

# “THE COOPERATIVE ENTERPRISE AS A PRACTICAL OPTION FOR THE FORMALIZATION OF INFORMAL ECONOMY”

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## 1. Nature of the Cooperative Model of Enterprise

Working together is the underlying principle on which cooperative movement is based. A cooperative is defined as *an autonomous association of persons united voluntarily to meet their common economic, social, and cultural needs and aspirations through a jointly owned and democratically controlled enterprise.*<sup>1</sup>

Cooperatives are therefore business enterprises. They are referred to as *social enterprises* – i.e. they have the specific feature of producing goods, services and knowledge while pursuing both economic and social aims and fostering solidarity. They are governed by a set of principles which are:

*Voluntary and open membership; Democratic member control (one member-one vote); Member economic participation; Autonomy and Independence; Education, training and information; Cooperation among cooperatives and Concern for the Community. Co-operatives are based on the values of self-help, self-responsibility, democracy, equality, equity, and solidarity. In the tradition of their founders, co-operative members believe in the ethical values of honesty, openness (transparency), social responsibility, and caring for others.*<sup>2</sup>

Cooperatives have unique advantages based on the special relationship they have with their members. They have the power to bulk up demand and purchase supply at cheaper prices than their competitors.

From a legal point of view they are formal, legally constituted organizations – which means they enjoy legal recognition, and protection, can enter into contracts, own or dispose of property, sue or be sued and operate as corporate bodies with perpetual succession.

Cooperatives are found in practically all types of enterprise: *Agricultural supply and marketing cooperatives* organize bulk purchase and supply farm inputs to their farmer-members and, at the same time organize the collection and marketing of their members' produce. *Consumers cooperatives* operate retail stores where the members (owners) are at the same time the customers; *Cooperative banks and* ,

*Savings and credit cooperatives (SACCOS)* provide savings and lending facilities to their members while *Insurance Cooperatives* provide insurance services; there are also transport cooperatives (for commercial vehicle owners or consumers of the transport service). And then there are construction, housing, manufacturing, catering, entertainment, tourism, fishing, ranching, livestock marketing, and handicraft and health services cooperatives. Workers' cooperatives run enterprises in which the workers are at the same time the owners. Labour contracting cooperatives are formed by workers (skilled or unskilled) who are organized and hire out their labour (e.g. for cargo handling, construction work; farm work, garbage collection, office cleaning; shared service cooperatives (formed by entrepreneurs - micro-small, medium or large) to provide common services.

There are cooperatives in practically all countries of the world and they constitute a global movement with more than 850 million individual members. They employ over 100 million people. In Sub-Saharan Africa there are more than 150,000 cooperatives, with membership running to scores of million individuals. Cooperatives provide direct employment to between 0.5% - 1.3% of the total labour force while indirect employment is much higher.

Recent studies have established conclusively that in times of economic crises, such as the recent Global Financial Crisis, cooperatives have shown more resilience than other types of enterprise. Research<sup>3</sup> indicates that (i) risks have been diluted when there is a broad membership base; (ii) SACCOs tend to invest in less risky types of activities for the core objective of cooperatives is to serve members' long term interests and needs and (iii) African cooperatives are usually organized with an inclusive objective of reaching out to the poor, and in particular women and youth. Furthermore analysis<sup>4</sup> provides evidence that cooperatives worldwide do fare better than other types of enterprise and can be looked at as an interesting alternative business model that focuses on risk-averse investment, strong commitment to social responsibility as well as confidence in providing lowest rates/fees to their members. As one of the pillars of the social and solidarity economy, the cooperative sector offers an alternative and sound way of doing "value-based" businesses.

In the past cooperatives encountered many problems which at times compromised their credibility. These were mostly attributed to excessive government control and undue interference. At times they were given monopoly over certain business activities and generally spoon-fed. During the past two decades, however, cooperatives have undergone, and are still undergoing, drastic reforms in their organization and management. Of particular importance are the reforms made on cooperative policy and legislation so as to provide a more conducive environment for cooperative development to the extent that

today they are increasingly becoming more democratic, more autonomous and independent, and more responsive to their members needs and concerns. They are also becoming a more relevant and attractive option for the formalization of the informal economy.

