

LEGAL FRAMEWORK ANALYSIS

within the ICA-EU Partnership

National Report of New Zealand

ICA - Asia and Pacific (ICA-AP) is the voice of cooperative enterprises in the Asia Pacific region. ICA-AP, as a regional office of the ICA, is also a co-signatory of a Framework Partnership Agreement signed between the International Cooperative Alliance and the European Commission in March 2016, which aims at strengthening the cooperative movement and its capacity to promote international development. This agreement underpins the 'Cooperatives in Development' program and includes knowledge building activities at the global (harmonized) and regional (decentralized) level.

The activities planned within the framework of the program include diverse research activities conducted at the global and regional level. The primary activities undertaken at the global level include a Legal Framework Analysis (A2.2), which is led in a coordinated way by all ICA offices. Within this framework, ICA-AP oversees implementing the research in the Asia and Pacific region.

The study on legal frameworks under the Legal Framework Analysis (A2.2) will evaluate jurisdictions and policy regulations according to their enablement of cooperative development. The document will present recommendations for the next steps in renewing the legal frameworks and helping to shape the policy agendas in a targeted way in the different regions and countries. It will evaluate the cooperative legal framework in place with common indicators, delivering on a scale of how 'cooperative-friendly' the legislation in a country is. In the same context, this report deals with the Legal Framework Analysis of New Zealand.

Introduction

This report on the legal framework analysis on cooperative law in New Zealand is prepared by Ms Ann Apps, national and sub-regional expert appointed by the

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International Co-operative Alliance Asia and Pacific (ICA-AP).¹ The process of preparing this report began with the completion of a standard questionnaire for the analysis of the legal framework. The completed questionnaire was referred to New Zealand’s peak body for cooperatives and mutuals, Co-operative Business NZ for review and comment and their feedback was considered when preparing this National Report.

The legal framework analysis on cooperative legislation in New Zealand aims to:

- Provide a general overview of both the Co-operative Companies Act 1996 (NZ) (“CCA”) and the Industrial Provident Societies Act 1908 (NZ) (“IPSA”) comparing their main features including how each legal framework secures the cooperative identity and distinguishes cooperatives from other types of business organizations.
- Evaluate if New Zealand’s cooperative law supports or hampers the development of cooperatives, and to the extent that it is not “cooperative friendly”, make recommendations for reform.

New Zealand Cooperative Law

General Context

Unlike most countries, New Zealand does not have a single constitutional document. The Constitution Act 1986 together with a collection of statutes (Acts of Parliament), the Treaty of Waitangi, Orders in Council, letters patent, decisions of the courts and unwritten conventions make up New Zealand’s uncodified Constitution. No special recognition or protection is accorded to cooperatives under these laws.

In New Zealand, cooperatives may incorporate as cooperative companies or cooperative societies, unless they are financial cooperatives (building societies or credit unions). Non-trading organisations that function as cooperatives may register as incorporated associations. A list of the relevant instruments is set out in Table 1, below.

¹ Ann would like to acknowledge the work of research assistant Ms Elizabeth Makin

Table 1

Denomination	Date of Assent	Date of most recent update/reprint
Co-operative Companies Act, 1996	4 June 1996	1 December 2014
Industrial and Provident Societies Act, 1908	4 August 1908	12 November 2018
Building Societies Act, 1965	17 September 1965	12 November 2018
Incorporated Societies Act, 1908	15 September 1908	12 November 2018
Friendly Societies and Credit Unions Act 1982	1 December 1982	1 April 2019

The New Zealand’s cooperative sector, in terms of size and turnover is dominated by cooperatives registered under the Co-operative Companies Act 1996 (“CCA”). The CCA provides for the registration of companies as ‘co-operative companies’ and includes special provisions for ‘co-operative dairy companies’.² Paragraph (a) of the Long Title to CCA states that the law’s purpose is "to reaffirm the value of the cooperative company as a means of facilitating its shareholders carrying on business on a mutual basis". Cooperative companies must also be registered as companies under the Companies Act 1993 either prior to, or at the same times as, application for registration as a cooperative company (CCA ss7 and 36). The largest dairy cooperative in New Zealand is Fonterra Co-operative Group, and its establishment in 2001 and ongoing structure and operation is enabled by the Dairy Industry Restructuring Act 2001 (NZ) (“DIRA”). Because Fonterra is such a significant industry player in NZ, DIRA must also be recognised as having an impact on the cooperative law and policy landscape. A more detailed analysis is provided in the conclusion to this report.

