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Agricultural Cooperatives in the County of Trento (Italy): Economic, Organizational and Legal Perspectives

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Abstract
At present, agricultural cooperatives, like all cooperatives, are faced with many challenges. They are questioned about their organizational and management framework, their relations with local communities and with the market. In Italy, there is an ongoing debate relating to how cooperatives at large should or are supposed to evolve in a context in which the market pressure seems to overcome the traditional characteristics of the cooperative movement (mutuality, solidarity, the "one head one vote" principle, and so on). How to adequately balance the innovation thrust and the cooperative principles? How can agricultural cooperatives develop in the face of the ever overwhelming market forces? Is the legal framework provided for cooperatives still competitive? By taking into account the long-rooted experience of agricultural cooperatives in the County of Trento, the authors intend to analyze the main economic, organizational and legal problems affecting these cooperatives. On examining these problems, the article also intends to bring about some proposals and recommendations for the future developments of agricultural cooperatives.

Introduction
The County of Trento is one of the Italian geographical areas in which there is a wide-spread and long-rooted presence of agricultural cooperatives. Since the nineteenth century, more than 80 percent of the local agricultural production has been processed and marketed by means of a well developed net of cooperatives. The reasons for the development of this particular typology of enterprise are to be found in a complex historical and cultural tradition as well as in the specific structure of the local agricultural sector. This revolves around a system defined by small-sized, family-based enterprises, which are oriented towards a highly labor and capital intensive production.
Over the years, it has been through organized cooperatives that some of the many problems deriving from the weaknesses of the single cooperatives, with respect to the market in which they operate, have been dealt with and partly solved.

Originally, the cooperative movement in the County of Trento referred to the German Reiffeisen model. Later on, although one of the main characteristics of this model, namely, the strong linkage with the local area, has been maintained, cooperatives in Trentino (the County of Trento) have progressively diverted from it. In fact, they have oriented themselves towards specialization. Consequently, at present, in one given local area (i.e. city council) there can be more than one agricultural cooperatives. Each carries on its activities in one single production sector (for example, wine, fruit, milk, and so forth). In the past, vertical integration was pursued through second-level cooperative organizations, whereas the integration with other cooperatives (credit, consumption, work) has occurred only occasionally and often only by virtue of good neighborhood relations rather than as the result of an institutional strategy (Piccinini, 1994).

After years of successes, including economic ones, the organizational model of agricultural cooperatives in the County of Trento is presently debated. The changes in the socio-economic processes have undermined the validity of the existing model. Thus, after a period in which transformations have been dealt with by increasing the number of first level cooperatives, nowadays the main question relies on the opportunity of adopting different organizational frameworks. This article, then, places itself in the ongoing debate.

The article is structured in three parts. In the first part, the theoretical reasons underlying the strengths and weaknesses of the cooperative organizational model will be presented. In the second part, some proposals concerning the possible solutions, including the legal ones, to some of the problems presently affecting the agricultural cooperative movement in the County of Trento will be offered. Finally, the third part of the article will present some essential conditions that are deemed necessary to ensure that the changing processes may successfully last over time.

Peculiarities and effectiveness of cooperatives

As economic organizations, it is obvious that cooperatives are affected by the social and economic context in which they operate and that they interpret the spirit of their time (Pacciani e Petriccione, 1993). In the past, cooperatives were mainly regarded as organizations pursuing political and ideological purposes rather than economic ones. On the contrary, over the last decades, cooperatives have progressively adapted to the market. The peculiarities of cooperatives, which are established on the consistency with the three basic principles of mutuality, solidarity
and democracy, urge to adopt specific organizational rules and provisions. These, though, are different from those used in for-profit companies.

Given the abovementioned peculiar aspects, it is necessary to consider what are the essential conditions and aspects that may allow agricultural and food cooperatives to be effective on the contemporary market, which, in many respects, is different from that of late nineteenth century, when cooperatives were established. These aspects or rather their importance is often underestimated. Such an approach concerns the whole European agricultural cooperative movement (COCEGA, 1998). It especially relates to the County of Trento as to both the role of agricultural cooperatives in this area and the fast process changes defining the area itself.

The concept of mutuality

Despite many uncertainties and doubts concerning the meaning of mutuality, it is necessary to underline that its essence is normally presented under two different aspects, namely, internal and external mutuality (Bonfante, 1977). The latter is referred to the fact that cooperatives pursue a goal that goes beyond the immediate interests of the members and relates to purposes affecting the collective welfare. External mutuality, which, in some respects, justifies a specific legal and tax treatment of cooperatives, is indeed an important aspect of the cooperative movement at large. Nevertheless, given the scope of the present article, the motivations and the consequences deriving from the concept of external mutuality are not dealt with here. However, those motivations and consequences cannot be forgotten if a comprehensive thinking on cooperatives is sought.