Today cooperatives globally are considered important instruments for development. The World Bank is advocating the cooperative form of enterprise as an option for effective agricultural development and acknowledges the contribution of cooperatives in providing options for producers to organize, have voice and improve their livelihoods<sup>5</sup>

In the words of ILO Director-General, Juan Somavia,

*“Cooperatives empower people by enabling even the poorest segments of the population to participate in economic progress; they create job opportunities for those who have skills but little or no capital; and they provide protection by organizing mutual help in communities”*

Former UN Secretary General, Kofi Anan had this to say about cooperatives:

*“The cooperative movement is one of the largest organized segments of civil society, and plays a crucial role across a wide spectrum of human aspiration and need. Cooperatives provide vital health, housing and banking services; they promote education and gender equality; they protect the environment and worker’ rights. Through these and a range of other activities, they help people in more than a hundred countries better their lives and those in the communities”*

Such is the key role of cooperatives that the United Nations has designated the year 2012 as the *International Year of Cooperatives*.

## **2. Cooperatives and the Informal Economy**

Workers in the informal economy are mostly involved in micro and small enterprises. In the majority of cases they are unprotected and have no formal recognition. They operate as individuals or in small groups, have no access to financial services, nor do they have representation or voice. They are susceptible to all kinds of risks and their transition from informality to formality is slow and dreary.

On its part cooperative model is ideal for self employed people in small enterprises - including those operated by informal economy workers. The table below shows how cooperatives are relevant to workers in the informal economy and how they can provide solution to the problems discussed above

COOPERATIVE CHARACTERISTICS	RELEVANCE TO INFORMAL ECONOMY
<p><b>They stand for strength through unity</b>  <i>(United we stand, divided we fall)</i></p>	<p>Informal economy workers in the same business line often work individually or in small groups and, quite often, compete with each other. By forming and using the services of a cooperative they forge solidarity, have voice and can consolidate and strengthen their businesses - for example through bulk purchases of the commodities they deal in. Or in defending their rights. The cooperative model also helps achieve economies of scale.</p>
<p><b>Legal status:</b> The registration of a cooperative renders it a corporate body with power to enter into contracts, own property or dispose of it, sue or be sued and operate as a legal entity. They have registered and recognized premises where they operate and can be contacted</p>	<p>Almost invariably informal economy workers have no legal status. It is thus difficult for them, as enterprises to access loans from banks, enter into legal business contracts or own immovable assets as an enterprise. In short they have no legal recognition or protection. .</p>
<p><b>Voluntary and open membership.</b> Anyone who can use a co-operative's services should be free to join. In a retail co-operative, any customer is entitled to become a member and enjoy the benefits of the co-operative. In a worker co-operative, any permanent employee in the co-operative is entitled to join. In a producer co-operative for example marketing craft products any maker of local crafts can. No one is barred from membership in a cooperative on the grounds of race, tribe, nationality, religion, status in the community, or other 'artificial' restrictions</p>	<p>As a small-scale entrepreneur it is not always easy to be accepted in a group of informal entrepreneurs. Groups are sometimes too protective or selfish to accept new members even where they could have helped strengthen the group enterprise. With an entrepreneurs' cooperative anyone can join as long as s/he agrees to comply with the by-laws (constitution) of the cooperative</p>
<p><b>Democratic member control:</b> Cooperatives have elaborate</p>	<p>Sometimes informal economy workers organized in groups break up for lack of</p>