Cooperative companies are hybrid vehicles, sharing features of both the investor-owned company and the member owned cooperative. They may tend towards either type, depending on the internal governance structure set out in their constitution. However, the legal restraint on registering and continuing to operate as a cooperative company under the CCA is that it must be involved in a ‘co-operative activity’ i.e. where it engages in a business that transacts with its shareholders, CCA s

² See: <http://www.legislation.govt.nz/act/public/1996/0024/latest/DLM376810.html>.

3 and no less than 60% of its voting share capital must be in the hands of those transacting shareholders, CCA s 4.

However, the Industrial and Provident Societies Act 1908 (NZ) (“IPSA”) which sets out a more traditional legal framework for cooperative societies will also be considered and compared in this report. An industrial and provident society “will usually consist of the owners of small businesses who, while continuing to operate independently, become part of this larger entity for mutual benefit”.³

With the exception of financial cooperatives (credit unions and building societies) which have their own legislation (see table above), cooperative laws do not make specific provision for particular types of cooperative (i.e. worker cooperatives, social cooperatives, educational cooperatives, etc.) however the various laws for cooperatives shown in Table 1 above, provide ample flexibility to accommodate the various types of cooperatives including producer cooperatives, purchasing / shared service cooperatives, financial cooperatives, consumer cooperatives and worker cooperatives.⁴

Specific elements of the cooperative law

Definition and objectives of cooperatives

Cooperative Principles

Application of Cooperative Principles (General)	Relevant section CCA (link)	Relevant section IPSA (link)
General reference to principles	n/a	n/a
Requirement for registration that business is designed to function in accordance with cooperative principles.	The use of the word ‘co-operative’ in the name of a company registered under the Companies Act is restricted to those	To be registered a society must be either “a bona fide cooperative society” or a society where its activity “will improve

³ New Zealand Companies Office, “About the Industrial and Provident Societies Register, How they’re established, their advantages and features”, <https://www.companiesoffice.govt.nz/all-registers/industrial-and-provident-societies/about-the-industrial-and-provident-societies-register/>

⁴ See generally Co-operative Business New Zealand: <https://nz.coop/types-co-operatives/>.



	who are also registered as cooperative companies and must meet the requirements for registration under the CCA, CCA s 14.	the conditions of living or the social well being of members of the working classes”, or be for “community benefit”. S33(2) Statutes Amendment Act 1939
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Application of Cooperative Principles (Specific)	Relevant section CCA (link)	Relevant section IPSA (link)
Voluntary and open membership	A cooperative company may issue shares at a nominal value and accept surrender of those shares at that nominal value (CCA ss15 and 18) facilitating voluntary membership.	The terms of admission and withdrawal of members must be set out in the rules of the Society (Schedule 2) s7.
Democratic member governance	One member/one vote is not prescribed, however no less than 60% of voting rights must be exercised by transacting shareholders, thus requiring some degree of member control, CCA s2. Only transacting shareholders may vote on resolutions unless the	Voting rights are set out in the society’s rules. (Schedule 2) but requirements for special resolution assume one member one vote (s14) Individual shareholding is capped at \$4000 or such amount as prescribed s4(2)

	constitution states otherwise. CCA s 33.	
Member economic participation.	This is inherent in the definition of ‘co-operative activities’ CCA s3 when coupled with the meaning given to ‘transacting shareholder’ in CCA s 4(1). Not all members need to be transacting shareholders but must be more than 60% to qualify as a cooperative company.	Terms of admission to membership are set out in the societiy’s rules (Schedule 2)

Specific elements of the CCA or IPSA which secure the cooperative identity when compared to the identity features of a for-profit company.

The CCA s2 defines a cooperative company as either “a company, this principal activity of which is, and is stated in the constitution as being, a cooperative activity and in which not less than 60% of the voting rights are held by transacting shareholders” or “a company that is a subsidiary of a [co-operative company] and the principal activity of which is, and is states in its constitution as being, a co-operative activity”. A ‘transacting shareholder’ is defined in CCA s4 as a shareholder of the company that either supplies goods or services to, or purchases goods or services from, or otherwise enters into commercial transactions with the company. Cooperative companies are not precluded from carrying out transactions with non-members however CCA s3 lists a range of valid activities that might be defined a ‘co-operative activity’ and requires that the activity involves the company in transactions with its shareholders, whether as suppliers or consumers.

