

2012 International Cooperatives

Mission Check

Are members growing in the same pace as coops grow? – Cooperative Auditing might give an answer?

Experiences from Germany


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Outline

- Nature and Facts of Cooperatives
- DGRV and the German Cooperative Organization
- Growth of members and coops
- Introduction of cooperative auditing




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Nature and Facts on Cooperatives

1. Business Association of independent persons with similar economic, social and cultural needs.
2. Jointly owned Enterprise owned and controlled by the people who use its services.
3. Organization based on values and principles and not on Profit.
4. Main Cooperative mission is the promotion task, the stakeholder approach and the regional business model. Benchmark for the policy of the coop is the member's promotion as an primary purpose of the enterprise.
5. Each Cooperative should be capable and attractive for their members – by a consequent economic direction, adequate internal organization and well educated management and staff.

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Short Profile: DGRV and the German Cooperative Organization



F.W. Raiffeisen



H. Schulze-Delitzsch

Postulation of F.W. Raiffeisen: At first more concentration on the economic growth of members and then an expansion of the business volume of the cooperative can be realized more efficient as members wind up more business transactions with the coop.


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Key Facts about DGRV

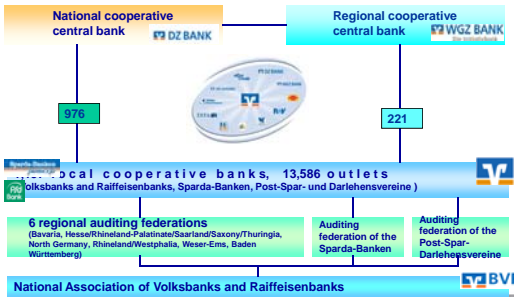
- DGRV is:
 - national cooperative apex organization and
 - top-level auditing federation
- DGRV unites as apex organization the coops in 4 sectors:
 - banking,
 - agriculture,
 - crafts/trade/services,
 - consumers
- DGRV has:
 - approx. 5,650 cooperatives affiliated to with
 - 18,4 million memberships and
 - > 800,000 jobs
- Cooperatives as a group have more members than any other business organization in Germany
- German cooperatives → 150 years of business - tradition

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The Cooperative Financial Network (Finanzverbund) 1/2

Member and basis-oriented with Subsidiarity Principle

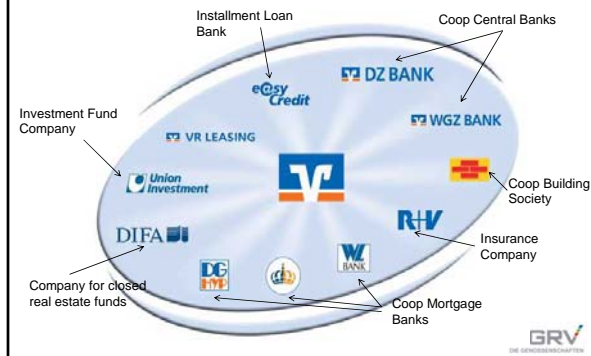


The diagram shows a hierarchical structure. At the top are two national cooperative central banks: DZ BANK (976) and WGZ BANK (221). Below them are regional cooperative central banks. At the bottom are 6 regional auditing federations, which are part of the National Association of Volksbanks and Raiffeisenbanks. The federations cover: Bavaria, Hesse/Rhineland-Palatinate/Saarland/Saxony/Thuringia, North Germany, Rhineland/Westphalia, Weser-Ems, Baden-Wuerttemberg; the Sparda-Banken; and the Post-Spar- und Darlehensvereine.

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The Cooperative Financial Network (Finanzverbund) 2/2



Credit Cooperatives in Germany

- Treatment as independent cooperative banks (high regulation) and cooperatives according to the cooperative law
- About 1.237 billion € of total assets
- Non-member's transactions and all financial services with the support of the cooperative financial network
- Comprehensive and nationwide provision of financial services by 13.571 bank service locations and thus the densest bank service network of Europe
- Financing for SME's and middle class (earlier: Self-help institution for small entrepreneurs)
- Group rating AA- (before: A+) by Standard & Poors
- Institute protection by a stabilizing protection scheme (managed by National Confederation of Coop Banks BVR)

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Mission Check:

Growth of members and cooperatives:

A moral or a legal question?