<p>procedures for decision making in which decisions are made by members in a democratic manner. The members are the supreme authority in a cooperative</p>	<p>proper democratic practices. Some become more domineering than others; at times major decisions are made by a small clique within the group without any consultations with the larger group. There will be no such behavior if members are organized in a cooperative</p>
<p><b>Autonomy and independence</b> Co-operatives are autonomous and independent institutions that should work without any interference from government, politicians, or other external parties. Because they value their autonomy and independence, they have strict rules about shareholding and profit. They do not want to be taken over by outside investors.</p>	<p>Informal economy workers are often susceptible to interference by the authorities (and even other entrepreneurs) for one excuse or another - or for no reason at all... Quite often they are harassed by city or municipal authorities for lack of voice.</p>
<p><b>Education, Training and Information:</b> In principle cooperative education and training starts during the formation stages of a cooperative and continues to be provided as a regular feature in the activities of a cooperative. In this way cooperatives can be very useful in developing skills and resources of people with little or no skills as well as those who are relatively disadvantaged. Members can learn how to pool their resources and how to help one another set up a commonly-owned business so that together they can meet needs, which they couldn't meet on their own because it would be too difficult or expensive.</p>	<p>Entrepreneurs - small or large - need education and training in business knowledge and entrepreneurship in order to cope as modern business people and to survive in a globalized business environment. They also need regular business information - e.g. on markets, financial services, new products, processes and systems. The opportunities created through education and skill development can create opportunities for people already in the informal sector, or those with potential to join. Equally important, it is an effective tool for the transition from informal to formal economy</p>
<p><b>Self-help and control over members' economic affairs.</b></p>	<p>Individual entrepreneurs operating as a cooperative will access common services</p>

People organized in a cooperative have a better control over their businesses affairs	from their cooperative, exercise control over its management but at the same time retain their individual businesses
<b>They are enterprises with ethical values</b> ( <i>business with a human face</i> )	This is important to informal economy enterprises as it provide them with business integrity and respect among their customers and the community generally They also fare relatively better in times of economic crisis
<b>Eliminating or minimizing exploitation</b>	The unity forged by forming and using the services of a cooperative will protect them against exploitation by suppliers, agents, principals or other business enterprises
<b>Employment Creation</b> Cooperatives can help generate employment or consolidate and sustain existing ones. Through schemes such as savings and credit cooperatives members can borrow money to start businesses thus creating self-employment for them.	Workers in the informal sector can consolidate and sustain their cooperatives through such cooperatives. They can also expand their existing businesses through cooperatives thus creating employment for others. There are various types of cooperatives particularly suited to employment creation. These are discussed later in this paper.

### 3. Types of cooperatives most suited to Informal Economy Workers

As explained earlier there are different types of cooperatives that are found in practically all economic sectors. However, certain types are more suited to the nature and circumstances of informal economy workers than others. Below are a few examples of such types which such workers may be encouraged and, if need be, supported to form.

3.1 *Shared Service Cooperatives (SSC)* (also known as *entrepreneurs' cooperatives*) are formed by enterprises (as distinct from individuals). Thus two or several or *businesses* run by informal economy workers trading in secondhand clothes can come together and form a cooperative which provides them with services such as bulk importation of clothes, organizing storage facilities for the merchandise, provide accounting services, organize insurance cover and organize member education. Where manufacturing is involved, an SSC may

provide common working facilities, procure raw materials, equipment or tools in bulk, organize marketing and help develop members' skills – services that would have been more costly if secured by individuals. Another type of an SSC is one that manufactures goods for its members. For example a group of carpenters may form a cooperative to run a sawmill and supply timber and other material and tools to its members.

A Member continues to own and run their individual businesses; the cooperative only provide *common services* such as those described above. In this way the members (businesses) gain from the economies of scale and whatever net surplus (profit) is made by the cooperatives reverts to them – in cash or in kind. This type of cooperative is ideal not only for small entrepreneurs but also for big business. Informal economy workers will find SSCs to be one way of improving their enterprises and earnings.

### **3.2 Savings and Credit Cooperative Societies (SACCOS)**

A savings and credit cooperative society (or credit unions as they are known as in some countries) is a cooperative that provides financial services to their members – i.e. members can save their money and borrow when in need. Like consumer cooperatives, the owners of SACCOS are at the same time the customers – that is, the people who save their money in and borrow from this type of cooperative.

