münkner 1974, pp. 18 f.; Münkner 1979, pp. 38 f.

<sup>29</sup> Co-operative Credit Societies Act, India, 1904, section 27 (2) (k); Calvert 1959, p. 132: The Registrar must approve before registration, he is practically given power to impose model by-laws.

<sup>30</sup> Calvert 1959, p. 101.

<sup>31</sup> Co-operative Societies Act, India 1912, section 9.

<sup>32</sup> As prescribed under the Co-operative Law of Saskatchewan, cf. SurrIDGE 1952, p. 176. The new Co-operative Societies Act of Fiji, 1996, contains model by-laws as a schedule to the Act under section 17.



the co-operatives failed to do so on their own<sup>33</sup> was the next step of increasing government control over co-operative societies.

The substance of freedom of association with self-determined rules was lost.

### 9.3 Organisation and Management

Following the rules governing the British legal system, the original Co-operative Credit Societies Act only mentioned some key points regarding the organisational structure of co-operative societies to be governed by regulations made under the Act, however, without going into detail<sup>34</sup>:

- That members in general meeting constitute the supreme authority,
- how to convene a general meeting,
- the need to have a management committee or board of directors and to elect office-bearers from among the members for a term of office.

Some issues were regulated, others (e.g. the liability of board members) were not. According to the rules of the British legal system at that time, the distribution of powers between members and office-bearers and their obligations should have been left to be decided by the members in the by-laws or ad hoc according to the unwritten principles of the law of agency<sup>35</sup>. It would have been an ideal arrangement to organise the distribution of decision-making powers within co-operatives according to the needs of the individual society, if members would have been conversant with the law of agency and if they would have had access to legal advice. Both was not the case.

In practice, the executive stepped in: The regulations made under the law or model by-laws contained an almost full codification of rights and obligations of the members, their elected leaders and appointed managers, which could only be repeated in the by-laws and supplemented where necessary.

Problems of officialisation arose, when the co-operative officers in charge for the proper functioning of the co-operatives under their supervision were not satisfied with the persons elected by the members to serve as office-bearers, or with decisions taken by members or their elected representatives or their employed staff.

Initially, co-operative department staff interfered in order to have other persons elected or appointed or to have decisions corrected, which they considered to be wrong. The co-operative officers saw such (exceptional) interventions as part of their non-statutory powers resulting from their overall responsibility for the well being of “their” co-operatives<sup>36</sup>.

Later, in many countries following the CBIPC, these powers became statutory powers and interference of government officers in matters of indoor management of co-operatives became routine, certain potentially dangerous decisions (e.g. investment of funds) could only be taken after approval of the co-operative officer in charge. Where the RCS was of the opinion that the board members of a co-operative society were unable to run the business properly, he could order dismissal of the board members by the society or dismiss them ex-officio and appoint a care-taker committee or second a co-operative officer to take over the management of the society<sup>37</sup>.

<sup>33</sup> E.g. Co-operative Societies Act of Malaysia, 1948, section 10A, Co-operative Societies Rules of Malaysia, 1949, Rule 11; Co-operative Societies Amendment and Extension Act, Malaysia 1976, section 10A.

<sup>34</sup> These matters had to be contained in the by-laws, Co-operative Credit Societies Act, India, 1904, section 27 (2) (i) and (j). They were already dealt with in detail in the Model Co-operative Societies Rules, Colonial Office, Enclosure to Circular Despatch dated April 23, 1946, Rules 21-41.

<sup>35</sup> Cf. Münkner 1971, pp. 65 f.; Münkner, General Report 1989, p. 117 f.

<sup>36</sup> Münkner, General Report 1989, pp. 118 f.

<sup>37</sup> See quotations from Malaysian Co-operative Societies Acts and Rules supra in note 27. See also Münkner 1974, pp. 15 f.

#### 9.4. Financing

From the very beginning it was clear that co-operatives would be formed mainly by persons of limited means and that there should be no impediments for the formation of societies by requiring a certain minimum initial capital<sup>38</sup>.

It was also clear that co-operatives should have a special tax regime as an incentive to form this new type of organisation<sup>39</sup>.

The law prescribed shares, entry fees and fines as sources of own capital and initially prescribed unlimited liability of the members for the debts of their society for rural societies and limited liability for urban societies<sup>40</sup>. The law remained silent on the need of building up reserves from undistributed surplus.

From the very beginning the question was discussed, whether co-operatives should be promoted with government funds<sup>41</sup>.

