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**XXIII Congrès et Colloque Européens de Droit Rural
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Round Table – Table ronde – Runder Tisch

**AGRICULTURAL COOPERATIVES – EVOLUTION, IMPORTANCE,
PERSPECTIVES**

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Agricultural Co-operatives – Evolution, Importance and Perspectives

1. Generalities

- 1a.** The Agricultural Co-operative hasn't really flourished in England and Wales, the literature instead refers to FCB's (Farmer Controlled Businesses) most of which are in fact constituted as limited companies rather than co-operatives under the terms of the Industrial and Provident Societies Act. An industrial and provident society is an organisation conducting an industry business or trade either as a co-operative or for the benefit of the community, and is registered under the Industrial and Provident Societies Act. Co-operatives are run for the mutual benefit of their members with any surplus being ploughed back into the organisation to provide better services and facilities. A society for the benefit of the community, an industrial and provident societies number ends in R or RS. An Industrial and Provident Society is registered with the Financial Services Authority.

It is interesting to note that the "co-operative development model" provided by Co Active, the co-operative development agency for the south west of England provides for a company limited by guarantee and not an industrial and provident society. A company limited by guarantee is normally incorporated for non profit making functions. The company has no share capital and has members rather than shareholders, the members of the company guarantee to contribute a predetermined sum to the liabilities of the company which become due in the event of the company being wound up. A member's contribution is normally £1. The Memorandum of Association of the company usually includes a non-profit distribution clause and these companies are usually formed by clubs, professional trade or research bodies. A company limited by guarantee is registered at Companies House.

A survey carried out by English Food and Farming Partnerships in 2001 found that there are currently 563 farmer controlled businesses in the UK. Of these, 221 are constituted as Industrial and Provident societies, 154 as private limited companies (limited by guarantee) and 6 as public limited companies. The remaining 177 gave no response as to their legal constitution.

The farmer controlled businesses employ 13,600 staff and have a combined membership of 241,000 producers. The major share of turnover of these businesses is accounted for by the marketing of members produce amounting to £5.4 billion in 1999.

- 1b.** Co-operatives have their roots in the late 18th and early 19th centuries during the industrial revolution.

The co-operative venture launched by the Rochdale Pioneers in 1844 is generally seen as a turning point in the growth of the co-operative movement. The Co-operative wholesale society now the co-operative group was set up as a supply organisation by Rochdale and other retail societies in 1863. The society began to manufacture products for sale in co-op stores and developed the co-op brand and set up the country's only co-operative insurer as well as the co-operative bank. A

federal body for all co-ops the co-operative Union (now Co-operatives UK) was established in 1869.

2. Definitions – sources

- 2a.** Whatever its legal constitution to be recognised as a genuine co-operative, a business will have the following characteristics:
- It will be carrying on an industry, business or trade;
 - It will be run primarily for the benefit of its members;
 - Control will be on a one member one vote basis;
 - Interest paid on money borrowed must be limited;
 - There must be no artificial restrictions placed upon membership;
 - It will be a “not for personal profit” organisation.
- 2b.** Co-operatives which are not constituted under the Companies act are subject to the Industrial and Provident Societies Act 1965, as discussed below in the context of Agricultural Co-operatives.
- 2c.** There is no statutory or other general definition of an Agricultural Co-operative that applies. Such a co-operative may be as between farmers, or between farmers and others manufacturers or marketers as the members of the co-operative decide. Although to benefit from the exclusions from competition, regulations and tax more specific criteria must be met.
- 2d.** Agricultural Co-operatives as other forms of Co-operatives are governed by the provisions of the Industrial and Provident Societies Act 1965. There is no separate statute for Agricultural Co-Operatives which register as Societies under the Act.
- 2e.** Any society registered under the Act (including any Agricultural Co-operative) is free to define its own rules - but they must contain provision for the following:
- The name of the society;
 - The objects of the society;
 - The place which is to be the society’s registered office;
 - The terms of admission of members;
 - The mode of holding meetings, voting rights and the means for altering the rules of the society;
 - The appointment and removal of the committee and the officers of the society;
 - The maximum number of shares which a member can hold;
 - Provision as to whether shares are to be transferable and the mechanics of how shares can be transferred;
 - Provision for the auditing of the societies accounts and the appointment of auditors;
 - How any profits made by the society are to be used or distributed to members;
 - Whether the societies funds can be invested and if so where.

3. Constitution of the Agricultural Co-operatives

- 3a.** The most common objective of an Agricultural Co-operative is to provide a mechanism whereby individual farmers can join together to gain marketing strength to improve the profitability of their core businesses.
- 3b.** There are no regulations on the capital constitution of an Agricultural Co-operative save for those contained in the provisions of the Industrial and Provident Societies Act.
- 3c.** Anyone can be a member of a co-operative society if the terms of the Society admit them, please refer to the answer to 3b above.
- 3d.** The only state control of the constitution is via the Industrial and Provident Societies Act as referred to above. Although where a co-operative wishes to take full advantage of the tax concessions available, other criteria must also be met. See below.
- 3e.** The Statute for a European Co-operative Society was put to consultation in a Document prepared by HM Treasury in 2001. Given that the implementation deadline for the European Co-operative Society statute is late 2006, the Treasury advises that it intends to publish a further consultation document on the legislation to make this statute effective in UK law by the end of 2005. No firm timetable however, has been set.