Informal economy workers will find SACCOS particularly useful in developing their enterprises. As it happens, most informal economy workers, as indeed low wage earners, have no access to commercial banks when in need of loans. They have no collateral and sometimes the interests are much too high. Moneylenders are even worse. Their best refuge in this situation is a savings and credit cooperative. With the principle of *Voluntary and Open membership* that characterises a cooperative, any adult who accepts the conditions of membership can join a SACCOS and enjoy the services they offer. As with Shared Service Cooperatives, informal economy workers can get together and form a SACCOS, save their money there and borrow to improve their enterprises. In so doing they stand a good chance of developing to a level where they can transit into formality, for prosperity in the informal sector has the potential of being a turning point towards formalization. It also helps generate employment. Conversely, SACCOS can also help unemployed young people access funds for starting small informal enterprises, thus creating jobs for them.

## MINI CASE

### **Integration of Informal Economy Workers in the Cooperative Movement (Capacity Building of Informal Associations/Groups through Formation of Cooperatives Project)<sup>7</sup>**

*The Centre for Informal Sector Promotion (CISP) based in Moshi, Tanzania has been implementing a project supporting Informal Economy Workers (IEWs) and use the services of cooperatives. Dr Abdullah Makange, CISP's Executive Director and coordinator of the project reports on its outcomes*

The Project effected the removal of the special constraints that have hindered growth and graduation from informal to formal economy. The following are the outcomes of the Project:

- Informal Economy Workers, through their newly formed Cooperatives, are now in a position to **access financial services** through their SACCOS, thus qualifying for A special Presidential Fund for development, and the regular local Government allocation of loan fund to SACCOS. Loans and credit for business growth to finance investments related to formalization (acquiring permanent business sites, increased level of business activities and profits and sufficient working capital).
- Social and legal recognition and platform for advocacy through their Cooperative Society. The Cooperative statute provided effective **platform for advocacy or/and representation** to the extent that the Moshi Municipal Council undertook to allocate IEWs over 100 building plots in a 5 acres land, where residential and permanent business sites have now been established. These **permanent business Sites** provide a permanent location at which Government is able to enforce laws governing registration, taxation, monitoring and evaluation of the IEWs and provision of support services in orderly manner.
- In addition to the education and technical support provided by the Project, regular **training and skills up-grading** for the IEWs in these Cooperatives is now inherent in the wider national and global cooperative movement programmes. The long term impact of this will be effective business management, increased productivity and quality, gaining market competitiveness and increased social protection through linkages with local Governments and Institutions.
- The Project has provided practical education on the democratic leadership election process (the members resolved on Membership Registration Fees, a regular monthly minimum savings by each member, and voluntary adherence to rules and regulations and share contribution).

These outcomes (**accessing financial services, platform for advocacy or/and representation, training and skills up-grading, permanent business Sites** resulting from inclusion of Informal Economy Workers into the Cooperative Movement, are the ingredients for gradual and effective transformation from informal to formal economy (formalization).

### **3.3 Workers' Cooperatives**

A workers' cooperative as mentioned earlier is one where the members are at the same time the employees. People form this type of a cooperative as a way of creating employment for themselves. Workers in the informal economy may find this as a way of creating more secure jobs, which may earn them more income than working individually. Informal economy workers may find forming this type of cooperative more rewarding than working individually. It is also one way of formalizing the informal sector. It must be pointed out, however, that workers' cooperatives are rather complex and not quite easy to operate – especially by people who are not fully committed to working together. They require a high degree of commitment, cohesion and readiness to forego one's preferences to the common will.