If the company is registered as a dairy cooperative company, all suppliers must also be shareholders of the cooperative company unless otherwise authorised by its

constitution, CCA s39. For both types of cooperative company, the CCA includes features which allow it to ensure continuously active membership. It can do this by issuing shares to transacting shareholders at nominal value and allowing for the redemption and surrender of those shares when the member wishes to leave or no longer transacts with the cooperative company, CCA s21.

The IPSA s4 defines a society that is registrable under the Act as ‘a society for carrying on any industry, business, or trade, whether wholesale or retail, specified in or authorised by its rules, including dealings of any description with land, but excepting the business of banking’. The society must be either “a bona fide cooperative society”, a society where its activity “will improve the conditions of living or the social well-being of members of the working classes” or be for “community benefit”.⁵ Cooperative organisations registered under the IPSA must not have a primary purpose of member profits, s33(3) Statutes Amendment Act 1939, although they may make distributions on surplus to their members in the form of rebates on transactions, as provided for in their rules, IPSA Schedule 2.

While the CCA does not accommodate non-profit cooperatives, IPSA can accommodate businesses that are for community benefit or ‘not for profit’ businesses for member benefit. Cooperatives of this nature may also be registered under the Incorporated Societies Act 1908 (“ISA”), which requires that the association must not be intended for ‘pecuniary gain’, IPSA ss 4 and 5. However, unlike not-for-profit organisations in other jurisdictions, an incorporated society may distribute its assets to its members on winding up, s 5(b) of the ISA.

Establishment, cooperative membership and governance

Legal requirements for the establishment and continuation of a cooperative

Registration of a cooperative company must take place in accordance with CCA s6 which requires an application to the Registrar, which has been authorised by either the company constitution or by special resolution of its shareholders. A compliant application must be made in the prescribed form, signed by a person with express or implied authority to represent that company and accompanied by a statutory declaration made by each director stating that ‘in the opinion of the director, the

⁵ S 33 Statutes Amendment Act 1939.

company is a cooperative company within the meaning of this Act and the grounds for that opinion’.

It should be noted that the CA does not require a company to have a constitution, CA s26. If a company does not have a constitution, relevant provisions of the CA apply by default. Although there is no express requirement for a cooperative company to have a constitution, the requirement is implied by the CCA. For example, the CCA defines a cooperative company as one whose principal activity is defined in its constitution as a cooperative activity, CCA s 2.

There are no express minimum member number requirements under the CCA however given the requirement that no less than 60% of voting rights must be held by a transacting shareholder, a cooperative company will need at least 2 members to form a cooperative company. By way of comparison, IPSA s5 expressly requires a minimum of 7 members to register as a society, and the Incorporated Societies Act 1908 s4 expressly requires a minimum of 15 consenting persons to register as a society under that Act.

Admission of new members

Rules concerning the admission of new members will generally be set out in the company constitution and there is no specific requirement that a cooperative company accepts third parties as members, Companies Act 1993 s30, but there is a limit on the number non-transacting shareholders. CCA s2(1)(a).

Subject to its constitution and a test for solvency, a cooperative company may accept the surrender of shares having a nominal value by a person who has ceased to be a transacting shareholder: CCA ss18 and 20. These provisions enable both the freedom of members to leave the cooperative, and operation of the principle of open and voluntary membership under NZ cooperative law, whilst allowing for some flexibility between cooperatives.

The ‘open door’ principle was mandated for Fonterra by DIRA, which required that Fonterra accept the entry and exit without penalty (with minimal exceptions) of any dairy farmer in New Zealand that was willing to hold shares in proportion to their milk supply as a member of the cooperative. Proposed changes to DIRA will remove this requirement, so that the ‘open door’ policy is no longer mandated. ⁶

⁶ Dairy Industry Restructuring Amendment Bill (No 3) access at <http://legislation.govt.nz/bill/government/2019/0166/latest/d1921852e2.html>

The terms of admission of new members of cooperative societies are set out in the rules, IPSA Schedule 2.

Member's voting rights

Democratic member governance (i.e. one member, one vote) is not required under CCA. Generally, voting rights attach to shareholding unless otherwise provided for in a cooperative company's constitution and the terms of issue for shares, Companies Act 1993 s36. However, the CCA does state that only transacting shareholders will be entitled to vote on a resolution unless the constitution expressly provides otherwise, supporting a culture of control by the active members of a cooperative company, CCA s33. This is further supported by the requirement that no less than 60% of voting rights must be exercised by transacting shareholders, thus requiring some degree of member control, CCA s2. IPSA does not expressly deal with voting rights, but the rules will typically provide for one member one vote.⁷

Governance structure

Both the number and qualifications of cooperative company directors will generally be set out in the company constitution and cooperative companies have considerable flexibility in this regard, Companies Act 1993 ss150 and 151. Democratic member control of a cooperative company is provided through transacting shareholder voting rights, such as the power to appoint or remove directors: Companies Act 1993 s36 and CCA s33. Most directors of the cooperative company do not need to be transacting shareholders (i.e. active members) of the company unless this requirement is set out in the constitution.