Creating artificial incentives by offering access to easy money from government or (later) development aid, was generally seen as dangerous. Laidlaw strongly objected to financial support by the state: "Government money is the kiss of death to co-operatives"<sup>42</sup>. The arguments were and still are that external funds (cold money) will serve as a disincentive to raise own capital (socially controlled money) and will destroy the co-operators' sense of ownership<sup>43</sup>.

Yet, the laws based on the CBIPC provided for access to government money, introduced provisions governing control of government funds in co-operatives, using government money in co-operatives as a reason for introducing strict supervisory powers of government, according to the proverb saying "He who pays the piper can call the tune".

In India, new forms of government participation in financing co-operatives were entered into the law: The state partnership fund<sup>44</sup>.

#### 9.5. Audit

Co-operatives are group enterprises carrying out economic activities and participating in the market. They are usually run by people without much business experience. Therefore, there is need for internal and external audit, to discover mistakes and to protect members, creditors and the public.

Initially, the Indian Co-operative Credit Societies Act provided for external audit along the lines of Raiffeisen's co-operatives, i.e. audit by specially trained co-operative auditors of the Co-operative Department<sup>45</sup> or later of a co-operative federation. In addition, provisions were made for a special audit (inquiry) in case of irregularities discovered during audit. Originally, inspection outside audit was not a statutory function of the RCS but was carried out as a non-statutory function when

<sup>38</sup> Committee on the establishment of co-operative credit societies in India, 1903, pp. 6 and 7, No. 7.

<sup>39</sup> Committee on the establishment of co-operative credit societies in India 1903, p. 7 No. 10, Co-operative Credit Societies Act, India, 1904, section 25.

<sup>40</sup> Committee on the establishment of co-operative credit societies in India 1903, p. 7 No. 10, Co-operative Credit Societies Act, India, 1904, section 7.

<sup>41</sup> Ibbetson 1904, p. 108.

<sup>42</sup> Laidlaw, Alex: Report of the Royal Commission on the Co-operative Movement in Ceylon, pp. 108,109.

<sup>43</sup> See Balkenhol, Bernd (Ed.): Credit Unions and the poverty challenge, extending outreach, enhancing sustainability, ILO Genf, 1999, pp. 8 f, 11.

<sup>44</sup> Maharashtra Co-operative Societies Act, Act No. 24 of 1960, sections 50-59; Vidwans, M. D.: The Maharashtra Co-operative Societies Act 1960, Text and Commentary, Bombay 1962, pp. 90 f.

<sup>45</sup> Surridge 1953, p. 176; Münkner, Ten Lectures on Co-operative Law, Friedrich-Ebert-Stiftung Bonn 1982, pp. 107 f., 117.

necessary. Later, inspection of co-operatives by co-operative officers became routine and was added to the growing list of statutory powers<sup>46</sup>.

Co-operative audit differs from company audit in so far as not only the annual reports, balance sheet and profit and loss accounts are audited, but also “performance audit” has to be carried out, i.e. assessment of the quality of management in pursuing the objects of the society<sup>47</sup>.

Special problems arise when most of the members and even office-bearers of co-operatives are illiterate and managers have to be assisted by co-operative officers to keep the books, which the officer later has to audit<sup>48</sup>.

Other problems arise, when co-operative officers influence decisions taken by co-operatives by giving advice or refusing approval to certain activities and officers of the same department are auditing the results achieved by such “supervised” co-operatives. To maintain the neutrality of the auditor, it becomes necessary to separate the government agency in charge of promoting and supervising co-operatives from the agency carrying out the audit. This was proposed already in 1966 by the Afro-Asian Rural Reconstruction Organisation (AARRO)<sup>49</sup> but not generally implemented. Only Thailand has separate government services for promotion and audit of co-operatives<sup>50</sup>.

Finally, if government provides co-operative audit (often of debatable quality and with much delay) free of charge, it becomes difficult, if not impossible, for co-operative federations to build up their own audit service, for which fees have to be charged.

Here the problem of phasing out government involvement and phasing in co-operative self-regulation becomes visible. To avoid such development, the Model Co-operative Societies Rules under the Model Co-operative Societies Ordinance proposed by the Colonial Office in 1946 contained provisions for establishing a co-operative audit and supervision fund<sup>51</sup> from which audit services by co-operative federations could be paid. This idea was developed further in Singapore where a Central Co-operative Fund was introduced in 1979, accumulated from annual contributions by co-operatives and used among other things to finance co-operative audit by the Singapore National Co-operative Federation (SNCF)<sup>52</sup>. In their Critical Study on Co-operative Legislation and Competitive Strength, Soedjono and Cordero recommended this approach for the whole region. “A ‘co-operative taxation scheme’ similar to the Singapore model is highly recommended to ensure a sustainable and self-financing Co-operative Development Fund”<sup>53</sup>.