### **3.4 Labour Contracting Cooperatives**

This is another form of a workers' cooperative. The main difference is that while members of a workers cooperative will need to have start-up capital for their cooperative as well as some training in certain skills relating to the work involved in their cooperative, members of a Labour Contracting cooperative do not need to have much start up capital except for renting an office with an address where they can be reached. Members do not need any particular skills as long as they are healthy and strong; their main capital is their labour. The cooperative maintains contacts with potential employers (construction companies, harbour and cargo handling authorities, airport authorities, railways, farms, etc.) When labourers are needed the cooperative arranges contracts with the prospective employer and sends out its members to do the job). The cooperative ensures that the contracts issued guarantee occupational health and safety, that decent wages are paid and that the work contracted and the work environment comply with statutory labour standards.

Wages may be paid to the cooperative, which in turn pays the member-labourers, retaining a small percentage for running costs. Alternatively the wages are paid directly to the labourers who then pay a small portion of their earnings to the cooperative for operational costs. In many cases though, the organization hiring labour pays a commission directly to the cooperative. In a way Labour Contracting Cooperatives work in a similar way as an employment agency; only that the business (the cooperative) is owned by the workers and whatever commission is paid to the cooperative reverts to members after deducting administrative and other statutory costs.

Since minors are not eligible for membership in a cooperative (with the exception of school cooperatives), and since cooperatives adhere to a code

of conduct and ethics embodied in their principles and values, the incidence of child labour is non-existent in Labour Contracting Cooperatives.

Labour Contracting Cooperatives are particularly suited to young people with no training in any particular skill. Such cooperatives have a great potential for creating employment. People opting for this form of accessing employment bypass informality, for Labour Contracting Cooperatives are in every respect formal enterprises.

### 3.5 Other types of workers' cooperatives

Other types of workers cooperatives include (but not limited to) the following:

- *Catering* – where members form a cooperative to run a restaurant or a chain of them
- *Entertainment*: where members (skilled musicians – modern or traditional; actors, comedians, etc) come together as a cooperative to cater to the public
- *Tourism*: where tour operators, tour guides, travel organizers form a cooperative to cater to the tourism industry
- *Manufacturing*: where small scale manufacturers come together in a cooperative to achieve economies either as one large manufacturing or processing cooperative or as a Shared Service Cooperative that provides services to individual manufacturers.
- *Collective Farming*: where members jointly own land which they cultivate collectively and share proceeds from their farming activities.<sup>6</sup>
- *Shoe shiners*: where shoe shiners in large towns or cities organize themselves into a cooperative and provide shoe-shining services to the public

Professional people such as health service providers, auditors, accountants, consultants in different fields, lawyers, business service providers, legal aid service providers etc. can also come together and form cooperatives even though, such people are not really informal economy workers.

#### MINI CASE

The Uganda Shoe-shiners Cooperative Society in Kampala is one example of a successful cooperative of this kind. Initiated by homeless street boys and girls who had, for a long time, been harassed by the city authorities for operating in the city without permit, they organized themselves into a workers cooperative and having attained legal status proceeded the same city authority for allocation of working areas in different parts of the city. Success followed success and in a couple of years they had branched into the manufacture of shoe brushes, using environment-friendly materials (natural wood and ox-tail bristles. The brushes became very popular

#### **4. The ILO and Informal Workers' Cooperatives**

The ILO considers the cooperative model as an ideal for informal workers in micro and small enterprises. For nearly a decade now it has been supporting programmes designed to help unprotected informal economy workers to organize cooperatives as a means of creating decent employment for themselves, provide social protection and increased incomes from better managed enterprises. One practical example of this is the ILO SYNDICOOP Project.

The Project was developed as a collaborative initiative by the Africa Regional Office of the International Trade Union Confederation (ITUC), the International Cooperative Alliance (ICA) and the International Labour Organization (ILO). Launched in 2002 the project aimed at helping improve the working and living conditions of unprotected informal economy workers, the underlying aim being poverty reduction among members of this vulnerable target group. Not entirely by coincidence, the project was designed to operate in concurrence with the Poverty Reduction Strategy Programmes that were in process in the region – programmes that had been developed in the context of the Millennium Development Goals (MDGs).