As to internal mutuality, it can still be properly and adequately defined with the words used in the Report to the Italian Civil Code of 1942, No. 1025, namely, as “mainly a mutual purpose consisting of supplying goods and services or work opportunities directly to the members of the organization at conditions that are more convenient than those on the market”. In the light of this definition, it is then necessary to consider whether, in the present market situation, the stringent rules imposed by internal mutuality so as to prevent speculative diversions, help cooperatives to pursue their goals. Moreover, it is necessary to examine to what extent the agricultural cooperative system of the County of Trento, which is based upon relatively small-sized enterprises, mainly operating on national markets and

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1 Among these, let us here recall only the following: the “one head, one vote” principle; the “open door” principle; the mandatory provision aimed at transferring profits into reserve funds; the maximization of the value of the factors bestowed in the management; the cooperative education and inter-cooperative collaboration.

2 Recently, the Italian Ministry of Finance (Regulation No. 89/E of 12 June, 2001) has reinforced the importance of external mutuality as the precondition for cooperatives to benefit from some tax exemptions: “(...) The mutual aim is tied to, for fiscal purposes, the prohibition of distributing profits with respect to the capital invested which are higher than the legal interest rate and to the indivisible nature of the cooperative’s assets”.
established on strong solidarity ties, can be questioned. In other words, it is necessary
to ask to what extent the nature of cooperative enterprise can match the effectiveness
and development conditions without diverting from the interests of the agricultural
world. All the same, it is important to assess when agricultural cooperatives are to
adopt a different model of enterprise.

The reasons for competitiveness of cooperatives

To answer these questions, it is useful to take into account the reasons why
cooperatives may appear to be more competitive than for-profits and the reasons why
the latter can be more effective than the former.

With special reference to agricultural cooperatives, the reasons for a greater
competitiveness of cooperatives may be the following:

• The presence of situations linked to asymmetric information (Hansmann,
1980). Indeed, when there are information asymmetries, that is, when the
different economic actors possess different information and some information
is available, either on the whole or partly, only for some operators, the market
standard mechanisms are not wholly effective. Under these circumstances, the
organizational forms based upon trust networks, as cooperatives should be,
can be more effective (Sextan, 1990). In the case of agricultural products,
asymmetric information may derive from at least three aspects. The first is
related to the size of production. Given the characteristics of the agricultural
production process, which rests on biological mechanisms, the quantities being
produced are to be determined only within very wide ranges of fluctuation.
Hence, the storage of all the produce has long been the main problem of
agricultural enterprises, especially for those agricultural products difficult to
store away. The importance of the cooperative as the guarantor capable of
collecting all the quantities produced has proved itself until recently. Yet,
over the last few years, the changes in agricultural techniques and higher
effectiveness of market mechanisms have made this function of cooperatives
much less important than in the past.

The second aspect refers to the quality of products. In this respect, it is useful
to stress that the implicit qualities of agricultural and food production are not
easy to assess upon purchase. Consequently, the reputation of the producer
or seller becomes essential. In Italy, according to some surveys, consumers
tend to prefer products supplied by cooperatives than by other enterprises. The
importance of this aspect is growing but it is not always adequately used by
agricultural cooperatives in the definition of their marketing strategies.

The third factor is concerned with the relations with local communities.
In the case of the County of Trento, where agricultural cooperatives have
been developed along the Reiffeisen model, they tend to present a stronger
reputation compared to other entrepreneurial organizations. Indeed, the direct knowledge of their members and the fact that profits and investments are kept within cooperatives make them comparatively more trustworthy. Although this third aspect is bound to become more and more important in the future, the cooperative movement seems to underestimate it. In this respect, let's consider the legal provision according to which, upon winding up of the cooperative, its final assets are to be transferred to the Italian cooperative development fund rather than to the local community. This provision, which has been strongly endorsed by the Budget Law 2001, is aimed at maintaining all the resources available within the cooperative movement. Nevertheless, it prevents the single cooperative from deciding which community purpose to serve best. In fact, it is the national cooperative development fund that is in charge of channelling the assets or capital it gets from winding up cooperatives. The risk of this mechanism is to perpetuate a kind of *manomorta*³ in the hands of a national board that is not linked to local communities;

- The capacity of attracting low-cost or zero-costs (e.g. volunteers) energies. This represents a fundamental function performed by cooperatives, especially in their start-up phase and in small-sized cooperatives (Zandonai, 2000). However, the same capacity loses its importance in large-sized cooperatives. The ever growing complexity of decision-making processes and the necessity of acquiring highly skilled know-how reduce the possibility of using voluntary work even in the board of directors, where, up to recent time, this was the general rule;