Directors' duties are primarily set out under the Companies Act 1993 Part 8 and include the duty to act in good faith and in the best interests of the company; the duty to exercise powers for a proper purpose; and the duty to disclose conflicts of interest, CA ss131, 133 and 140. In exercising these duties, a director may rely upon professional or expert advice or information provided by another director, a committee or an employee, CA s138.

The rules of a cooperative society must provide for the appointment and removal of a committee of management, managers or other officers and set out their respective powers and remuneration, IPSA Schedule 2 (4). The officers of the society have a duty to fulfil the duties of the society which are set out in IPSA s 8. If there is no officer

⁷ http://nz.coop/wp-content/uploads/2018/01/LetsGetStarted-Manual_2018.pdf

appointed with responsibility for the relevant duty that has been breached, then the offence is deemed to have been committed by every member of the committee (unless the committee member can prove that they were ignorant or attempted to prevent the commission of such offence) IPSA s 8(1)(c).

Boards of cooperative companies and management committees of societies are accountable to their members through requirements for annual reporting to members through audited or reviewed financial reports and director reports, IPSA s8G, CCA Ss120, 124, 201. The obligations of a cooperative society to prepare financial statements and have them audited will depend on whether the cooperative is 'large' (as defined by s 45 Financial Reporting Act 2013) and/or whether the members have passed a resolution opting out of requirements to prepare financial statements and or have those statements audited (IPSA ss8K, 8L). A resolution passed under s8K or s8L must be passed at a meeting by not less than 95% of the members of the society who are present in person or proxy and are entitled to vote. Cooperative companies may also opt out of preparing annual reports, depending on the size of the company, the number of shareholders and whether members are willing to opt in or out of compliance with requirements for reporting and auditing. CA ss207I, 207J, 207K.

The directors of a cooperative company are required to pass an annual resolution stating the board's opinion as to whether the company has, throughout the accounting period, been a cooperative company. The board must give reasons for its opinion. CCA s10. Any application by the company to cancel its registration as a cooperative company must be authorised by a special resolution of its shareholders, CCA s12.

New Zealand cooperative societies or cooperative companies are not presently required by law to engage in any social (non-financial) auditing or reporting to demonstrate the non-financial value of the cooperative's economic, social and cultural performance in light of the common needs and aspirations of their members.

Cooperative financial structure and taxation

Capital contributions

IPSA limits member share capital in cooperative societies to \$4,000 (the Minister may authorise a higher value in respect of any society by notice in the New Zealand Gazette), IPSA s 4(2).

There is no minimum capital contribution in cooperative companies other than the requirement that there are two or more shareholders who each hold shares of some value. Shares in a cooperative company may have a nominal value and different classes of shares may have different nominal values, CCA s 15. There is no limit in the CCA on the size of the shareholding of a single transacting shareholder, so long as no less than 60% of voting rights are in the hands of transacting shareholders. However, there may be a limit set out in the constitution. This limit may be determined based on transactions with the company during a defined period. CCA s 21 authorizes the cooperative company to require a shareholder to surrender excess shares where the shareholder holds more shares of nominal value than is required under its constitution.

Continuing member contributions to capital may be linked to the member's volume of transactions (patronage). This may occur by issuing shares in lieu of rebates to transacting shareholders who agree to accept the issue of the shares, either wholly or partly in lieu of the proposed rebate, CCA, s30, 31. Cooperative dairy companies may also include a power in their constitution to require members to take up additional shares, CCA ss 40, 41, 42.

Other sources of finance

Subject to powers in their constitution and the requirement that 60% of shares are to be held by transacting shareholders, cooperative companies can raise capital by issuing transferable shares to non-transacting members in accordance with the relevant provisions in the Companies Act and its constitution. Cooperative companies may also raise capital by issuing debentures and obtaining loans in the same way as other companies. Cooperative Societies also have the power as set out in its rules, to raise capital from other sources by borrowing and issuing debentures, s10(e). The offer of all securities of either cooperative companies or cooperative societies must

be properly disclosed in accordance with the requirements of the Financial Markets Conduct Act 2013.