4. Organisation: Organs of direction of agricultural co-operative societies

- 4a.** The societies whether companies or Industrial and Provident societies determine their own organs of direction. Although for an industrial and provident society the one-man one vote rule applies, a limited company may decide to allocate voting rights proportionately to shareholding.
- 4b.** A co-operative constituted as an Industrial and Provident Society is governed by the terms of its constitution and one constituted as a company by its memorandum and articles. An example of the type of corporate governance operated by an agricultural co-operative can be taken from Anglia Farmers Ltd. This co-operative is an Industrial and Provident Society. It has a Board of 8 directors and the chairman all of whom are farmer members of the co-operative save for the Chairman who was formerly a partner in a multi national firm of accountants. Directors' contracts are available to members to increase the accountability of the board. The members' capital investment results in a share allocation limited to a minimum subscription of 50 £1 shares. The only benefit to the structure of the co-operative as an Industrial and Provident Society is that its mutual status means that it pays no tax on its trading profit. However it is anticipated that in the longer term an Industrial and Provident Society may not be the most appropriate structure for an undertaking of this size. The objective of the co-operative is to deliver price reduction to its members on commodities such as feed, seed, fuel and fertiliser through the exercise of its enhanced buying power. The price at which it buys is the price at which it sells with price adjustments being passed to members through rebates only a very small percentage being retained to cover administration costs.

5. Functions

It is impossible to answer questions 5a to 5h with the degree of specificity, which the drafting of the question anticipates. The activity of the co-operative society, its connections

with its members and suppliers, the responsibilities of company members and the means of transmission of shares, are all matters to be specified individually by the memorandum and articles of the society if it is a company, or its constitution if it is an industrial and provident society.

There are no fixed rules on the way the company must interact, the obligations of its members, the means of transmission of shares or the allocation of its profits and reserve funds. All these are matters to be determined either by the board in a meeting or the members in a general meeting according to the individual constitution of the society or company.

The officers and directors of companies have obligations to third parties and a fiduciary duty to the company itself. There are similar statutory obligations for the officers of Industrial and Provident Societies but these are not particular to Agricultural Co-operatives. To take an example to illustrate the role of the co-operative in determining farming production methods: OMSCO (the Organic Milk Suppliers Co-operative) is a co-operative organisation of 300 farmers. Originally constituted as an Industrial and Provident society it now trades as a private limited company. Members of the co-operative who supply milk are required to maintain their certification with both the Soil Association (the Organic standards certification body) and National Dairy Farm Assured. Both of these bodies put independent inspectors on the farm to monitor that the organic and animal welfare standards prescribed by the certification schemes are adhered to. The co-operative itself monitors quality by weekly random milk testing. The objective of the co-operative is the collective marketing of organic milk. However it has only been able to survive and thrive due to a unique niche marketing opportunity with a local yogurt manufacturer Yogurt Valley. The co-operative has a rolling 3 year purchase agreement with Yogurt Valley which guarantees farmers a fixed price for their milk and increasing volumes of milk to supply. Yogurt Valley also provides a bonus scheme to co-operative members which gives them a share of Yogurt Valley's profits. This situation is unusual and has arisen due to the high value which the manufacturer/customer places on sustainable, organic raw materials and not with any power in the market which lies with the co-operative producers.

5.1 Tax

To benefit from taxation as an Agricultural Co-operative the constitution of the society (the co-operative must be constituted as an industrial and provident society to benefit from the special tax concessions) must provide that:

- only members can use the facilities and services the co-operative provides;
- if the co-operative is a marketing agency;
- the co-operative sells on behalf of the growers and never owns the produce;
- members agree to market a certain amount of produce through the co-operative or an amount for processing;
- any surplus is shared out among members according to the amount of business which the co-operative society has taken;

If these criteria are met then surpluses arising from transactions with and services provided to the members of the co-operative are exempt from Corporation Tax. This means that the co-operatives liability for Corporation Tax arises only in respect of profits generated through transactions with non-members and other sources such as bank interest, rents and capital gains.

Model terms are available to co-operatives so that they can conduct business upon mutual terms that benefit from the tax breaks in BIM24020.

Members cannot deduct a loan to a co-operative from their income when calculating the income upon which income tax is payable.

Where a co-operative is engaged in mutual trading:

- its operating surplus is not liable to Corporation Tax;
- its operating deficit is not a trading loss allowable against its members income tax;
- it may not claim capital allowances in respect of capital expenditure incurred for the mutual trade; and
- its liability to corporation tax will be confined to other profits bank interest capital gains and the profits of any non mutual trade derived from trading with any non members,

5.2 Competition

There can be problems with competition law in some circumstances and the Office of Fair Trading (OFT) issued a guidance paper in July 2004 to deal with this issue.

