2014

"Sea Water Fish in a Freshwater Pond:" An Institutional Approach to Understanding Cooperative Scarcity in the United States

Caroline E. Malone
Scripps College

"SEA WATER FISH IN A FRESHWATER POND:" AN INSTITUTIONAL APPROACH TO UNDERSTANDING COOPERATIVE SCARCITY IN THE UNITED STATES

BY

CAROLINE E. MALONE

SUBMITTED TO SCRIPPS COLLEGE IN PARTIAL FULFILLMENT OF THE DEGREE OF BACHELOR OF ARTS

PROFESSOR SAMFORD
PROFESSOR CHAUDHARY

APRIL 25, 2014

Acknowledgements

I would like to express my sincere thanks to my thesis readers. Thanks to Professor Samford, for always offering very thoughtful, critical feedback and being so generous with his time. And, thank you to Professor Chaudhary, for providing such helpful comments on my work and pushing me to consider all sides of an issue. I also owe huge thanks to my parents, for their constant love and support. Finally, I would like to thank all the friends who supported me throughout this process and lent an ear whenever I needed to toss an idea around.

Table of Contents

Introduction

On December 18, 2009, the United Nations General Assembly proclaimed 2012 the International Year of Cooperatives. The UN Resolution recognized “that cooperatives, in their various forms, promote the fullest possible participation in the economic and social development of all people…are becoming a major factor of economic and social development and contribute to the eradication of poverty.”[1] Around the world, more than 1 billion people are members of cooperatives. They provide about 100 million jobs worldwide, 20 percent more than multinational enterprises.[2] From Kenya, India, and Vietnam to France, Germany, Canada, and the United States—and most places betwixt and between—consumer, producer, purchasing, and worker cooperatives—as well as some hybrids—exist to meet the needs of people. Some countries witness profound cooperative density while others experience cooperatives as a scarce organizational model. And, in different countries, different cooperative varieties experience differing degrees of popularity and prevalence.

In the United States, about 30,000 cooperative enterprises boast more than 100,000 million members.[3] Over 3,000 farmer-owned producer cooperatives market roughly 30 percent of all farm products in the country today. Close to 6,500 housing consumer cooperatives house more than 1 million households. 270 telephone consumer cooperatives service 2 million homes. Almost 1,000 rural electric consumer cooperatives provide power for 36 million people. 250 purchasing cooperatives serve over 50,000 independent small businesses for the purpose of group buying and shared services. Over

[1] A/RES/64/136
[2] "Cooperatives Around the World." Home. Accessed January 25, 2014. http://usa2012.coop/about-co-ops/cooperatives-around-world.
[3] *Ibid*.

80 million Americans are members of credit unions—a form of consumer cooperatives. And, about 300 worker cooperative businesses operate in the United States.[4]

While, by and large, these figures appear rather impressive, the overall share of the market commanded by cooperatives is rather small and the extreme scarcity of worker cooperatives in particular is striking. In some instances, cooperatives serve as a niche response to market shortcoming, and therefore should be expected to be a small portion of the market; for instance farmer-owned producer cooperatives, telephone and electric consumer cooperatives, and purchasing cooperatives generally perform this function. However, in other instances the scarcity of the cooperative form is more mysterious. The scarcity of credit unions, relative to for-profit commercial banks, and the pronounced scarcity of worker cooperatives generally are particularly interesting.

The UN proclamation touts the benefits of the cooperative form, based on principles of self-help, self-responsibility, democracy, and member-equity, for not only the economy but also for workers. While big, and small, hierarchically structured, investor-owned, for-profit firms dominate the American economy, they may not all be working for the economy and American workers as well as some democratically structured, cooperative firms would. Industrial organization literature seeks to explain why firms organize the way they do. The vast majority of such literature finds that firms organize as hierarchical and investor-owned for purposes of productivity and efficiency (which translate into profit). Other research, however, suggests that institutions do not need to organize hierarchically and be investor-owned to be productive and efficient, even as they grow to be quite large. Research on cooperative ownership reveals that, in

[4] John Curl. *For All the People: Uncovering the Hidden History of Cooperation, Cooperative Movements, and Communalism in America*. Oakland, CA: PM Press, 2009.

terms of productivity, survivability, and longevity, cooperative firms can perform as well as or better than their more conventional counterparts while improving patron or worker welfare and building stronger communities. Somewhere in the contradiction between the UN proclamation and US reality, and the broad, contentious literature regarding cooperatives, I stumbled upon my interest in pursuing the questions of why financial consumer cooperatives (credit unions) and worker cooperatives are so scarce in US and what opportunities exist for cooperatives to scale up in both size and scope. It is my hope that this thesis contributes to creating a more thorough understanding of these questions.

Defining Cooperatives

The International Cooperative Alliance (ICA) defines cooperatives as "businesses owned and run by and for their members. Whether the members are the customers, employees or residents they have an equal say in what the business does and a share in the profits."[5] This broad definition of cooperatives is usefully supplemented by 7 fundamental principles which act as guidelines for putting the cooperative values of self-help, self-responsibility, democracy, equality, equity, and solidarity into practice. These 7 principles are: voluntary and open membership, democratic member control, member economic participation, autonomy and independence, education, training and information, cooperation among cooperatives, and concern for community.[6] Within these cooperative principles and values, a number of different specific forms occur. Different iterations of producer, consumer, worker, and purchasing operate under these values and principles throughout the world. As this paper focuses narrowly on credit unions and

[5] "What's a Co-op?" ICA: International Co-operative Alliance. Accessed February 21, 2014. http://ica.coop/en/whats-co-op.

[6] "CICOPA." What Is a Cooperative? -. Accessed February 21, 2014. http://www.cicopa.coop/What-is-a-cooperative.html#workers.

worker cooperatives, I will provide a somewhat more specific explanation of each, although variation exists within each category.

Credit unions, as a form of cooperative, necessarily conform to the above values and principles. In particular, as a form of mutual financial intermediary, credit unions maintain key features of one-man/one-vote, residual claimants (owners) both supply and use funds, and dividends are distributed to both savers and borrowers.[7] Importantly, because the owners are also the consumers, cooperative banks return their profits to their owner-customers in the form of preferable rates on loaning and saving instruments before distributing any remaining dividends.

Worker cooperatives generally conform to the overarching cooperative definition, but are unique in some ways. Although a hard and strict universal definition of a worker cooperative does not exist—indeed, cooperative 'hybrids' have emerged recently, further complicating matters[8]—several defining characteristics are identifiable. The United States Federation of Worker Cooperatives asserts two central characteristics of cooperatives: 1) "Worker members invest in and own the business together, and it distributes surplus to them" and 2) "decision-making is democratic, adhering to the general principle of one member-one vote."[9] Additionally, dividends are distributed on the basis of worker contribution in the form of time commitment rather than financial contribution.

---

[7] Carlos Cuevas and Klaus Fischer Cuevas. *Cooperative Financial Institutions: Issues in Governance, Regulation, and Supervision*. Washington, D.C.: World Bank, 2006.

[8] See Fabio Chaddad. "Advancing The Theory Of The Cooperative Organization: The Cooperative As A True Hybrid." *Annals of Public and Cooperative Economics* 83, no. 4 (2012)

[9] "What Is a Worker Cooperative?" US Federation of Worker Cooperatives. Accessed November 7, 2013. http://www.usworker.coop/about/what-is-a-worker-coop.