Distribution of surplus to members

A cooperative company may distribute its profits or surplus to its transacting shareholders as cash rebates or shares in lieu of rebates, CCA s 30, s 31. Rebates are usually calculated in relation to the volume of ‘transactions’ made during the particular accounting period. If the cooperative company has non-transacting shareholders, it will also need to make provision out of its profits for the payment of dividends on those shares. The CA makes provision for the payment of differential dividends for different classes of shareholders and for the payment of shares in lieu of dividends. CA Ss 53, 54.

The profits of a cooperative society may be applied to any lawful purpose, IPSA s 10(f). IPSA does not otherwise expressly deal with the distribution of surplus and leaves this to the rules of the society, IPSA Schedule 2 (9). However the definition of a ‘co-operative society’ in s33 Statutes Amendment Act 1939 says that it “does not include a society which carries on, or intends to carry on, business with the object of making profits mainly for the payment of interest, dividends, or bonuses on money invested or deposited with, or lent to, the society.” This impliedly requires the Society to either apply its profits for the benefit of its members as a whole or for community benefit, or as a patronage rebate.

Distribution of surplus upon dissolution

The CCA does not make any special provision relating to the winding up or dissolution of a cooperative company, and the provisions of the CA will apply. A cooperative company (or any company) may provide for the disinterested devolution of any surplus assets following a liquidation in its constitution, CA, s 313 (4).

If a cooperative society is put into liquidation because it is insolvent, CA Parts 16 and 17 will apply, IPSA s15(1) (a). If the cooperative society is not insolvent it may be dissolved by an instrument of dissolution signed by three-fourths of its members, s15 (1) (ab). The members of a cooperative society may make provision for the distribution of any surplus in the instrument of dissolution or leave this to the award of the Registrar, IPSA s 15(1) (c).

Taxation of cooperatives

Cooperative companies attract some preferential treatment under NZ taxation law. For example, ss CD 34B and DV 11 of the Income Tax Act 2007 provides that distributions made to members (in relation to transaction shares) will not be classified as dividends and will therefore be deductible to the cooperative company (and taxed as income in the hands of cooperative members). The common law principle of mutuality is overridden, so that under section DIV 19 of the Income Tax Act 2007 any "mutual association" is allowed a deduction, for a distribution to its members of net taxable profits (termed "an association rebate"). Importantly also, s CD 34B(9) of the Income Tax Act 2007 provides an exception for cooperative companies to s125(2) of the Companies Act 1993, which allows these entities a degree of flexibility in determining the date of distributions to its members.⁸ This is particularly important for agricultural cooperatives, for example, which may have different trading and financial year ends.⁹ Cooperative companies can also use imputation credits non-deductible rebates so that payments are franked, eliminating the double taxation of cooperative distributions to members.

Other specific features

Cooperatives in New Zealand are generally free from government interference. The Registrar has power to cancel the registration of a cooperative if satisfied on reasonable grounds that the company is not, or has ceased to be, a cooperative company, CCA s 11. The Registrar of IPSA also has power to cancel or suspend the registration of a society on certain grounds, s 6 and has powers to inspect and investigate the affairs of a society to ascertain compliance with the IPSA, s 13A.

Both CCA and IPSA allow for the formation of cooperative groups (comprising two or more cooperatives or a corporation or other body otherwise allowed to obtain membership of the cooperative group), so that cooperatives may choose to form secondary cooperatives. But the legislation does not deal specifically with cooperative federations and they have no legally recognised role controlling or self-regulating member cooperatives.

⁸ See generally: <https://www.ird.govt.nz/technical-tax/legislation/2010/2010-109/2010-109-distributions/leg-2010-109-distrib-co-members.html>.

⁹ Information on taxation of cooperatives was kindly provided by Alistair Hercus for Co-operative Business NZ.

The cooperative peak body in NZ is Cooperative Business NZ.¹⁰ The organisation was originally formed in the 1960's when agricultural cooperatives formed an incorporated society, the NZ Agricultural Co-operatives Association. It was later re-named as the NZ Cooperatives Association in 1997, and then Cooperative Business NZ in 2012 and includes members from non-agricultural sectors. Cooperative Business NZ promotes cooperation among cooperatives by enabling information sharing, reciprocal supply agreements and leverage on combined purchasing volumes to lower operating and capital costs for its members.