## 10. Conclusions

After 100 years of practical application, the CBIPC allows to assess its viability, to define the conditions of its successful application and the reasons for failure.

<sup>46</sup> E.g. section 47, Co-operative Societies Ordinance of Nigeria 1935 (No. 39 of 1935); Colonial Office: section 36 Model Co-operative Societies Ordinance 1946; Münkner 1974, pp. 10 f.; Indian Co-operative Union: Co-operative Law Part II, New Delhi 1960, p. 32: “In India the Registrars have made a custom of inspecting co-operative societies, a practice which was not intended by the Co-operative Societies Act of 1912.

<sup>47</sup> Cf. Münkner, Ten Lectures 1982, pp. 107 f.

<sup>48</sup> Münkner, Ten Lectures 1982, pp. 117, 18.

<sup>49</sup> Münkner, 1974, pp. 36 f.; Afro Asian Rural Reconstruction Conference, Nairobi 1966: Background papers ARRC-II-RC-1 (b), Co-operative Law, Subject I, Co-operative Legislation.

<sup>50</sup> Soedjono, Ibnoe et al. 1997, pp. 84 f.

<sup>51</sup> Colonial Office, Model Co-operative Societies Ordinance, enclosure 2 to the Circular despatch dated March 20, 1946 from the Secretary for the Colonies to the Colonial Governments, section .

<sup>52</sup> Co-operative Societies Act, Singapore, Act No. 24 of 1979, sections 71 and 72 and Co-operative Societies Rules, Singapore 1979, No. 278; Soedjono et al. 1997 p. 24.

<sup>53</sup> Soedjono, Ibnoe et al. 1997, p. 24.

There is good reason to believe that the model works when applied in its pure form, i.e. meeting all requirements laid down in the statement of objects and reasons when Sir Denzil Ibbetson presented the Co-operative Credit Societies Bill in 1904 to the Indian Legislative Assembly. In its original form, Co-operative Credit Societies Act of 1904 showed many elements of a good “development law”<sup>54</sup>:

*Experimental and flexible*, easily adjusted to needs and circumstances as found out in the course of practical experience.

*Oriented strongly towards human resources development* with the initiative of spreading a new model of organisation originating from government, using the RCS as a “development entrepreneur” rather than as an administrative officer or policeman.

*Working by persuasion, information and advice* without power to coerce and punish.

*Opting for temporary state-sponsorship*, building up local organisations with the intention of phasing out government’s involvement as soon as people learned to stand on their own feet and had built their own institutions ready to phase in.

*Allowing people to learn by making their own mistakes*, giving them autonomy of self-regulation and self-responsibility rather than opting for tight supervision to avoid mistakes and risking failure of the experiment, by acting according to the slogan “to prevent is better than to cure”.

Unfortunately, most of the features giving the CBIPC its special character were forgotten and lost when the application of the model spread and became routine. RCSs turned into common users with little or no knowledge of co-operative matters, who filled the post of RCS as one of many steps in their career as civil servants, instead of being highly specialised and experienced development entrepreneurs, serving a lifetime in this capacity<sup>55</sup>. RCSs were appointed for political reasons and given the task to use co-operatives as instruments for the implementation of political programs (e.g. in Ghana 1966<sup>56</sup> or in Tanzania 1976<sup>57</sup>) or as tools for carrying out development schemes, trying to meet unrealistic goals set by government or political deadlines. As a career post within civil service structure, new promotion opportunities or career steps were invented: Registrar, Joint Registrar, Chief Registrar, Director or Commissioner for Co-operative Development<sup>58</sup>.

When the co-operative movement spread, the Co-operative Departments tended to spread as well, rather than helping co-operatives to build up their own federations and services and to phase out as soon as co-operatives were capable of phasing in. It turned out to be unrealistic to ask a Co-operative Department to work itself out of its business and to shrink rather than to expand. Singapore is one of the few cases where the Co-operative Department turned into a registry and where the staff of the Registrar of Co-operative Societies was reduced to two (down from 46 in the 1980s), while the co-operative federation (SNCF) took over most of the former RCS’s work.

In some countries of Asia, co-operatives have spread but at the same time co-operative departments have grown into huge bureaucracies (e.g. India, Malaysia). The originally flexible laws with much room for the co-operative societies’ autonomy have turned into voluminous codifications

<sup>54</sup> Münkner, General Report 1989, pp. 10 f.

<sup>55</sup> Ibbetson 1904, p. 107; Calvert 1959, pp. 105 f.; Strickland 1933, pp. 72 f.; Rhodes, Rita: Colonial Co-operatives through the Eyes of their Co-operative Registrars, in: Münkner, Hans-H. (Ed.): 100 Years Indian Co-operative Credit Societies Act, 1904 – A worldwide applied model of co-operative legislation, Marburg 2004, in print.