Literature Review

My literature review will proceed in two parts. As I will be narrowly discussing credit unions and worker cooperatives in the body of my thesis, I will first review literature surrounding financial consumer cooperatives and then review literature surrounding worker cooperatives.

Credit Unions

Credit Unions developed in their earliest iterations as the Schulze-Delitzsch and Raiffeisen credit societies in mid-19th century Germany. These antecedents to modern credit unions were developed in response to perceived failures in formal financial institutions. Credit cooperatives could operate where banks could not due to "a detailed knowledge of local economic conditions which allowed these credit cooperatives to more efficiently screen potential members, and thus more easily and quickly identify borrower who might default," which allowed the cooperatives to dispense of high-cost practices and pass along these saving to members.[10] Importantly, the earliest credit unions were built on cooperative principles coming out of Great Britain, with the experiments of Robert Owen at New Lanark and the Rochdale Pioneers, that highlighted the abovementioned values rather than profit-maximization, which is crucial for understanding credit union theory to this day.

Neoclassical theories of the firm are not entirely useful for understanding the economic behavior of any cooperative firm, including credit unions, because such theory assumes that firms seeks to profit maximize. Credit unions, like all cooperative firms, do not primarily seek to profit maximize and thus do not fit this model. As a consequence,

---

[10] Donal Mckillop , and John O.s. Wilson. "Credit Unions: A Theoretical and Empirical Overview." *Financial Markets, Institutions & Instruments* 20, no. 3 (2011). Pg. 6

there is a divide in theoretical literature regarding credit unions. More neoclassical approaches to understanding the firm often predict instability and failure for credit unions, but more flexible approaches to modeling firm behavior have generated credit union predictions that are decidedly more optimistic.[11]

Credit union theory steeped in neoclassical assumptions tends to view credit unions as potential sources of weakness in financial systems. Goodhart (2004) suggests that "the presence of any non-profit maximizing baking entities may make financial systems more fragile."[12] Hesse and Cihak (2007) reflect that "if a cooperative bank's pursuit of objectives other than profit maximization results in very low profitability, its balance sheet risks grow faster than its capital, leading to deteriorating solvency."[13] And, they further suggest that if cooperative banks "accept lower profitability as the price to pay for delivering financial services as below-market prices to retail clients, they may pull down the profitability of the banking system, with negative repercussions for other banks' soundness."[14]

Because credit unions do not fit the model of a profit maximizing firm, a number of authors have offered alternative modeling systems for credit unions to demonstrate how they accomplish stability without a primary goal of profit maximization firm.[15] Unlike the above assumptions, these theories argue that, despite not being profit driven,

---

[11] It is worth note that the literature on cooperative banking is generally rather scarce itself. Heiko Hesse and Martin Cihak (2007) "Cooperative Banks and Financial Stability" IMF Working Paper, Monetary and Capital Markets Department note that "only about 0.1 percent of all banking-related entries in EconLit, a major database of economic research, relates to cooperative banking."
[12] Hesse and Cihak (2007) pg. 5, referencing Goodhart (2004)
[13] *Ibid.*
[14] *Ibid.*
[15] See Smith, P.F. (1971). Financial Intermediation, *in Economics of Financial Institutions and Markets,* Homewood, IL: Irwin Publishing; Taylor, R.A. (1971a). The credit union as a cooperative institution, *Review of Social Economy*, 29: 206-17; and Davis, K. (1994). Prudential regulation and Australian credit unions, *Australian Journal of Management*, 19: 31-46.

credit unions still take profit into account in order to negotiate best serving member savers and borrowers. Importantly, Worthington (2004) notes that credit unions in more deregulated markets (such as the US) must contend with competition and balance the fulfillment of ideological imperatives against survival, necessarily encouraging credit unions to achieve financial stability even if they do not profit maximize.[16] Furthermore, rather than viewing low credit union rates as a source of instability, some consider it an important mechanism for disciplining consumer credit rates offered by banks.[17]

Empirical evidence from credit unions around the world suggests that neoclassical concerns that credit unions will be inefficient as a result of their non-profit-maximizing priorities are for naught. Studies of the returns to scale credit unions experience overwhelmingly demonstrate finding of increasing returns. In the US, at least 6 studies find evidence of increasing returns to scale.[18] Esho (2000) finds increasing returns to scale in Australia.[19] In Canada, two studies from the 1980s find slight increasing returns to scale for credit unions.[20] And, other studies find corroborating increasing returns to scale in both the UK and New Zealand.[21] Not only do these findings of increasing returns to scale indicate that credit unions are operating efficiently, they suggest that credit unions might be well served in sizing up.

[16] Worthington, Andrew C. "Determinants of Merger and Acquisition Activity in Australian Cooperative Deposit-taking Institutions." *Journal of Business Research* 57, no. 1 (2004): 47-57

[17] SeeTokle, R. and Tokle, J. 2000. “The influence of credit union and savings and loan competition on bank deposit rates in Idaho and Montana”, *Review of Industrial Organization*, 17: 427-39. and Feinberg, R.M. 2001. “The competitive role of credit unions in small local financial services markets,” *Review of Economics and Statistics*, 83: 560-63.

[18] McKillop and Wilson (2011), referencing Croteau (1956), Dran (1971), Taylor (1977), Wolken and Navratil (1980), Fry et al. (1982), and Kohers and Mullis (1988)

[19] *Ibid*, citing Esho (2000)

[20] *Ibid,* citing Murray and White (1983) and Kim (1986)

[21] *Ibid*, citing McKillop et al. (1995) and Sibbald and McAlevey (2003)

Sanchez Bajo, and Bruno Roelants. Capital and the Debt Trap: Learning from Cooperatives in the Global Crisis. Houndmills, Basingstoke, Hampshire: Palgrave Macmillan, 2011.

In addition to demonstrating efficiency, credit unions have recently shown their relative resiliency as compared to commercial banks, suggesting that concerns about credit unions being a source of fragility in the financial sector are misplaced. While some researchers suggest that cooperative banks may have greater difficulty adjusting to adverse circumstances and changing risks, others posit that credit unions, by their very nature, engage with less risk and are therefore more stable. Both Hansmann (1996) and Chaddad and Cook (2004) find that credit unions in the US tend to adopt less risky strategies than demutualized ones.[22] The importance of this less risky strategy of cooperative banks was illustrated in the recent financial crisis. Bajo and Roelants (2011) illustrate that in both the US and in EU countries, credit unions were more resilient during the financial crisis and have outperformed commercial banks since; fewer credit unions failed than other financial enterprises, credit unions have maintained higher solvency ratios, and have maintained lending rates higher than other financial enterprises.[23] Credit unions thus demonstrate both efficiency and stability while offering members better rates on saving and borrowing devices.

There is surprisingly little discussion of credit union scarcity relative to commercial banks in the US. But, foremost among explanations offered for credit union scarcity that do not assert inefficiency focus on the relative inconvenience of using credit unions and explain their size and scope in terms of demand for credit unions. Essentially the argument asserts that credit unions generally offer fewer financial products and

---

[22] Henry Hansmann. *The Ownership of Enterprise*. Cambridge, MA: Belknap Press of Harvard University Press, 1996.; Fabio R. Chaddad, and Michael L. Cook, 2004, “The Economics of Organization Structure Changes: A US Perspective on Demutualization,” *Annals of Public and Cooperative Economics*, Vol. 75, No. 4, pp. 575–94.