- Reduction of opportunistic behaviors. This aspect is particularly important when the tools to analyze the products delivered are either not available or are available only at very high prices. It goes without saying that the reduction of opportunistic behaviors is closely linked to the sense of belonging that the members feel and to the mutual control among themselves. Obviously, all these are factors more likely to be detected in small-sized cooperatives and with relatively limited number of members;

- The control of processing by producers leads to choices that may advantage the producers themselves. In fact, it has been demonstrated (Ferretti, 1994) that if the objective is the maximization of the processing price, this being, as in the case of cooperatives, the difference between the value of final products and the production costs, the organizational ways of the production process are different from those prevailing under the same circumstances, should the objective be the maximization of profits (Le Yay, 1983). The greater the

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³This term refers to the nineteenth century Italian legal experience in which large charitable organizations, especially those linked to the Catholic Church, were accused of possessing rich assets bound to specific given public purposes. On the contrary, the Enlightenment ideology of the time wanted these assets to be used "on the market" (Santuari, 1997).
differences the less the share of the final price of the product is represented by
the price of the agricultural product and the more heterogeneous the production
by members, both as to quantity and quality.

Cooperatives vs other enterprises: some disadvantages

By contrast, in the present socio-economic scenario, cooperatives present some
disadvantages with respect to other entrepreneurial organizations. In the specific case
of cooperatives operating in the processing and sale areas, these disadvantages can
be summarized as follows:

1. Under capitalization due to both small start-up capital and the difficulties in
financing through either self-funding or market capitals. In Italy, the problems
relating to this particular aspect have been only partly solved with the passing
of Law No. 59, 1992. This has introduced a new category of members, namely,
the “financing members” and the so-called cooperative participatory shares.
However, these two tools have not been actually implemented. In fact, the
small percentage of profits that the law allows to be distributed to the members
does not represent an appealing incentive for any potential capital investor;

2. The difficulty in adapting the dimensions of the organizations to the changed
needs of the market. Unlike traditional companies, the dimension of
cooperatives – which are influenced by the quantities of products delivered
by the single farmers – can adapt itself only slowly. In fact, new actions, such
as mergers and the recruitment of new members, are necessary but at the same
time imply a high degree of energy waste and changes in the cooperative’s
membership. This difficulty becomes even more evident in a situation, like the
present one, in which the market is characterized by rapid changes;

3. The difficulty in finding an adequate mix of products aimed at sustaining
appropriate marketing strategies. This difficulty increases in those cooperatives
that are specialized and have members spread within a small geographical area.
In these cases, not only are cooperatives confined to one single product (for
example, apples or grapes) but also grow a reduced number of varieties due to
the constraints imposed by the orographic and environmental conditions;

4. The management rigidity, which progressively increases according to the
dimensions, and the fact that members become heterogeneous and holders of
different interests;

5. The de facto separation between property and control (Zago, 1998). In many
cases, indeed, the actual power is concentrated in the hand of directors and
managers. They can work with wide discretion and they are entrusted with
powers that are subject to limited checks. This occurs because there is no
precise indicator to measure the success of management in an enterprise as is
the case for profits in companies;
6. The necessity of producing satisfactory results in the short term for the members in order to avoid tensions in the membership may contrast against the growth and balance of cooperatives in the long run. This also relates to what has been described in the foregoing paragraph concerning the difference existing between the maximization of the processing price and of profits in terms of management models.

**Discussion and conclusion**

Given the start-up conditions, the probable evolution of the socio-economic scenario, the comments on the pros and cons of the cooperative formula, the solutions that can be detected to allow the agricultural cooperation to keep on effectively matching the members' income exigencies vary. Indeed, due to the heterogeneity of cooperation in the County of Trento it is difficult to find out a single answer likely to be the same for all the situations. Particularly, one may state that in some cases, in other European countries, the "double legislation" way has been chosen (Saccomandi, 1992). This implies that while maintaining the legal and tax status provided for mutuality, a parallel specific legislation for commercial cooperatives has been designed. This provides for the relaxation of the mutual constraints, which have been balanced with less tax benefits and public funds. Doubtless, this represents an interesting experiment. Nevertheless, it cannot be tackled in this article since it deals with decisions to be made by the national parliament, which at the moment are not foreseeable in the short run.