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Outcomes of cooperatives

- Growth of the co-operative should keep pace with the growth of the members or vice versa: However, can growth be really synchronized and transmitted one to one? Is this perception not too all-inclusive or too easy?
- Growth is also created for the region from which the members can benefit
 - > Emergence of other business industries
 - > Creation of new jobs and traineeships
 - > Financing of SME's and middle class and thus also creation of jobs
 - > Coops as the biggest employers, trainers, taxpayers, investors in the region (= guarantor for the level of development of the rural region)
- Conclusion: The regional growth brings indirectly benefits also for the members. (Example: Loans to other members who stimulate regional business circles with investments and consumption and by which members benefit again)

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Outcomes of cooperatives

- Pure access to financial service products for wide parts of the population is regarded as a growth by many experts
- Ensuring of the participation in the social live and growth for disadvantaged groups of population
- Savings and deposit policy contribute to the wealth-building and private pension plan (private growth)
- Development of the general standard of living and increase of the purchasing power
- Cooperatives contribute to economic (directly) and social development (indirectly), mainly in rural regions as promoters for regional economic cycles

economy → social effects → social structure

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Aspects for growth

- Call for a "healthy growth" of cooperatives (risk-avoiding growth, member-oriented growth)
- If members grow then other providers of services might be relevant for them. Member retention and loyalty have to be observed and maintained very carefully.
- Growth of the members is derived from the promotion task. However, the support lies not only in the growth. The business and economic activities of the member are in focus within the promotion task and not growth alone.
- The promotion task enhance a conservative business model, social orientation, sustainable growth and investment in human capital



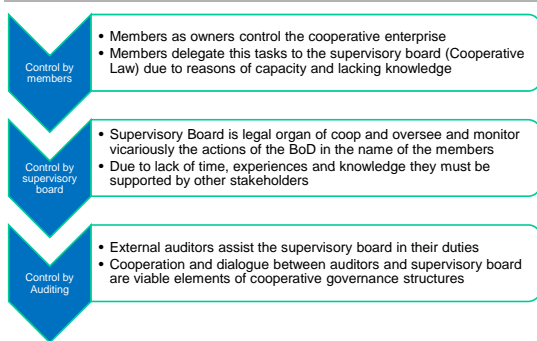
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Aspects for growth

- ❑ Changes in the structure of membership unveil growth and shifts of the promoted groups (strong increase of the non-member business, more heterogeneous member groups)
- ❑ Indicators: Official statistics on income increase, Interviews of members, Turnover of members with the cooperatives, Savings volumes, Demand for new services
- ❑ Orientation on Member Value and stronger relationship management to members
 - Business policy should be committed to the mandate of members
 - Operational Management guided by a Balance Scorecard System (Finance, Members, Market, Employees)
 - Long-term commitment to members, customers and local communities
 - Intensifying of cooperative member relationship (versus investor relationship). In return members are requested to support the coops in the long-term run.
 - **Economic sustainability to realize the promotion task towards members** (sustainable benefits for members versus short-term dividends)

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Development Stages of Control Structure



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Training on financial literature

- ❑ Indebtedness of members is not wanted and not in the sense of the promotion task
 - Over-indebtedness of members is an endangerment of members. (Conscious distinction to commercial banks and MFIs as social responsibility)
 - High risk volume from credit business and arising of credit risks for the coop as negative economic factors in case of enormous lending rates
 - Principles of consumer rights and customer protection according to other legal directives. The observance of the rights of members might be ensured by cooperative auditing.
- ❑ Training and advising program as a promotion task of coops to enhance financial literature and skills
 - But financial literature is not only task of coops also for schools and state institutions (e.g. protection against indebtedness for the Youth, cooperation models between coops and schools, formation of budget plans and personal finance plans as services for members)

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Definition of growth

- ❑ Level of Coop: quantitative
 - Total Assets, Adequate surplus (no maximization)
 - Loan and savings volumes
 - Number of members, Market Share
 - Built-up of equity and reserves
 - Number of branches and outlets
 - Dividends (no promotion task, only financial compensation on share capital), patronage systems (calculation surplus from the business transactions with members)
- ❑ Level of Coop: qualitative
 - Enhancement of a long-term capacity for promotion quality (defined by member) by investment in products and innovations
 - Development of sales and procurement markets in the regional business area
 - Additional achievements and outcomes for the region

Definition of growth

- ❑ Level of members: quantitative
 - Increase of income
 - Price advantages and favorable conditions (if enforceable on the market)
 - Dividends (no promotion task, only interests on share capital), patronage
- ❑ Level of members: qualitative
 - Demand-driven products and services from an cooperative financial network system (e.g. saving products, current account for salary/wages)
 - Service concepts and social benefits
 - Trainings, Consulting, Education and Information campaigns as personal support for members to generate growth by knowledge transfer
 - Involvement in business policy of the coops by capitalizing of democratic voting rights
 - Transparency of the business model (growth of confidence, integrity)
 - Independence of the business activities of each members

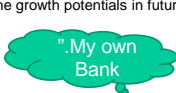
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Conclusion of growth

- ❑ Closing remarks
 - With reaching of a certain size class the distance between coops and members might increase. This kind of growth could endanger the members retention and loyalty. And furthermore: Members could leave the coop with taking out their share capital. **Our experience**: The greater the credit coop is the more we can see competitive pressure and the less the member's influence is perceived. Can Cooperative Auditing correct the situation?
 - Balance between quantitative and qualitative results and outcomes can not be evaluated and ascertained properly in any time. The comparison of the growth of the members with the growth of the cooperative remains complex.
 - Change of credit cooperatives and change of attitude of members (trend for multi-banking-relation and drift of members to competitors)
 - Counter Measures: Promotion plan, promotion report
 - Examples from members of Vietnamese People's Credit Fund
 - Recording of income increase
 - Expansion of their business activities (new shops in other towns)
 - Expenses for consumption and savings are rising