[23] Claudia B.,

operate on a much smaller scale than commercial banks which creates barriers to attracting a broader customer base. Some argue that credit unions operate in this fashion in order to achieve credit union goals. But, research demonstrating that credit unions in the US achieve increasing returns to scale suggests that credit unions would seek to grow to maximize member benefits. In line with this view, I argue that credit unions are subject to unique regulatory burdens that limit their size and scope, ultimately leading to them being comparatively less convenient than commercial banks. Effectively, there are both supply and demand side reasons for the scarcity as a result of government policy; public policy coercively limits the ability of credit unions to supply banking services, which in turn decreases demand for credit unions.

Worker Cooperatives

Worker cooperatives, like credit unions, find their history rooted in the ideas of Robert Owen and the Rochdale pioneers. These ideas emerged in response humanitarian concern for the poor working conditions created by the Industrial Revolution and sought to create a viable alternative. The viability of those ideas, as they relate to worker cooperative in particular have been greatly contended over. A review of the literature surrounding employee ownership[24] provides insight into various explanations for the scarcity of worker cooperatives and the support for such explanations. Firm performance measured by productivity, longevity, and survivability are often at the center of worker cooperative theory, which speculates about the impacts of employee ownership on a firm. Early theoretical work suggests that employee ownership creates inefficiency by creating

[24] Note that employee ownership research includes non-cooperative style ownership. A large amount of evidence is gleaned from ownership in the form of Employee Stock Ownership Plans that, at times, greatly resemble worker cooperatives in structure. Because of cooperative scarcity, it is useful to include such research.

a free-rider, or 1/n, problem where employee-owners shirk because the fruits of their labor are broadly distributed.[25] Another source of concern with employee-ownership is the presumed inefficiency of costly collective decision making.[26] Additionally, early theory regarding employee ownership contends that employee-owners are likely to be extremely risk-averse, because they have all of their eggs in one basket.[27]

Proponents of employee ownership, meanwhile, theorize that such schemes will do precisely the opposite; they suggest that employee ownership increases efficiency. Proponents assert that employee ownership solves the principal-agent problem[28] by aligning the interests of employees with those of the firm (either partially, through some stock ownership, or more thoroughly, as with cooperatives) and thus incentivizes employees to work harder voluntarily.[29] They argue that the free-rider problem is mitigated by peer monitoring and pressure not to shirk.[30] Additionally, proponents claim that the coincidence of interests created by employee ownership eases collective decision-making costs because conflicts between management and employees are less likely.[31] Critically, some research suggests that a combination of both financial interest and decision-making authority is necessary to capture the benefits of employee

---

[25] See Armen A. Alchian and Harold Demsetz. "Production, Information Costs, and Economic Organization" *The American Economic Review*, Vol. 62, No. 5 (Dec., 1972), pp. 777-795

[26] Hansmann (1996)

[27] *Ibid.*

[28] The principal-agent problem concerns the difficulty in motivating employees (agents) to act in the best interest of their employers (principals) when the two parties have divergent interests. For instance, a simple hourly wage may not induce peak performance from an employee because they do not gain from inputting increased effort that improves their productivity.

[29] Margaret Blair., D. Kruse, and J. Blasi. "Employee Ownership: An Unstable Form or a Stabilizing Force?" In *The New Relationship: Human Capital in the American Corporation*, ed. M.Blair and T. Kochan, 241-298. Washington, DC: The Brookings Institute 2000.

[30] *Ibid.*

[31] Rhokeun Park, Douglas Kruse, and James Sesil, "DOES EMPLOYEE OWNERSHIP ENHANCE FIRM SURVIVAL?," *Advances in the Economic Analysis of Participatory & Labor-Managed Firms* 8 (July 6, 2004)

ownership, making worker cooperatives a strong option due to their inherent pairing of ownership with workplace democracy.[32]

In large part, empirical research supports the arguments made by proponents of employee ownership. By giving employees a financial stake in the company they work for through profit sharing, employee stock ownership plans (ESOPs), or directly as in worker cooperatives, firms generally improve performance relative to similar firms without employee ownership.[33] Studies assessing the impact of employee ownership in the form of ESOPs tend to demonstrate neutral or positive relationships between employee ownership and firm performance, but fail to establish significance individually. Despite lacking individual significance, Kruse and Blasi (1995), performing a meta-analysis of ESOP studies found a significant positive overall relationship and determined that firm productivity improves an average of 4.4% in the year an ESOP is adopted.[34] This relationship lends support to the theoretical finding that employee ownership can incentivize employees to work harder. But, the variability of effects among ESOPs may reflect the impact of differing levels of ownership and the presence of employee involvement in decision making relative to financial stake.[35] There is some conflicting evidence about whether, in the presence of an ESOP, employee participation in decision-making yields positive or negative productivity effects, but the former generally appears to be true.

---

[32] Avner Ben-Ner, and Derek C. Jones. "Employee Participation, Ownership, and Productivity: A Theoretical Framework." *Industrial Relations* 34, no. 4 (1995)

[33] Georgeanne M. Artz, and Younjun Kim. *Business Ownership by Workers: Are Worker Cooperatives a Viable Option?* Working paper no. 11020. Iowa State University, 2011.

[34] Douglas L. Kruse. and Blasi, J. R.. Employee Ownership, Employee Attitudes, and Firm Performance. NBER Working Paper w5277, U.S. National Bureau of Economic Research 1995.

[35] Artz and Kim (2011)

Empirical evidence on worker cooperatives specifically tends to find positive productivity impacts as well. Craig et al. (1995) demonstrated that worker cooperatives in the US plywood industry are between 6 and 14 percent more efficient than their more traditional counterparts with regard to output, holding inputs constant.[36] Bartlett et al. (1992) found higher value-added per worker, indicating higher productivity, among cooperative workers in a comparison of Italian worker cooperatives in light manufacturing with similar similarly sized private firms in the same sector and region.[37] Perhaps something unique about cooperative structure better incentivizes worker productivity; it may be the level of employee investment, the level of employee involvement in decision-making, or the relationship between these two factors.

In addition to productivity, rates of firm survival and longevity are studied as a means for assessing the performance and efficiency of employee-owned firms. Theoretical work cautions that employee-owned firms will be shorter lived than more conventional firms. Vanek (1970) argues that worker cooperatives are often likely to fail as a result of their reliance on internal investment, which is likely insufficient because of members' incentive to keep a greater portion of profits than they ought, rather than reinvesting.[38] Ben-Ner (1995), meanwhile, applies 'degeneration theory' and asserts that cooperatives are likely to degenerate into more traditional firms over time as non-members replaced members. Others claim that cooperatives will degenerate into investor-

[36] Artz and Kim (2011)
[37] *Ibid.*
[38] Jaroslav Vanek. *The General Theory of Labor-managed Market Economies*. Ithaca: Cornell University Press, 1970.

owned firms over time as they grow and become successful because worker-members can sell their shares at a high price.[39]

Empirical support for these theories of cooperative behavior is limited; indeed, empirical evidence suggests that cooperative survival and longevity exceeds that of comparable conventional firms. Robinson and Zhang (2005), analyzing firm survival for a set of UK public companies between 1988 and 2001, found that “companies with employee ownership stakes of 5% or more were only 76% as likely to disappear (merge, be acquired, or fail) compared with all public companies…For 100% employee-owned firms, the relative rate of failure falls to 33.5%.”[40] They found that employee ownership protects investments in firm-specific knowledge and skills for both the firm and the employees. In a study of the viability of employee-owned firms in France, Estrin and Jones (1992) showed that 30% of worker cooperatives across a variety of industries had existed for over 30 years in 1979. Not only did they demonstrate little evidence of degeneration, they also found that the cooperatives were as productive, profitable, and capital-intensive as other firms.[41] Park, Kruse, and Sesil (2004) suggest that employee-owned firms may be more long-lived than other firms because of “functional flexibility in which employees have a broad range of skill, input into decision-making, and a greater willingness to make adjustments during economic difficulties.”[42] The survival rate and longevity of cooperatives suggests that they can act as an important stabilizing force during times of economic recession or downturn. Employee-owned, and more specifically, cooperative, firm structure, then, contrary to early theory on the matter, has

[39] Artz and Kim (2011)
[40] *Ibid* pg. 19
[41] Saul Estrin, and Derek Jones. “The Viability of Employee-Owned Firms: Evidence from France.” *Industrial and Labor Relations Review* 45(2):323-338 (1992).
[42] Park, Kruse, and Sesil (2004) pg. 29

empirically demonstrated to be efficient in terms of productivity, survivability, and longevity performance.