In East Africa the project was implemented in four countries: Kenya, Rwanda, Tanzania and Uganda. A separate project for South Africa was launched in 2004. Some of the pilot projects have been able to grow and to extend their outreach. Although both projects were later discontinued owing to lack of funding, in East Africa some of the pilot activities initiated under the project are still in evidence in some of the countries – for example Kenya and Rwanda.

Discussions on the best ways of continuing to support workers in the informal economy through cooperatives have been kept alive within the ILO and its social partners. At a Sub-regional workshop for leaders (chairpersons and chief executive officers) of national trade union federations in ten countries of Eastern and Southern Africa held in Nairobi in 2009, one of the objectives was *“to develop practical ways of strengthening collaboration between trade union and cooperative organizations and institutions in supporting informal economy workers organize and participate in the type of cooperatives most appropriate to their need”*<sup>8</sup>

It was noted at the workshop that

*“different types of cooperatives were widespread among union members and there was great potential to establish new ones while supporting the existing ones for diversified and better services for union members. It was stressed that it should be the union members who formed cooperatives, not the unions themselves. To strengthen existing union members' cooperatives and help establish new ones, unions should develop support services and use collective bargaining agreements to assist work-place cooperatives (particularly savings and credit as well as consumer cooperatives) in collecting members' contributions through a*

*mechanism similar to the check-off system, and providing office and selling space within the workplace by the employer, etc. As for the trade union-cooperative collaboration in the informal economy, it was highlighted that organizing the unprotected workers was among the priorities of trade unions, and if they worked with cooperatives in this particular area they would benefit considerably from the cooperative movement approaches and methodologies”<sup>9</sup>*

Even more recently, discussion on cooperatives and workers in the informal economy came up at a Sub-Regional Workshop on *Employers Organizations and Cooperatives* organized jointly which recommended, among other things, that

*“Employers’ Organizations work with cooperatives to help formalize the informal Sector through cooperatives”<sup>10</sup>*

## **5. Conclusion**

Cooperatives are democratic, member-based and member controlled enterprises whose policy and legal environment is constantly being reformed and for increased democratic organization, good governance and entrepreneurial efficiency. Although they cannot claim to be the panacea of all the complex problems facing workers in the informal sector, nor can they provide solutions to every case or every situation, they do represent a practical, ideal and time-tested model for self-employed people and small entrepreneurs with limited means and lacking voice. They are relatively easy to organize or join, and if their underlying principles and values are adhered to, and with sound management, good leadership and governance, they can help people create or consolidate employment, create wealth, improve livelihoods and contribute to poverty reduction. Both workers and employers organizations acknowledge this and are committed to support workers – including informal economy workers – organize and use the services of these member based enterprises. Cooperatives certainly are one practical option for the formalization of the informal economy.

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### **Notes:**

- 1 As defined in the International Cooperative Alliance’s *Statement of Cooperative Identity*, 1995.
- 2 *Ibid*
- 3 *Patric Develtere, Ignace Pollet, Fredrick Wanyama (editors) 2008. Cooperating out of Poverty: The renaissance of the African Cooperative Movement*
- 4 Johnston Birchall and Lou Hammond Ketilson (2009) *Resilience of the cooperative business model in times of crisis*.
- 5 *World Bank 2008 World Report*
- 6 Collective farming cooperatives are particularly active in Zimbabwe
- 7 The Project described in this Mini Case is supported by the ILO Cooperative Facility for Africa (COOPAfrica) through its Challenge Fund mechanism.
- 8 ILO COOPAfrica (2009) *Report on Sub-regional Workshop on Trade Unions and Cooperative*
- 9 *Ibid*
- 10 ILO COOPAfrica (2010) Draft Report on the proceedings of the Sub-Regional Workshop on *Employers and Cooperatives*” jointly organized by the Pan African Confederation of Employers, the Federation of Kenya Employers and the International Labour Organization, Nairobi , 15<sup>th</sup> -26<sup>th</sup> February 2010.