Degree of “cooperative friendliness” of the NZ cooperative law

The CCA is more cooperative friendly than not. This is because the legislation has been tailored (together with the Dairy Industry Restructuring Act 2001 (DIRA) to meet the specific requirements of the dairy industry, which is the largest industry in the cooperative sector and one of the largest exporters in New Zealand. The CCA is a hybrid cooperative company model and does not itself encourage compliance with the cooperative principles, this is left to the constitution/by-laws of the individual cooperatives registered under the Act. The IPSA is more cooperative friendly than not because it requires the registrar to determine if the organisation seeking to register is a bone fide cooperative. The IPSA has worked well for service cooperatives in New Zealand, but other cooperatives might also be registered as incorporated societies under the Incorporated Societies Act 1908 (NZ) (ISA) which is not considered in any detail here. The IPSA and (ISA) are archaic laws, that are otherwise very flexible, leaving it to the cooperative's constitution/by-laws to set out the cooperative's adherence to the cooperative principles. A more detailed analysis of the strengths and weaknesses of each cooperative law (CCA and IPSA) is outlined below:

Legal obstacles or barriers

New Zealand has very different cooperative laws to Australia, and consequently very different issues and strengths. In terms of the size of the NZ cooperative sector, annual revenue of the top cooperative businesses and their overall contribution to GDP, NZ outperforms Australia and has been described as the ‘world's most

¹⁰ Cooperative Business NZ, see website at <https://nz.coop/>

cooperative economy.’¹¹ In terms of legal obstacles, the following are the opinions of the author (also noting where my opinion is based on input from Coop Business NZ):

CCA is a ‘hybrid’ model. This has advantages and disadvantages. One disadvantage is ‘isomorphism’ in the sense that by locating the model ‘within’ the company model, it obscures and waters down a distinct cooperative identity. One consequence of this is an absence of attention to the specific features of the cooperative model in policy and regulatory circles dealing with business regulation generally.

The Registrar for cooperative companies and cooperative societies is the Companies Office within the Ministry of Business Innovation and Employment. There is no specialised unit for the regulation and administration of cooperatives.

What is pitched in NZ as ‘regulative neutrality’¹² – tends towards the homogenisation of law for business models. A ‘one size fits all’ approach to regulation, discriminates against those businesses which do not fit the dominant model.¹³ Arguably this approach also reduces the opportunities for diversity in business models in NZ.

While the CCA model offers flexibility, the legal restraints on registering and continuing to operate as a cooperative company requires cooperative companies to have sophisticated and tailored constitutions/internal governance rules. This may operate as a barrier for those who cannot afford access to specialised professional advice at ‘start-up’ and to continue to adapt as the business and its circumstances evolve.¹⁴

¹¹ In a 2014 global survey commissioned by UNDESA, measuring the membership penetration of cooperatives relative to the total population (i.e., membership /population), employment by cooperatives relative to total population (i.e., employment/population) and annual gross revenue or turnover of all cooperatives in a country relative to the country’s GDP, NZ was ranked number 1 in the world, <https://nz.coop/research-reports/top-40/>.

¹² Evans, E, & Meade, R “The Role and Significance of Co-operatives in New Zealand Agriculture: A Comparative Institutional Analysis” (2005, New Zealand Institute for the Study of Competition and Regulation Inc. Wellington), 5.

¹³ This point was raised in a discussion with Coop Business NZ, speaking about the cooperative and mutual sector as a whole. Business regulation in NZ is generally geared to the investor owned and profit maximising company model. This leads to an unequal playing field where the differences in risk when a regulation designed for investor-owned business applies to member owned businesses, is not properly taken into account.

¹⁴ This problem also stems from a lack of recognition of a distinct identity for cooperatives. It means that there are very few experts with the skill set to assist new businesses to enter the sector and consequently the legal assistance required is scarce, complex and expensive. This was an issue raised by Coop Business NZ.

The CCA model does not expressly require a cooperative company and its directors to prioritise member benefit over the financial interests of investor members. While these interests may sometimes merge (for example where members are the only investors) the lack of express and clear prioritisation of duty increases the risk that where a conflict arises - the financial interests of investors will prevail.

The IPSA is an archaic piece of legislation that has not been replaced since 1908. Being archaic is not necessarily a legal obstacle, however it indicates a lack of interest in updating and modernising the law for cooperative societies at regulatory and policy levels.¹⁵

IPSA imposes a restraint on member contributions to capital, which must not be more than \$4,000 per member unless a Ministerial exemption is claimed.¹⁶

Features of CCA that stand out as ‘best practice’

The benefits of legislation for a hybrid cooperative company model which is particularly well suited to agricultural cooperatives should not be discounted. The legislation allows adaptive solution to problems facing most agricultural cooperatives, who are under pressure to expand and modernise to survive in increasingly competitive global markets. The features of the CCA which stand out as ‘best practice’ include:

Generally, the law is very flexible. It enables but does not require cooperatives to issue nominal value shares. Some cooperatives have changed from nominal value to ordinary shares, which are not subject to redemption risk and this may help to attract further capital investment.