Additionally, it appears that economic measures of efficiency can indeed be compatible with worker welfare. Evidence demonstrates that employee ownership produces better pay, job security, and job satisfaction than other firms do. Blasi, Conte, and Kruse (1996) "found that US public companies with broad-based employee ownership plans [at least 5 percent of stock] had 8 percent higher average compensation levels than other comparable public companies, and compensation increased with the percentage of stock held by employees."[43] And, case evidence for worker cooperatives often report higher compensation as compared with non-cooperative firms in the same industry. Hochner et al. (1988) reveal a grocery cooperative in Philadelphia that "maintained higher levels of full-time jobs at higher wages than competitors without decreasing profits.[44] At a worker-owned grocery in the San Francisco Bay Meyer (2006) showed that average compensation for employees was 40% greater than that of unionized grocery workers in California.[45]

Along with better compensation, evidence demonstrates that worker cooperatives provide greater job security than other firms. Employee-owner participation in decision-making results in a greater tendency among cooperatives to adjust wages rather than cut jobs when the firm is stressed. Craig and Pencavel (1993) show that, between 1968 and 1986, plywood cooperatives in the Pacific Northwest were more likely to adjust wage

---

[43] Douglas Kruse, Richard B. Freeman, and Joseph R. Blasi. *Shared Capitalism at Work: Employee Ownership, Profit and Gain Sharing, and Broad-based Stock Options*. Chicago: University of Chicago Press, 2010 pg. 260
[44] Artz and Kim (2011) pg. 20
[45] *Ibid.*

levels than employment levels compared with other types of mills.[46] Generally, cooperatives are more inclined to adjust wages rather than employment; in times of increased output, cooperatives have demonstrated a tendency to increase wages rather than employment. Blair, Kruse, and Blasi (2000) found in a study of employee owned firms (with at least 20% ownership) in US in 1983 that such firms had a statistically significant lower variance in their annual percentage in employment than comparable, conventional firms.[47] Furthermore, Bartlett et al. (1992) observed that among members, cooperatives have lower quit rates, which has the benefit of allowing for “skill accumulation and learning, which can improve firm productivity and profitability, translating into higher earning for worker cooperative members.”[48] Critically, the job security offered by cooperatives may provide a mechanism for mitigating unemployment during economic recessions.

An additional, less tangible benefit of employee ownership is increased job satisfaction. Evidence shows that workers are more satisfied with their jobs when they have a voice in decision-making. Kruse et al. (2010) find that the positive relationship between employee ownership and job satisfaction to be the result of the positive effects of employee ownership on “training, freedom from supervision, rating of benefits, and job security.”[49] Empirical evidence on employee ownership, particularly when paired with decision-making participation as is present in cooperatives, thus not only provides significant support to the idea that employee-owned firms offer economic benefits in

---

[46] Ben Craig and John Pencavel. "The Objectives of Worker Cooperatives."*Journal of Comparative Economics* 17, no. 2 (1993)
[47] Blair, Kruse, Blasi (2000)
[48] Artz and Kim (2011) pg. 21
[49] Kruse, Freeman, and Blasi (2010) pg. 274

terms of productivity, survival, and longevity, but they achieve these benefits while furthering worker welfare.

It is important to emphasize that cooperative firm organization need not be limited to small firms. The Mondragon Cooperative Corporation located in the Basque Country of northern Spain defies all of the criticisms of cooperative organizations on a massive scale. Founded in the mid-1950s, Mondragon cooperative firms "employed more than 83,000 full-time workers, and 15-20,000 part-time workers" as of 2011.[50] The cooperative organization grew from a single producer cooperative into a network of 120 cooperative companies as well as being a part-owner of 75 subsidiaries in other countries. And, in 2012, the organization had revenues over $16 billion and maintained assets of $64 billion.[51] Remarkably, Mondragon has accomplished all of this while maintaining an average ratio of 4.5/1 between its highest and lowest wages. Mondragon stands as an exceptionally efficient and globally competitive cooperative success story. Its success highlights the reality that worker-owned firm organization it not antithetical to firm productivity, growth, and stability.

In light of empirical evidence of worker cooperative successes, some researchers have attempted to explain worker cooperative scarcity in terms other than inefficiency. Podivinsky and Stewart (2012) assessed panel data on UK manufacturing in an endeavor to determine the reason for the relative rarity of labor-managed firms as compared to capitalist firms. They found that the evidence "suggests that labour-managed firms (LMFs) are relatively rare in market economies not because they are unable to survive as long as their capitalist firm (CF) counterparts, but because they are created much less

[50] Charles Sackrey, Geoffrey Eugene. Schneider, and Janet T. Knoedler.*Introduction to Political Economy*. 6th ed. Cambridge, MA: Dollars and Sense, Economic Affairs Bureau, 2010. pg. 265
[51] *Ibid*.

frequently."[52] They determined that for a 0.1 unit increase in their measure of risk, there is a corresponding 15% decrease in the likelihood of cooperative formation while there is only a 2% decrease for conventional firms. And, a .01 increase in their capital intensity measure produced an expected 26.7% decrease in cooperative formation but only a 9.4% decrease for capitalist firms.[53] Perceptions of cooperative riskiness make finding financing extremely difficult, which in turn, keeps cooperatives out of the market. Furthermore, "traditional cooperative statutes [in the US] prohibit non-member investment in cooperatives and limit the amount of return on equity," which means that if loans cannot be attained and potential employee-owners do not have independent ability to finance the cooperative, other options for financing are limited. Dickstein (1991) argues that the difference in prevalence of cooperatives in Europe and the US is attributable to the more extensive institutional structure supportive of cooperative development in Europe.[54]

In light of the existing research on the impact of employee ownership and on worker cooperative scarcity, I argue that worker cooperative scarcity exists not because worker cooperatives are inefficient or short-lived, but rather because of a combination of institutional factors. Public policy in the US neglects the worker cooperative organizational form and no strong non-governmental source provides a support system for worker cooperatives. Furthermore, the organizational form is at odds with hierarchical norms that permeate the US.