<sup>56</sup> Cf. Münkner 1971, pp. 39 f.; Obuobi, Jeremy: Comparative Study of the Relevant Law on Co-operative Societies and Other Self-help Organizations in Ghana, in International Association of Legal Science, Paris: Comparative Study of Co-operative Law in Africa, Marburg 1989, pp. 273-346 pp. 278, 279, 309 f.

<sup>57</sup> Mporogomyi, Kilonsi: Co-operatives and Development in Tanzania: Theory and Evidence of lost Opportunities, in Hedlund, Hans (Ed.): Co-operatives Revisited, Uppsala 1988, pp. 71 f.

<sup>58</sup> E.g. in India and Malaysia.

supplemented by lengthy regulations, containing provisions for every detail and long lists of statutory powers of government officers controlling co-operatives<sup>59</sup>.

However, during the past several years it has been rediscovered that co-operatives perform best, when left alone to work according to their own rules. In India in 1984 and 2002 new multi-state co-operative legislation for autonomous co-operatives has been promulgated, which co-operatives can choose if they opt for working without government support and without government control.

The long title of the Indian Multi-State Co-operative Societies Act, 2002<sup>60</sup> outlines this new trend to come back to the old approach:

*“An Act to consolidate and amend the law relating to co-operative societies, with objects not confined to one State and serving the interests of members in more than one State, to facilitate the voluntary formation and democratic functioning of co-operatives as people’s institutions based on self-help and mutual aid and to enable them to promote their economic and social betterment and to provide functional autonomy and for matters connected therewith or incidental thereto.”*

Recently, some countries with co-operative laws based on the CBIPC (Fiji, 1996<sup>61</sup> and Namibia, 1996<sup>62</sup>) have gone back to the roots, promulgating laws for aided self-help rather than for state-controlled co-operatives, weeding out many of government’s statutory powers that had crept into the law over the years.

To sum up it can be said that the transfer of co-operative principles from Europe to India and other parts of the world has worked, if –

- the legal environment was conducive,
- capable, motivated and experienced “development entrepreneurs” were at work and
- people were allowed to develop their organisations at their own speed, to learn by making their own mistakes and to co-operate in order to meet their own needs.

Legal social engineering was successful when applied according to the rules mentioned earlier in this report. It is easy to see that success of legal social engineering depends to a large extent on the qualification and motivation of the engineers. Asia, where this model of state-sponsored co-operation was initiated 100 years ago, has become the fastest growing co-operative region and there are good reasons to believe that this trend will continue.

Co-operative self-help organisations have been rediscovered<sup>63</sup> by the international community (UN Guidelines, 2001<sup>64</sup>; ILO Recommendation 193, 2002<sup>65</sup>) as suitable models for coping with change, as a viable alternative to multinational conglomerates and their search for increasing shareholder value. If focussed on their members and on generating “membership value”, they have the potential of developing into modern local and global networks, serving to meet human needs and securing sustainable development.

<sup>59</sup> Cf. examples given supra in note 27.

<sup>60</sup> Multi-State Co-operative Societies Act, 2002, Act No. 39 of 2002.

<sup>61</sup> Co-operative Societies Act, Fiji, 1996, Act No. 16 of 1996.

<sup>62</sup> Co-operative Societies Act, Namibia 1996, Act No. 23 of 1996.

<sup>63</sup> Cf. Münkner, Hans-H.: Rediscovery of Co-operatives in Development Policy, in: International Co-operative Alliance, Regional Office for Asia and the Pacific, Coop Dialogue, Vol. 10 No. 1, January 2000, pp. 8-13; Birchall, Johnston: Rediscovering the Co-operative Advantage, poverty reduction through self-help, ILO Geneva 2003.

<sup>64</sup> UN General Assembly, Economic and Social Committee, Co-operatives in Social Development, Report of the Secretary General, A/56/73-E/2001/68, General Assembly, Fifty-Sixth Session, Item 121 of the preliminary list, 01-37539 (E) 280501; United Nations, Resolution adopted by the General Assembly Fifty-sixth session, Agenda item 108 (on the Report of the Third Committee (A/56/572)), 18 January 2002; A/RES/56/14 “Guidelines aimed at creating a supportive environment for the development of co-operatives, December 2001, <http://www.un.org/documents/ecosoc/docs/2001/e2001-68.pfd>

<sup>65</sup> International Labour Conference, Recommendation 193, Promotion of Co-operatives, Geneva, 2002.



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