The key rules relevant to collaboration in the farming industry are the Competition Act, Articles 81 and 82 of the EC Treaty and the Enterprise Act.

Under the Enterprise Act, the OFT reviews mergers between undertakings it has a duty to refer to the Competition Commission for further investigation any mergers which it believes have resulted or may be expected to result in a substantial lessening of competition in a UK market.

The OFT recognises the particular position of the agriculture sector and in particular the aims of the Common Agricultural Policy. When applying competition law the OFT must respect the objectives of the CAP to make sure they are not made impossible by the application of competition law. Nevertheless agricultural co-operatives are subject to competition rules.

Most forms of collaboration do not raise any competition problems. It is only where co-operation could appreciably affect the competitive process, by fixing prices, sharing markets or limiting production that the OFT is likely to be concerned.

Some forms of agricultural collaboration are excluded from the Competition Act, agreements between farmers or farmer's associations which concern:

- the production for sale of agricultural products, including livestock, dairy meat and fish products as well as fruit, and vegetables and other crops; or
- the use of joint facilities for the storage treatment and processing of agricultural products.

But the exclusion only applies if the agreements meet certain conditions, the main ones being that the agreements are only between farmers or associations of farmers. For example an agreement between a group of dairy farmers and milk processors would not come within the exclusion nor would an agreement between livestock farmers and slaughterhouses.

Crucially the agreement does not involve an obligation on the farmers to charge identical prices for their products. Arrangements whereby farmers agree to sell through a co-operative and take whatever price the co-operative realises in the market should, however, benefit from the exclusion. The OFT can withdraw the UK agricultural exclusion where it considers that the co-operation is likely or intended substantially and unjustifiably to prevent, restrict or distort competition. The OFT would give the parties an opportunity to discuss the operation of the agreement before withdrawing the exclusion.

An agreement between a farmer's association and another business, for example a buyer in the food chain, may be a vertical agreement. Vertical agreements are excluded from the chapter one prohibition provided that they do not include price fixing. But the law is changing. From 1 May 2005, the UK vertical agreements exclusion will be revoked and businesses will need to satisfy themselves that they are able to benefit from the EC rules exempting vertical agreements which will also apply in UK law. To benefit from these exemptions the agreement must not involve any of a small number of restrictions including price fixing and the parties must not have market shares exceeding 30 per cent of the relevant market.

The agricultural exclusion does not apply to the prohibition on abuse of a dominant position. A dominant position exists when an undertaking has substantial market power. It is highly unlikely that any individual farmer or local co-operatives will hold a dominant position but a national co-operative may do so if the relevant market is not international.

Co-operatives have insufficient market share to influence the organisation of markets for the produce, which they supply. The majority of Agricultural Co-operatives are on a small scale and exist either for the joint procurement of supplies for farms, the sharing of machinery as machinery rings or the marketing of agricultural produce.

6. Dissolution

There are no special rules relating to the dissolution of an Agricultural Co-operative society. The rules are determined by its constitution as an Industrial or Provident Society or a Company.

A Company as wound up (dissolved) upon the making of an application to the court by the members of the company or by its creditors in the event that the company becomes insolvent and cannot pay its debts.

An Industrial and Provident Society may be dissolved by an instrument of dissolution to which at least three quarters of the members have given their consent by signing the instrument. An application is then made to the Financial Services Authority to terminate the Societies' registration on the basis of the instrument of dissolution.

7. Organisation

There has not been any recent restructuring of co-operatives in the UK. They remain a minority undertaking without a significant size or financial stake in the market.

There are no specific legal obstacles to the merger or restructuring of co-operatives they are merely subject to the general provisions of the legislation under which they are constituted. It is not necessary for the merged co-operative to even retain the same legal structure as the founder Organisations. Anglia Farmers Limited is an Industrial and Provident Society formed through the merger of two limited Companies – Loddon Farmers Limited and Mid-Norfolk Farmers Limited, both Norfolk based agricultural buying groups. Staff issues were resolved under TUPE regulations to the new company. The company has since grown further through the acquisition of the Northamptonshire-based Samuel Rose buying group, this was a take over not a merger with the acquiring company imposing its culture and process on the other, The buying group was not a co-operative but part of the larger Samuel Rose Property consultant company.

8. Federation of the Co-operative Societies

The Federation of Agricultural Co-operatives (UK) Ltd doesn't exist anymore. It was an independent representative organisation for producer-controlled businesses. It was the UK forum for developing strategies on their behalf. The FAC paid the UK contribution to

COGECA and nominated delegates to COGECO committees to those jointly with COPA and to the European Commission Advisory Committees. It was also the UK focal point for specific legislation dealing with co-operative type businesses.

English Farming and Food Partnerships has been set up to encourage and promote Farmer controlled businesses, but not exclusively co-operatives. It is telling that this organisation is itself constituted as a limited company. It is encouragement and promotion, which is the reason for the “federation” which are an imposition of government and not a collaboration of co-operatives.