---

[52] Jan M. Podivinsky, and Geoff Stuart. "On the Choice Between Capitalist and Labour-Managed Production: Evidence from a Panel of Entrant into UK Manufacturing Industries." In *Advances in the Economic Analysis of Participatory and Labor-managed Firms*, edited by Jed DeVaro. Bingley: Emerald, 2012 pg. 77
[53] *Ibid*.
[54] Artz and Kim (2011)

Methodology:

Because my approach to explaining both credit union and worker cooperative scarcity is fundamentally institutional—as opposed to competitive—I use the theory of institutional isomorphism developed by DiMaggio and Powell in "The Iron Cage Revisited: Institutional Isomorphism and Collective Rationality in Organizational Fields" as a framework for understanding cooperative scarcity in the United States. I narrowly focus on explaining the relative scarcity of credit unions—a specific form of consumer cooperatives—as compared to for-profit commercial banks and on the virtual absence of worker cooperatives from the American economy through the lens of DiMaggio and Powell's three mechanisms of institutional isomorphism. The three institutional forces the authors identify are coercive isomorphism, mimetic isomorphism, and normative isomorphism, which I will discuss in turn.

Coercive isomorphism is explained by DiMaggio and Powell as the product of "both formal and informal pressures exerted on organizations by other organizations upon which they are dependent and by cultural expectations in the society within which organizations function."[55] Those pressures might be forceful, persuasive, or strongly incentivizing. In particular, the two note that "in some circumstances organizational change is a direct response to government mandate" and that "the existence of a common legal environment affects many aspects of an organization's behavior and structure."[56] Indeed, the government is one of the most, if not the most, important organization other organizations are dependent on because they define the rules of the game. The importance of government mandate and legal environment is the component of coercive

[55] Paul J Dimaggio., and Walter W. Powell. "The Iron Cage Revisited: Institutional Isomorphism and Collective Rationality in Organizational Fields." *American Sociological Review* 48, no. 2 (1983) pg. 150
[56] *Ibid.*

forces of isomorphism upon which I will most heavily rely in my explanation of credit union scarcity and will also apply to worker cooperative scarcity.

Mimetic isomorphism, DiMaggio and Powell argue, results from standard responses to uncertainty. They assert that "uncertainty…is a powerful force that encourages imitation. When organizational technologies are poorly understood…when goals are ambiguous, or when the environment creates symbolic uncertainty, organizations may model themselves on other organizations."[57] A modeled organization—the organization being imitated—"serves as a convenient source of practices that the borrowing organization may use" often without any intention to do so.[58] Indeed, "models may be diffused unintentionally, indirectly through employee transfer of turnover, or explicitly by organizations such as consulting firms or industry trade associations."[59] Particularly successful firms operate as models often because "organizations tend to model themselves after similar organizations in their field that they perceive as to be more legitimate or successful."[60] Importantly, the authors note that "the ubiquity of certain kinds of structural arrangements can more likely be credited to the universality of mimetic processes than to any concrete evidence that the adopted models enhance efficiency."[61] I find this conception of mimetic forces very useful in explaining the scarcity of worker cooperatives in America in light of the shortcoming of economic efficiency arguments.

Finally, normative isomorphism, "stems primarily from professionalization" which DiMaggio and Powell define as "the collective struggle of members of an

[57] *Ibid.* pg. 151
[58] *Ibid.*
[59] *Ibid.*
[60] *Ibid.*
[61] *Ibid.*

occupation to define the conditions and methods of their work, to control 'the production of producers'…and to establish a cognitive base and legitimation for their occupational autonomy."[62] They note that the struggle for self-directed professionalization is impeded by the need for professionals to "compromise with nonprofessional clients, bosses, or regulators."[63] More important for the purposes of assessing cooperative scarcity in the US, they observe that major growth among professions has been "among organizational professionals, particularly managers and specialized staff of large organizations" which produces greater conformity among this group of firm organizers.[64] Indeed, "while various kinds of professionals within an organization may differ from one another, they exhibit much similarity to their profession counterparts in other organizations."[65] DiMaggio and Powell outline two aspects of professionalization as important sources of isomorphism: "one is the resting of formal education and of legitimation in a cognitive base produced by university specialists; the second is the growth and elaboration of professional networks that span organizations and across which new models diffuse rapidly."[66] Normative forces, like mimetic forces, will primarily be used to explain worker cooperative scarcity.

DiMaggio and Powell readily accept, as do I, that institutional mechanisms are not solely responsible for organizational isomorphism, and thus exclusion, but operate in conjunction with competitive sources of isomorphism. They concede that competitive isomorphism, driven by "market competition, niche change, and fitness measures," plays a role in organizational isomorphism, but contend that "such a view…is most relevant for

[62] DiMaggio and Powell (1983) pg. 152
[63] *Ibid.*
[64] *Ibid.*
[65] *Ibid.*
[66] *Ibid.*

those fields in which free and open competition exists."[67] Importantly, they introduce their institutional mechanisms of isomorphism because while competition offers some explanatory value, it "does not present a fully adequate picture of the modern world of organizations."[68] Supplementing an assessment of competitive isomorphism with an assessment of institutional isomorphism allows us to acknowledge and account for the reality that organizations "compete not just for resources and customers, but for political power and institutional legitimacy, for social as well economic fitness;" it allows us to account for ways in which organizational structure is induced—even coerced—that are not explicitly economic.[69] And, this is precisely what I endeavor to do in applying DiMaggio and Powell's theory throughout this work; I do not intend to argue that competitive forces are unimportant, but merely that they are not all-important.

As a final note on methodology, I find it pertinent to make clear that the institutional forces discussed above do not all apply equally, or necessarily all apply, across sectors. Thus, I find that coercive forces of isomorphism are largely responsible for credit union scarcity, and discuss said scarcity exclusively in those terms, while I find that all three mechanisms of isomorphism impact worker cooperative scarcity and discuss worker cooperative scarcity in terms of all three.

Chapter Summaries

The body of this work is broken into three chapters that explore the institutional reasons for credit union and worker cooperative scarcity in the United States through the lens of DiMaggio and Powell's three mechanisms of institutional isomorphism. The first chapter is devoted to explaining the scarcity of credit unions in the United States. I argue

---

[67] *Ibid*. pg. 150
[68] *Ibid.*
[69] *Ibid.*

in the chapter that, despite superior performance by several metrics, credit unions occupy the small corner of the financial sector they do primarily due to mechanisms of coercive isomorphism. Government regulation unique to credit unions limits their ability to grow, take advantage of returns to scale, and provide better and more extensive services to customers. This limitation simultaneously limits credit unions, on the demand side, from providing as convenient of service as commercial banks and, thus, decreases demand for credit unions.

My second chapter focuses on the role of mechanisms of coercive isomorphism in contributing to worker cooperative scarcity in the US. I argue that public policy in the US is at least somewhat responsible for worker cooperative scarcity. Employee Stock Ownership Plans (ESOPs) dominate the field of employee ownership because, as a government defined and endorsed form for employee ownership, they are better understood than worker cooperatives and because they are tax-favored to provide firms with incentives for adopting them. Thus, although worker cooperatives combine ownership and employee participation to more reliably realize employee and firm benefits, firms interested in employee ownership are likely to turn to ESOPs instead. I contrast this impact of public policy with that of other countries that maintain similar policy, but for worker cooperatives.

Finally, my third chapter is devoted to exploring the forces of mimetic and normative isomorphism in contributing to worker cooperative scarcity. I argue that in the US, worker cooperative scarcity begets worker cooperative scarcity. Standard responses to uncertainty both encourage new entrants to the market to mimic the organizational form of successful model organizations and create tangible costs for non-conforming firms, thus discouraging such non-conformity. Furthermore, prevailing norms—both business professional and more general societal—promote hierarchical organization and condition Americans to accept hierarchical workplaces as normal.

