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3rd Consultative Forum on Coffee Sector Finance
10 September 2013
Belo Horizonte, Brazil

Case Study B
The emerging phase:
Registration as a legal entity

Background

1. The 3rd Consultative Forum will take place on Tuesday, 10 September 2013 from 09:00 to 17:30 in Belo Horizonte, Brazil; during the week of the 111th Session of the Council (information about these meetings is contained in document ED-2153/13). The objective of the event is to identify best practices and disseminate information to Members about aggregation as a platform through which access to finance and risk management could be achieved more effectively. The terms of reference developed by the Core Group were circulated in ED-2158/13. The Forum will be attended by ICO Members, observers and private sector representatives. In addition, experts in farmer aggregation from different geographical and coffee-growing regions have been invited who will form an 'Expert Nucleus' for the session. The programme for the Forum will be circulated separately.

2. A set of seven case studies with discussion questions has been prepared by consultants as the basis for small group discussions amongst delegates and experts. The purpose of the scenario exercise is to engage the entire audience in identifying best practices and the challenges that farmers face in developing farmer organizations or efficiently achieving the objectives of their organizations. This document includes the following case study: **The emerging phase: Registration as a legal entity**.

Action:

The Consultative Forum is requested to review and discuss this case study.

Managing and Growing Farmer Groups Group Discussion

Case Study B:

THE EMERGING PHASE:
REGISTRATION AS A LEGAL ENTITY

BACKGROUND

One of the most important tasks to be accomplished in the transition from informal farmer group to cooperative is registration, which establishes the organization as a legal entity, thus enlarging the scope of action the cooperative can undertake (e.g. borrow money) while also subjecting it to a stricter and more comprehensive range of external regulations that govern its performance. This important legal step also entails considerable organizational and individual attitudinal and behavioral changes if the transition is to be successful.

Cooperative Training, by Stephen Gudz

This Case Study is based in a country that went through a centralized economy after independence, followed by a long civil war before transitioning to a multi-party democracy with a market economy. At that point, the existing legal framework for cooperatives was a mix of old colonial legislation, post-independence communist-style laws, and more recently approved laws and decrees. The resulting confusing legislation remained in place for almost two decades and proved to be a significant obstacle to the growth of the cooperative sector. For example, registering even a small association (of any kind) could only be done in the capital. Each member needed to submit an ID card, birth certificate, police clearance, and other irrelevant documentation. Total cost of registration was in the order of USD$500, which could not be done without NGO financial support.

Passage of the new Cooperative law required a decade of concerted lobbying efforts by local farmer organizations, as well as extensive public education using studies that fed into seminars in which ministers, key government officials, parliamentarians and civil society institutions participated. With international legal support, a first draft of the new law was drawn and widely discussed during regional consultations organized by farmers' associations. The comments and suggestions from these meetings were then forwarded to a national workshop for discussion and incorporation into a revised version, which was then presented at another seminar in which senior government officials, lawyers, representatives of farmers' associations, and NGOs actively participated, before being submitted to the relevant Parliamentary Commissions.

This elaborate participatory, time-consuming approach resulted in a number of innovations being inserted:

- Cooperatives as autonomous economic units, whose management is accountable only to the members, rather than some kind of social organization;
- Cooperatives as a special kind of businesses, not aimed at maximizing returns on investment but at achieving optimum prices for its members;
- The law laying down only the basic obligatory and essential requirements, while leaving the regulation of all particulars to the cooperatives themselves;

- The rule stipulating one vote per member was modified to allow for limited proportional voting.

Subsequent to the passage of the new Co-op Law in 2010, a national association for the promotion of modern co-ops was created and was been supported by an international cooperative NGO. Three years after adoption the cooperative movement consisted of an apex association with 2,234 cooperatives and pre-coops with about 165,000 members working in areas of coffee, agro-livestock, credit, health, industrial enterprises, and housing.

THE CASE STUDY

With the passage of the new legislation, 18 informal farmer groups coming from 14 villages within a 45 km radius consolidated to register as the Progressive Coffee Growers Cooperative (PCGC) with almost 2000 members. The decision to consolidate was taken at a meeting of the group chairmen, sponsored by a local NGO. Later, when the decision was reported back to the members, 3 groups reversed the decision and dropped out.

Another important decision taken at the initial formation meeting was to have the current chairmen of the groups constitute the Board of the new cooperative; they in turn elected the officers of the PCGC. An older village chief, who had been the last Chair of the local post-colonial co-op, was elected President; the other officers elected were mainly large growers, whose political connections had secured large plots of land when the plantations had been broken up. The assembly also voted to adopt, in total, the model set of by-laws written by the Department of Cooperatives. This included a provision for an Annual General Meeting to be held in one year. The Directors would meet quarterly, while the Executive Committee was to meet monthly. Although the former government co-op manager was hired for that position as a matter of respect, the expectation was that his deputy – the son-in-law of the Vice-president – would do most of the work.