A second choice could consist of pursuing an increase in the dimensions. This may occur not through mergers, as has been the case until now, the results of which have not been always satisfactory. On the contrary, the adoption of specific contractual provisions with long run validity and affecting particular aspects related to some phases of delivery, processing and marketing of products, could prove effective. In this case, the guiding principle should be identified with subsidiarity, that is, to keep decentralized all that is possible and to centralize only what is strictly necessary. This avenue could be used in all those cases in which:

- the optimal dimensions are different for the different phases of the activity of cooperatives;
- there is a similarity among different first-level cooperatives;
- there is no necessity for large fixed investments for the phases being centralized;
- the effect of fixed costs is exactly definable and likely to be shared among the different associated organizations, since it relates to a very precise phase of manufacturing.

In the specific case of agricultural cooperation in the County of Trento this could well be the alternative solution to mergers of wine cooperatives. It could also be a
viable solution for joint purchase of the expensive machinery needed for the selection of fruit warehouses.

A third way would imply maintaining the mutual model for first-level cooperatives. These, in their turn, set up or take part in joint stock companies, in which organizations other than cooperatives might be interested too. This organizational model would consist of a community-based company in which 60 percent of the total shares are owned by one or more cooperatives, whereas the remaining 40 percent would be owned by local investors. This pattern may represent an alternative to the traditional cooperative model that is based upon integration among first and second-level cooperatives. Such a solution could be implemented when simultaneously:

- it becomes necessary to quickly find large investments of fixed capital;
- the costs of the different functions carried out are not easily identifiable;
- the markets in which cooperatives operate are dramatically expanding and allow for high levels of income;
- there is a kind of natural monopoly connected to the quality of the product, which makes it difficult and/or inconvenient to replace the product of members with that of others.

In the case of agricultural cooperatives, this solution is to be linked to forms of protection, such as “d.o.c.” or “d.o.p.” These are forms of protection designed by the European Community to safeguard the origin of products. Yet this solution presents the danger of potential conflicts of interest among the different members of the enterprise thus established. These dangers increase in case of crises on the market in which the cooperative operates. Furthermore, such a solution requires a particular attention towards the institutional framework, which is to provide the membership with adequate guarantees. For instance, it could be agreed that the trademark of products remains the property of the cooperative and only its use and management can be vested with the joint stock company. By adopting appropriate tools and despite the potential dangers described above, this solution, in some cases, appears to be successfully capable of increasing the overall effectiveness of the system. In this particular respect, the bill relating to the reform of corporate governance provides that in the future cooperatives may appeal to the market by issuing specific financial tools endowed with different administrative ownership rights for the holders (Bonfante, 2000).

Finally, in some cases, cooperatives may decide to set up private limited liability companies or similar organizational forms to manage a specific function. This solution does not display any specific hazards, except for those linked to the

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4 d.o.c.: article with controlled origin; d.o.p.: article with protected origin.
duplication of structures, the decrease in accountability and more difficulties in carrying out the relevant control.

However, setting the organizational model aside for the time being, the possibility for cooperatives of being successful is connected to at least four basic conditions. Firstly, in some cases, the failure of cooperatives is to be attributed to the management because of lack of professionalism and of adequate checks by the ownership. Should the organizational framework be changed without solving the management problems, it is unlikely that the difficulties of cooperatives may be overcome. The recent changes in the legislation concerning the corporate governance (Bonfante, 2000) could help in this respect. Indeed, the proposed legislative modifications would allow to change choices and behaviors, especially since the bill drafted extends to cooperatives the possibility of linking remuneration of managers with the outcomes they are capable of achieving. The bill also introduces the possibility, for cooperatives, of appointing non-members on the board of directors. This cannot but be a “must” when cooperatives operate in sectors that imply a high level of specialization in their management.

Secondly, a potential conflict between equity and effectiveness cannot be neglected (Fultan, 1995). This conflict can be solved in different ways according to the different rules applied. The most effective rules lead to a greater discrimination among members. To treat producers who provide differently qualitative products in the same way brings to the disintegration of cooperatives. The same result would follow the introduction of differences which are not accounted for. The problem concerning the transfer onto producers of the market price difference cannot be solved by introducing changes in the organizational framework. The definition of simple and comprehensible parameters to assess the quality is an essential and priority element. Furthermore, producers are willing to accept the market as their arbitrator rather than the board of directors.

Thirdly, it is necessary for cooperative members to regain the taste for participation. Without participation, no matter what organizational model, the cooperative movement has no future. It follows, therefore, that the relationships among members are not to be formal and occasional but intensive and decisive. In this respect, the proposed change introduced by the bill on corporate governance, which is aimed at, though only in some cases, diverting from the traditional “one head, one vote” principle, needs further thinking.

Finally, one is to observe that if innovation is necessary, it presents risks too. In any case, every action or intervention aimed at preserving the very essence of the cooperative form as the entrepreneurial form built on the principles described at the beginning of this article, can be of much help.

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