The scarcity of credit unions and worker cooperatives in the United States poses a puzzle. Traditional explanations of their scarcity which rely on neo-classical models that emphasize competition and profit-maximization do not adequately explain the cooperative landscape in the country. It is my hope that his project will shed light on the importance of institutional forces in providing supplemental explanatory value.

Chapter 1:

Credit Union Scarcity: Coercive Isomorphism

In 2010, the New York Times ran a piece entitled “Credit Unions Begin to Promote Their Strengths”. As the title suggests, credit union strengths are nothing new, but they have long gone unadvertised and underappreciated. In the wake of widespread dissatisfaction and anger at big banks after the financial crisis and in response to sky-high interest rates and exorbitant over-draft fees, however, some credit unions began to step forward and promote their advantages over for-profit banks. America’s First Federal Credit Union in Birmingham, Alabama, was one such bank. They launched a series of commercials in which “bankers” confess to charging a lot of unnecessary fees simply to boost their pay-checks.[70] In contrast, the credit union positions itself as a preferable and profitable alternative. The point that the commercials articulate is that there are more consumer-friendly products available in the banking market—products with lower interest rates for borrowing and higher rates of return for savings. But surely it is not simply a lack of marketing that explains the scarcity of credit union membership. Given their superior performance, it is striking that credit unions command as little of the market as they do and begs the question of why credit union use is really so scarce, relative to commercial bank use.

I argue that credit unions scarcity is somewhat attributable to characteristic endogenous to credit union norms, but that it is primarily the consequence of mechanisms of coercive isomorphism active in government policy. Credit unions are subject to unique regulatory burdens that limit their size and scope, ultimately leading to them being

[70] Martin, Andrew, and Ron Lieber. "Alternative to Banks, Now Playing Offense." The New York Times. June 11, 2010. http://www.nytimes.com/2010/06/12/business/12credit.html?pagewanted=all.

comparatively less convenient than commercial banks. Effectively, there are both supply and demand side reasons for scarcity resulting from forces of coercive isomorphism that privilege commercial banks; public policy limits the ability of credit unions to supply banking services, which in turn decreases demand for credit unions. The chapter proceeds in the following manner: I first provide a brief history of credit unions and their structure; next I illustrate the superior performance of credit unions relative to commercial banks in the US; I then articulate the endogenous and coercive institutional reasons for scarcity and substantiate my claims with empirical evidence.

Brief History of Credit Unions and Their Structure

Credit unions are unique from commercial banks in important ways, including in their historical purpose, organizational form, and regulatory burdens. These differences are central to explaining why credit unions are so scarce relative to their commercial counterparts and thus justify a brief exploration of the history of credit unions in America and their distinguishing characteristics.

The earliest credit union in America dates to 1909 in New Hampshire. In the same year, Massachusetts passed the Massachusetts Credit Union Act.[71] The impetus for credit union formation came in response to a lack of affordable credit for working-class families who typically were forced to turn to loan sharks charging exorbitant interest rates. The popularity of the institutions spread and credit union proliferation following these initial start-ups was remarkable. In 1934, after a number of states had already passed state-level credit union acts, President Franklin D. Roosevelt signed the Federal Credit Union Act

[71] "Credit Union History" NCUA. http://www.ncua.gov/about/history/Pages/CUHistory.aspx, Accessed January 21, 2013

into law, creating a national system to charter and supervise federal credit unions.[72] Since that time, credit unions in the United States have offered banking services to members at rates typically advantageous to those offered by for-profit competitors. Critically, credit unions increased their reach over time as the requirements for membership eligibility have changed to become more inclusive; while credit unions initially required membership in somewhat narrowly defined group, they now often require only that an individual live in the township or county served by a credit union. Thus, although individuals are not eligible to join any credit union due to the "common bond" requirement—which will be discussed in detail later—most people are eligible to join at least one credit union.

Given the cooperative structure of credit unions, the goals of credit unions differ significantly from those of for-profit banks. As consumer banking cooperatives, credit unions are owned and controlled by the individuals who use the institutions' services. In US credit unions, "consumer deposits or 'shares' fund the organization" and "each member is accorded one vote on credit union matters and decisions regardless of the size of the members' accounts."[73] Loans to members are made from member deposits. The result of this type of member ownership is that the goals of the owners are, inevitably, the very same as the goals of the consumers—the depositors and borrowers. In contrast, commercial banks are organized as investor-owned corporations in which "determination of deposit-taking and lending practices is made by outside owners whose objective is maximization of ownership (equity) value."[74] Thus, while profits at commercial banks

---

[72] *Ibid.*
[73] Randell Pozdena, and Michael Wilkerson. *Credit Unions vs. Banks: The Myth of the Uneven Playing Field*. Issue brief. Portland: ECONORTHWEST, 2013. pg. 7
[74] *Ibid.*

are distributed to owners, gains at credit unions are employed to maximize member benefit by providing the best rates possible. Any income net expenses is used to capitalize the institution to protect against loan losses and distributed to members as dividends.

Superior Credit Union Performance

The theoretical purpose of credit unions is well-established to be to offer better rates and service to its members, and based on organizational theory it makes sense that they would indeed be capable of doing so. But, in practice, just how well do credit unions in the US measure up to their for-profit, investor-owned banking counterparts? For 21 years in a row, until 2005, the American Banker newspaper performed a consumer satisfaction survey of banks, thrifts, and credit unions in which credit unions came in first every single year.[75] And, Allred and Addams (2000), in a survey targeting credit union and bank customers, found that "in all areas of service quality, credit union customers rate credit union service quality higher than bank customers rate bank service quality."[76] These polls reflect the greater satisfaction of credit union customers relative to bank customers, a superior satisfaction rooted in superior performance in several metrics. Not only do credit unions typically offer better rates for depositors and borrowers, they also demonstrated themselves to be more resilient during the recent financial crisis and to be a more reliable source of credit in the wake of the financial crisis.

Using data compiled by Datatrac, Inc., an independent company that tracks the interest rates and terms at financial institutions nationwide, the National Credit Union

[75] CUNA "Commercial Banks & Credit Unions: Facts, Fallacies and Recent Trends" PPT. Accessed at http://www.cuna.org/Research-And-Strategy/Credit-Union-Data-And-Statistics/

[76] Allred, Anthony T., and H. Lon Addams. "Service Quality at Banks and Credit Unions: What Do Their Customers Say?" *Managing Service Quality* 10, no. 1 (2000) pg. 55

Administration produced charts that compare the national average rates for 23 common loan and deposit products at banks and credit unions (as well as the same rates prevailing at banks that converted from credit unions).[77] The charts reveal that on the vast majority of products, credit unions offer favorable rates relative to their for-profit counterparts. The latest report, from September 2013, is reproduced on the following page and illustrates the difference in product rates. Taken together, they demonstrate that, on average, credit unions overwhelmingly offer better rates for the majority of products. Three financial products—30 year fixed rate mortgage, 15 year fixed rate mortgage, and 5½ year adjustable rate mortgage—are offered at marginally better rates at banks. Importantly, these rates are comparable with the prevailing averages in other quarterly reports and in the annual reports that pre-date the financial crisis and the recession.