Conclusion for growth

- ◆ Growth is geared to the current and potential demand of members for products and services
 - Diversification of products (all-financial-products-provider like insurances)
 - Cooperation with other financial institutions (properly surrender mechanism of members from the credit coop to a financial institution)
 - Setup of a cooperative financial link-up system as partner of the primary level (central institutions, cooperative enterprises)
 - Integration of the technological progress
- ◆ Today: Management and guidance of the credit cooperative according to aspects of profit and risks due to the increasing competition. Approaches of modern banking management with steering of credit risks, restructuring of processes for lending and credit monitoring have to be addressed. A sustainable stronger position ensure the realization of the promotion task and the growth potentials in future.



Cooperative Auditing



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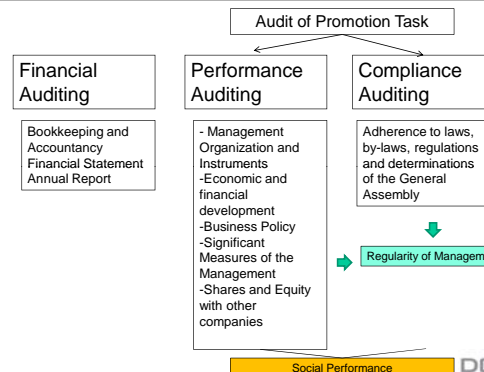
Cooperative Auditing

- Legal national Framework (commercial law, IFRS, cooperative law, credit institution law, auditing standards): cooperative auditing confederations are subject to supervision by the state according cooperative law
- Compulsory cooperative auditing as cooperative self-regulation (deduced from self-help principle)
 - Confederation is bearer of auditing with authorization to conduct the audits according cooperative law with certified public auditors and with full responsibility of the audit results
- Subject of cooperative auditing and extended audit assignment
 - Promotion Task
 - Material Audit of the regularity of the cooperative governance
 - Reporting (Audit Report, Report to GA, Final Audit Meeting)
- Audit is done in the interest of members, of cooperative, of the creditors and for the publicity (more transparency in business model of cooperative)

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Cooperative Auditing



Social Performance



Cooperative Auditing

- Audit of organization (internal, external, facilities)
- Audit of the financial position (equity, reserves)
- Audit of the economic situation as basis for the ability to promote the members (esp. revenue situation)
- Audit of the promotion purpose (original enterprise goal of the cooperative)
- Form of external audit and therefore quality control and assurance of the cooperative auditing
- No partiality by auditing and observance of professional principles and ethics of Certified Public Accountants
- Confederation is a society and is under control of the members (primary cooperatives) regarding the permissible purpose of the society (Consulting, Promotion, Perception of interests of the members, Auditing). But Auditing is independent to avoid conflict of interests.

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Cooperative Auditing

- Right and Obligation of cooperative auditor to point out serious shortcomings in economic position, organization and management
- Follow-Up-Audits (Audit Tracing)
- Assistance by recommendations, advices, Management Letter and further audit statements (written, oral)
- Continuous contact of the cooperative auditor with the cooperative to clarify auditing issues (ex-ante-Evaluations) and to avoid mistakes
- Profound analysis of the cooperative to ascertain the economic situation and to strengthen the position of the cooperative by mutual trust and respect („Doctor-Patient-Relationship“)
- Future-aimed consultancy function
- Permanent advising audits help the cooperative on the way of growth by creating valuable services and by increasing the trust of the members
- **Learnt Lessons: Stabilization of the coop sector and enhancement of member's trust**



Essential Questions: Promotion Task

- Are the business policy and the measures of the Board of Directors economically suitable for promotion and to which extent are they economically successful in terms of promotion?
- Instruments:
 - Market-related comparisons of conditions and prizes
 - Measurement of market shares
 - Evaluation of member's fluctuation
 - Business plan (promotion plan)
- Does the cooperative make such services available which are suitable for promotion by serving the growth of the members?
- Nevertheless a success from the promotion is not necessary and obligatory. The Coop must only aim the promotion and become active on this aim. Support is everything what is performed according to the by-laws – no matter whether the promotion can be measured in money. It is enough if the members take up, accept and use the services of the coop. The promotion is not thereby realized only then when the coop give a higher income to the members.
- Every member himself is responsible for the economic success (also growth) and with it alone from an audit-based and legal view.
- Nevertheless from the moral view the cooperative is highly addressed to support the growth of the members.

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Thank you for your attention!

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What one person can't achieve, many of them can"

(Friedrich Wilhelm Raiffeisen (1818-1888))

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