Much of the Board's time in the first year was spent on conducting an internal assessment (mandated by the donor support project) and in training - conducted primarily by Department of Co-op staff, who attended every Board meeting and assisted by drawing up the agendas. A member needs assessment was conducted to be used as the basis for developing a strategic plan sometime during the second year. Although the Board was instructed to hold regular meetings with their members, few did due primarily to the farmers' busy schedules and a growing lack of interest in attending meetings just to hear the reports coming from the Executive Committee.

The main goal for the PCGC was securing a market either with an export trader in the capital or (ideally) with an international company. This necessitated relatively frequent travel by the President to the capital, eventually requiring a slight increase in membership dues. The effort was successful and a contract to buy all of the members' coffee that met standards was signed; previously as an unregistered farmer group, they had to have an NGO sign any contract on their behalf. This pleased the members, who expected a significant increase in farm gate price over what they had been receiving from local traders.

The other main PCGC activity consisted of setting up a training programme for the members on correct pesticide use conducted by the Ministry of Agriculture. This was based on a notice from Ministry HQ that the presence of red-listed pesticides was threatening the market with international buyers. Most of the members attended – there was a free lunch provided by a local NGO—but little change occurred in practice as price and availability were the determining factors for which pesticides were used.

Other events during the first year included:

- Two months prior to harvesting, the Ministry of Agriculture tasked the PCGC with estimating the forthcoming harvest; the Board members were given that responsibility, which took much of their time for the next three weeks.

- One of the prevalent themes in the member survey was the lack of adequate health care; a sub-committee was formed at the Executive Committee, which devoted much of their meeting time to the issue for several months but without coming up with any solution other than applying for a grant from the Ministry of Health.
- A delegation was sent to meet with the branch manager of the national agricultural development bank to see about acquiring a loan to be used for purchasing inputs the following season; they were told that as a legal entity they were eligible for a loan but with no credit history and little collateral, the bank would only be able to supply about 25% of what they were seeking.
- The manager resigned after 4 months, citing the constant interference of the Board in day-to-day management decisions; his deputy took over and the issue disappeared.
- Noting that historically significant price increases usually occurred 2-3 months after harvest, the Board decided that it would be to the members' benefit to hold the beans, watch the price fluctuations, and sell later in the year. When told of this decision, most members were against the idea, saying that they depended on the coffee income to pay school fees. The issue was brought back to the Board by several of the group chairmen but was defeated in a vote that ended in voices being raised.
- The rumour started circulating that the PCGC President had cut a deal with the company and was going to receive a kick-back. He denied it and an audit committee was set up from within the Executive Committee to investigate. The committee found no evidence of wrong doing.
- The price published at harvest by the exporter was slightly higher than what the traders were offering, but less than last year's price. His explanation (that the international market was flooded depressing the price) was sent in a letter, which was read to the farmers but most didn't understand it and few were convinced.

At the end of the marketing season, the volume sold was about 15% less than expected based on the harvest forecast done for the Ministry. The farmers claimed that it was because of a poor harvest due to bad weather, but the general consensus among the Board was that farmers had sold at least a portion of their crop to the traders—probably for school fees. In 5 of the groups, the quality was Grade 4-5, and a large portion of the crop in another group was contaminated with foreign matter, including rocks to increase the weight. In spite of these hiccups, the Exporter was generally pleased and voluntarily pledged a second, bonus payment based on his selling price.

By the time of the annual meeting – postponed twice to give the treasurer enough time to prepare his financial report – membership had decreased by 8%. The Annual General Meeting (AGM) was planned as an all-day event to take place in the President's home village. Attendance was higher than expected – more than 400 members were present, but they came mainly from the nearby groups. The President gave his report followed by the Treasurer's accounting; the audit report was not ready due to a backlog in the Co-op Department. The other Committee reports took up most of the remaining time, leaving only 45 minutes for new business from the floor. The meeting was followed by a meal paid for by the sales commission earned by the co-op. All of the attendees felt the AGM was a great success.

CASE STUDY DISCUSSION QUESTIONS

1. What were some of the mistakes committed during the first year of CMCG? How could matters have been handled better?
2. How did government contribute to the development of CMCG? How did it hinder? What additional kinds of support could government provide without compromising CMCG's autonomy?
3. What were the strengths and weaknesses in the process of developing the new Co-op Law?
4. What recommendations would you give to CMCG for its second year?