In addition to offering favorable rates to members, credit unions demonstrated their relative resiliency during the financial crisis. Between the start of 2008 through the end of 2010, there were 366 bank failures in the United States.[78] During the same 3 year period, credit unions also suffered; 52 credit unions closed. But, measured as a percentage, these 52 credit unions represent a failure rate much less substantial than that of banks, because there are, in fact, a greater number of credit unions in the US than there are banks (not in brick and mortar presence, but in central organization).[79] The primary reason the credit union sector survived the financial crisis much less scathed than banks is that credit unions were much less likely to take part in the risky loans that many for-profit

[77] Comparison data is available in year-end periods for 2003, 2004, and 2005. Comparison data is available in quarterly periods for 2008-2013.

[78] Mark Klinedinst. "Going Forward Financially: Credit Unions as an Alternative to Commercial Banks." In *Advances in the Economic Analysis of Participatory and Labor-managed Firms*, edited by Jed DeVaro, 3-23. Bingley: Emerald, 2012.

[79] *Ibid.*

banks engaged with. This results from the difference in goals between credit unions and commercial banks; while commercial banks sought profits—irresponsibly, as we know retrospectively—most credit unions were simply focused on best serving their membership base and balancing the interests of their savers and borrowers. When it came to issuing bad mortgages, credit unions were less likely to do so because they were not trying to profit maximize but rather produce the best risk-adjusted rates they could for their members.

A final measure of US credit union performance relative to for-profit banks can be found in their propensity to loan. Particularly in the wake of the financial crisis, credit union loaning continued to be a significant source of credit while banks actually substantially restricted their loaning. Between 2007 and 2008, loans granted by credit unions in the United States increased by 6.68 percent in volume.[80] During the same time period, loans granted by traditional banks actually decreased by 0.39 percent.[81] And, in 2009 credit unions continued to increase their loan volume, although by a smaller 1.2 percent.[82] It is important to also note that although the rate of increase declined in 2009, the loans issued by credit unions were more productive than those issued by banks; the growth of productive loans[83] for credit unions reached 11 percent while productive loans from for-profit banks decreased by 15 percent.[84] The implication of this last comparison is important; not only were credit unions generating more loans than banks on the whole,

[80] Bajo and Roelants (2011) pg. 111
[81] *Ibid.*
[82] *Ibid.*
[83] Productive Loans are typically business loans for start-up or overdraft for members in business which are intended to increase the economy's output.
[84] Bajo and Roelants (2011)

they were producing the type of loans important for battling the recession and unemployment while banks were substantially deceasing such loans.

Given this backdrop—preferable rates, greater resilience and stability, and more reliable lending in the wake of the financial crisis and amidst the recession—it would seem reasonable to expect credit union use to be quite common. Reasonable, but wrong. As of 2011, US credit unions served only 93 million members, held 10 percent of savings deposits, made 9 percent of all consumer loans, and made 13.2 percent of nonrevolving consumer loans.[85] Meanwhile the four largest commercial banks in the US—JP Morgan Chase, Bank of America, Citigroup, and Wells Fargo—control combined assets of roughly $7.9 trillion. These same four banks maintain roughly 20,000 branches combined. The credit union presence is dwarfed by just these four, without considering the role of other large and small commercial banks in the US financial market. Indeed, even if credit unions performed only at the same level as for-profit banks, these numbers would be surprising. But, given the superior performance of credit unions, it is all the more striking. I now turn to explanation of the organizationally endogenous and coercive institutional reasons for credit scarcity.

Endogenous Sources of Scarcity

A partial explanation for the relatively small number credit union share of the banking market is that credit unions fail to market as aggressively as their competitors. As the New York Times article suggests, credit unions are not known for innovative or compelling advertising. Indeed, credit unions typically market themselves using conservative, often dated approaches such as paper pamphlets promoting rates in a rather

[85] Wheelock, David C., and Paul W. Wilson. "Are Credit Unions Too Small?"*Review of Economics and Statistics* 93, no. 4 (2011)

bland manner. So, while credit unions rely on their competitive rates selling themselves many commercial banks engage in aggressive and innovative advertising, seeking new and more effective ways to tap clients.

Largely, this difference may be attributed to institutional form. While banks are for-profit institutions primarily seeking to maximize profits for their investor-owners, credit unions are non-profit organizations with the primary goal of creating consumer loans and other financial products at a price best for members. As one credit union expert explains, “it’s more than profit versus nonprofit. It’s about philosophy and purpose. Banks are about profit which satisfies owners, directors, and/or shareholders. Credit unions are about providing low-cost services to its owner-members in a nonprofit environment.”[86] As such, credit unions are less aggressive in expanding their membership base, because their primary goal is to serve the current membership, not increase profits or membership. As Fountain (2007) observes, “since credit unions are not-for-profit institutions, the motivation for strategic and financial growth differs from for-profit businesses; however, credit unions must make some profit in order to provide for additional services which meets or exceeds those of competitors.”[87] Thus, while credit unions need to ensure that they are economically viable in the future, there is less impetus to increase membership and net profits as long as the credit union is achieving sufficient gains to pass along preferable rates to members.

A Rand survey conducted in 2009 provides some support for this view. The survey finds a lack of consumer knowledge about what credit unions do and who is eligible to become a member, which may be the consequence of poor or limited

[86] Wendell V. Fountain *The Credit Union World: Theory, Process, Practice--: Cases & Application*. Bloomington, IN: AuthorHouse, 2007. Kindle. Kindle Locations 1663-1665
[87] *Ibid*. Kindle Locations 653-655

institutional promotion. Of bank users who responded that they would not consider switching to a credit union if they had to switch institutions, the most oft cited reason was “a lack of knowledge about the services provided by credit union” while the second most often cited reason was convenience. Moreover, bank users were notably more likely than credit union users to believe that “credit union members must belong to a labor union, credit unions lack data security, and credit unions offer limited services.”[88]

Interestingly, though, a lack of knowledge about what credit unions are capable of and who is an eligible member do not seem to be the primary barrier to credit union membership—convenience, or inconvenience, does. The Rand survey cited above finds that “consumer selection of financial service providers is based primarily on convenience of branches, convenience of ATMs, and bank fees.”[89] The survey found that bank users tend to be more focused on convenience issues while credit union users are more interested in fees, which is telling about the limitations on convenience placed on credit union by regulatory burdens.

In practice, most former bank users who switched to a credit union cited “fees, free checking, and better service as primary reasons for the switch,” reinforcing the fact that service performance at credit unions tends to be better than at banks.[90] And, similarly, of credit union users who actually switched to a bank, those who did so for a reason other than a move—which were the majority—cited convenience as the primary reason for their decision. These consumer responses suggest that the biggest barrier to credit union membership is not a lack of awareness or a lack of desirability, but rather a

---

[88] Jinkook Lee et al., “Consumer Use of Banks and Credit Unions,” Product Page, 2009, http://www.rand.org/pubs/technical_reports/TR672.html. pg. ix
[89] *Ibid*. pg. viii
[90] *Ibid*.

matter of access and convenience. The common bond and other regulatory burdens on credit unions restrict their reach, and thus their ability to grow to support multi-branch convenience for members. Therefore, I proceed to argue that forces of coercive isomorphism in credit union and banking regulation are largely to blame for credit union scarcity.