The use of ‘cooperative’ in the name of the organisation is protected, so that only those companies that are also registered under the CCA (and meet its requirements) can use the word coop or cooperative in its business name. Cooperative societies

¹⁵ This is of course based on an assumption that the law needs updating and modernising. Interestingly the author was going to cite the law on partnerships as an example of another area of law where the legislation has not been updated since 1908, and the argument is that both are self-regulating business models and existing laws have been operating effectively. However I note that in 2019 NZ has introduced Partnership Law Act 2019 (NZ) and stated as its purpose in s 3, as being to: re-enact the [Partnership Act 1908](#) in an up-to-date and accessible form.

¹⁶ The rationale for this limitation is not clear, other than the note on the website of the New Zealand Companies Office that: “by restricting the degree of participation by any one member to a value fixed by the Act, domination by one member is not possible. This ensures the cooperative nature of industrial and provident societies continues.” It is possible for a cooperative society to include democratic control rights by including ‘the one-member/one-vote’ rule in its by-laws, but this is not mandated in the Act.

registered under IPSA may also use the words ‘cooperative’ in their business name where it is shown to the satisfaction of the Registrar that a society is a bona fide cooperative society.¹⁷

The CCA requires the board as part of its annual reporting process to pass a resolution stating whether in the board’s opinion, the company has, throughout the accounting period to which the report relates, been a cooperative company. The resolution must set out the full reasons for the directors’ opinion, CCA s 10. In the author’s opinion any requirement for the directors of a cooperative organisation to take their mind to the cooperative identity of the business – and report on this publicly is an example of best practice which should be replicated in other laws. In this instance the requirements are technical (i.e. attention to what is a ‘cooperative activity’? and who are its ‘transacting shareholders’?) but the reporting requirement could easily be extended to include reporting on the cooperative company’s attention to the cooperative principles.

Features from other jurisdictions that might encourage cooperative development in New Zealand.

While leaving the CCA to continue as a hybrid model, some features that could be added to strengthen the cooperative identity include some of the features of the Australian CNL including modifying the Act’s statement of purpose to go beyond reaffirming the value of members transacting on a mutual basis to the active promotion of the cooperative philosophy, principles, practices and objectives (CNL, s 3). Incorporating CNL s 10 (which simply sets out the cooperative principles) and s 11 which provides that statutory interpretation of any provision should prefer an interpretation that would promote the cooperative principles.

The UK recognises two types of incorporated society – a cooperative society and a community benefit society, Co-operative and Community Benefit Societies Act 2014. The community benefit society differs from cooperative society in that it is expressly for community benefit, not member benefit, and may adopt a statutory asset lock. A voluntary asset lock can be removed by members. The advantage of recognising both a cooperative society and a community benefit society as two specific and separate types of entity, is that it allows flexibility for organisations to choose the best fit and at the same time helps to solidify the legal identity of a cooperative as being specifically for member benefit. In New Zealand, the IPSA requires that to be

¹⁷ S33(4) *Statutes Amendment Act 1939* (NZ)

registered a society must be a ‘bone fide cooperative society’ or is otherwise for the benefit of the ‘working classes’ or for the benefit of the community (Statutes Amendment Act 1939, s33). While the reference to ‘working classes’ is offensive, the Act does not make a clear distinction between a cooperative and a community benefit association. The UK legislation which has evolved out of similar IPSA may be a good legislative model for NZ if it decides to update its existing legislation.

The cooperative audit is an important mechanism in German cooperative law, and it does not have an equivalent in NZ legislation on cooperatives. The cooperative audit looks at a wider set of indicators beyond financial performance and verifies the organization’s compliance with cooperative values and principles. There is an increasing interest in social accounting and auditing and good reasons for cooperative companies and cooperative societies to use these tools to brand their cooperative difference.

Recommendations for the improvement of the national legal framework

The following recommendations for improvement of the national legal framework may relate to either the CCA or IPSA frameworks of both as indicated:

- The replacement of the IPSA with new legislation for cooperative and community benefit associations as described above. As with the recent introduction of the Partnership Law Act 2019, the replacement of existing legislation with legislation that is in an ‘up to date and accessible form’ is overdue.
- A provision in the CCA and IPSA or equivalent which allows cooperative companies (with nominal share capital) to adopt accounting standards that are tailored for cooperatives; and a corresponding extension of New Zealand’s Accounting Standards Framework to include as distinct categories: for-profit entities and not for profit entities that are private organisations for ‘member-benefit’.
- The adoption by CCA of a mandatory cooperative governance code.¹⁸ This suggestion is linked to other recommendations including recognition of the

¹⁸ In Australia, the BCCM has published voluntary governance principles. The debate over voluntary or mandatory codes of governance for investor owned corporations is ongoing, however a mandatory code is arguably not a bold step for cooperative companies and may help directors stand their ground against

cooperative principles in the CCA; requiring directors to prioritise member benefit where there is a conflict in competing duties to investor and members (in their role as transacting members rather than investors) and finally extending the director's resolution in the annual report to include reference not only to whether the company was a cooperative company throughout the reporting period, but also the company's attention to implementation of the cooperative principles (noting that this does not mean that where an entity does not implement all of the cooperative principles that this is a bar to its continuing registration as a cooperative company).

Conclusions

The history and development of cooperative law in New Zealand is unique and its strong and efficient agricultural cooperative sector is the envy of many other countries. However, recently, in the face of relentless global competition, volatile markets, climate events and possible biological epidemics, there are signs of cracks in New Zealand's flexible approach to the cooperative business model. In 2019, Westland Milk Products demutualised its century old cooperative model when it was sold to China's Yili Industrial Group.¹⁹ Fonterra reported record losses and a \$7.4 billion debt including a \$4.74 m payout to its resigning Chief Executive Officer.²⁰

Fonterra is NZ's largest dairy cooperative and it was established in 2001 from the merger of two existing dairy cooperatives and the New Zealand Dairy Board. The deal and the continued operation of Fonterra (as an almost monopoly processor) was enabled by special legislation, the Dairy Industry Restructuring Act 2001 (NZ).²¹ The DIRA was amended in 2012 to increase liquidity and to "enhance the stability of its capital base" by listing non-voting units on the stock exchange.²² The amendments

executive management who are often inclined not to prioritise cooperative principles. Moreover, mandatory requirements for cooperative specific reporting may increase understanding and focus on all of the cooperative principles under the law. See CME Governance Principles: <https://bccm.coop/wp/wp-content/uploads/2018/09/BCCM-Governance-Principles.pdf>

¹⁹ A Fox, "Co-operative ownership of Westland dairy company passes into history." NZ Herald, 18 July 2019, at https://www.nzherald.co.nz/business/news/article.cfm?c_id=3&objectid=12250777

²⁰ J Smythe, "Fonterra's global ambitions sour dairy group's fortunes." Financial Times, 26 August 2019, at <https://www.ft.com/content/86450ea2-c4a1-11e9-a8e9-296ca66511c9>

²¹ N Shadbolt and A Duncan, "Perspectives from the Ground: Fonterra Co-operative Case Study" in T S Chieh and C T Weber (eds), *The Capital Conundrum for Co-operatives*, ICA 2008, 96.

²² *Ibid*, 100.

provided Fonterra with a green light to continue its rapid expansion into global markets. While the legislative framework included mechanisms to protect the notion of member-control, the sheer distance between the global arm of its business and its dairy farmer members in NZ created governance issues that have proved to be a problem and continue to threaten its cooperative identity.²³ While a detailed analysis of the particular legislative framework that attaches to Fonterra is beyond the scope of this report, it's brief summary highlights the fragility of hybrid cooperative structures, particularly when executive management are able to use increasingly complex business structures to escape from democratic member control.

While the author of this report accepts that the cooperative business model may not be best suited to global ventures at scale, there remains the question of exactly what it is that the members want, and how a cooperative can better protect the interests of members when those interests do not align with the strategic plans of its executive.

The cooperative company has some good features and it has served its farmer members well for 24 years, but it needs to reclaim and reinforce the cooperative side of its hybridity or it may risk losing its relevance. The IPSA needs modernising and updating and this provides a new opportunity for the cooperative sector in New Zealand to refresh the memories of those legislators and policy makers who might be involved in its renewal.

²³ A Fox, "Fonterra shareholder views on their embattled 'watchdog' council to be shared." NZ Herald, 20 February 2020, https://www.nzherald.co.nz/business/news/article.cfm?c_id=3&objectid=12309421