Coercive Isomorphism: The Common Bond and Financial Services Regulation

A defining characteristic of credit unions is the concept of the "common bond". Credit unions "cannot do business with the general public due to charter limitations based on serving a membership that is characterized by a common bond…based on occupation, association [such as a fraternal or religious organization], or residence."[91] The residence requirement is more narrowly defined as "a well-defined neighborhood, community, or rural district."[92] The origin of the common bond finds its place in the assumption that a banking institution in which close ties between members is required will offer solutions to information asymmetries in lending. The common bond requirement "was seen as the cement that united credit union members in a cooperative venture, and was, therefore, thought important to credit unions' continued success."[93] And, the common bond was historically—and still is today, to some extent—considered "advantageous because it can reduce the cost of assessing the creditworthiness of potential borrowers and thereby facilitate unsecured lending on reasonable terms to the credit union's members."[94]

---

[91] Black, Harold, and Robert H. Dugger. "Credit Union Structure, Growth and Regulatory Problems." *The Journal of Finance* 36, no. 2 (1981) pg. 529
[92] William R. Emmons and Frank A. Schmid, "Credit Unions and the Common Bond," Federal Reserve Bank of St. Louis *Review* 1999 pg. 41 (quoting from the Federal Credit Union Act of 1934)
[93] *Ibid*. pg. 44 (quoting from Supreme Court, 1998, pp. 17-18, citing 988 F.2d, at 1276.)
[94] Wheelock and Wilson (2011) pg. 1343

Since the federal legislation of credit unions in 1934, the domain of the common bond has developed quite dramatically. In the early years of credit unions, interpretation of the common bond was rather restrictive. Indeed, most credit unions formed as single occupational unions. However, in the 1970s there began a "less restrictive interpretation of the common bond requirement for membership, which created new opportunities for growth and merger."[95] Perhaps most notably, in 1982 the National Credit Union Administration (NCUA) "ruled that a single credit union could serve employees of multiple employers even when not all employers were engaged in the same industrial activity."[96] The dilution of the common bond requirement in this way offered credit unions the opportunity to enlarge their membership base and size. The American Bankers Association (ABA), understanding the market threat posed by expanding credit union base, filed suit, challenging the permissibility of the multiple common bond under the 1934 legislation. And, in 1998 the Supreme Court found in favor of the ABA, concluding that the practice of allowing multiple common bonds in one credit union was not permitted by the 1934 Act.[97] In quick response to the Court's decision, Congress passed, and President Clinton signed, the Credit Union Membership Act, "which authorized individual credit unions to serve multiple groups, within some restrictions."[98]

This was a big victory for credit unions. As one credit union expert explains: "1998 was the watershed year at the federal level in legislation regarding credit unions. President Bill Clinton signed the Credit Union Membership Access Act into law on August 7, 1998, despite the efforts of the powerful banking and lobbying interests which

---

[95] John A Goddard, Donal G. Mckillop, and John O.s Wilson. "The Growth of US Credit Unions." *Journal of Banking & Finance* 26, no. 12 (2002) pg. 2328
[96] Wheelock and Wilson (2011) pg. 1344
[97] *Ibid.*
[98] *Ibid.*

had lined up fiercely against the credit union movement-industry."[99] Importantly, though, while the 1998 Act loosens the common bond, it certainly does not eliminate it; as long as the common bond persists, it imposes restrictions on credit union size and, thus, the number of people credit unions can serve and the types of services they can offer.

As technology advances enable credit-reporting agencies to provide reliable creditworthiness information, the dilution of the original common bond requirements are perhaps not very dangerous. Indeed, "because of the low cost and ease with which lenders can gather consumer creditworthiness information, and the repayment incentive their presence provides, the relative advantages of creditworthiness knowledge gained by maintaining direct contact with the borrower through a common bond and the motivation to repay produced by common bond relationships are reduced." Thus, while the common bond restriction on membership once served a very legitimate purpose in the credit union structure, it now seems to act as a limiting factor on credit unions' ability to grow and offer services to a broader consumer base. Walter (2006) observes that the 1934 Act, with its restrictive common bond requirements, "essentially predicted that such a huge credit union would not have been a safe and sound financial institution, nor consequently a viable one in the long run" and expresses his skepticism that this remains true.[100]

In addition to the common bond restriction on credit unions, other regulatory burdens have historically limited credit unions' ability to broadly meet consumer wants. In particular, regulation regarding what types of financial services credit unions are permitted to offer has historically limited credit union market share, and continues to do so. In their early iterations, credit unions offered, almost exclusively, small-value,

---

[99] Fountain (2007) Kindle Location 595
[100] Emmons and Schmid (1999) pg. 47

unsecured consumer lending while other financial institutions offered large-scale loans. Prior to amendments to the Federal Credit Union Act in 1977, "federal credit unions were limited to providing short-term mortgage loans such as second mortgages and mobile home loans."[101] While most credit unions now offer long-term home loans, this is the direct result of easing of regulation on the matter. Importantly, such easing has not taken place for all financial products credit unions want to offer. In particular, credit unions are not a substantial source of business loans. Although credit unions have expanded their service and product offering greatly over time, the 1998 Credit Union Membership Access Act actively limits the ability of credit unions to lend to businesses at 12.25 percent of the credit union's total assets.[102] Undoubtedly this cap limits the clientele who turn to banks for business loans and, in this manner, restricts credit union assets.

The maintenance of the common bond and other restrictions on credit unions has not been the result passive negligence, but largely the result of banking industry lobbying done by the American Bankers Association. The ABA did not only come into play during the relaxation of the common bond in the 1990s. The ABA actively seeks to keep the functional abilities of credit unions limited, arguing that if the common bond is dismissed or credit unions offer more diverse financial products that credit unions are no longer acting like credit unions and cannot be regulated as such, thus intrinsically linking credit union continuation with common bond and other regulation.[103] The ABA is a very powerful lobby with extensive resources and it appears that their work to limit credit union de-regulation is quite successful, despite the reality that the most distinguishing

[101] John Walter, *Not Your Father's Credit Union*, SSRN Scholarly Paper (Rochester, NY: Social Science Research Network, 2006), http://papers.ssrn.com/abstract=2186135. pg. 371
[102] *Ibid.* pg. 372
[103] Michael McKelly. *The Secret War on America's Credit Unions*. 2012.

characteristics of credit unions have not to do with the common bond and the specific financial services they provide, but with the ownership scheme, democratic operation, and prioritization of member service over profit maximization.

Empirical Evidence of Common Bond and Regulatory Impact

There is substantial evidence that common bond restrictions have a meaningful impact on the performance of credit unions. In the wake of the relaxation of the common bond in 1982—and more decidedly in 1998—credit union growth witnessed a marked increase. Adjusted for inflation, "the average credit union held 6.5 times more assets in 2006 than the average credit union in 1985."[104] A great deal of this increase in size is attributed to the Credit Union Membership Act of 1998 for facilitating consolidation of credit unions. Support for this position is found in the fact that during the period of growth in size of credit unions, there occurred a simultaneous sharp decline in the number of credit unions and marked increase in the number of credit unions characterized by multiple common bonds.[105]

This should not be surprising. There is strong precedent in the experience of commercial banks in the 1990s for expecting de-regulation to encourage financial institutes to take advantage of economies of scales. Changes in banking regulation allowed commercial banks to grow into the national mega-banks we know today. Colomiris and Haber (2014) explain that the Riegle-Neal Interstate Banking and Branching Efficiency Act of 1994 knocked down the last barriers to interstate banking and allowed banks to combine into national banking systems.[106] This legislation allowed

[104] Wheelock and Wilson (2011) pg. 1344
[105] *Ibid.*
[106] Charles W Calomiris and Stephen H. Haber. *Fragile by Design: The Political Origins of Banking Crises and Scarce Credit*. Princeton: Princeton University Press, 2014. Note that while I merely articulate this in

for, even encouraged, the creation of JP Morgan Chase, Bank of America, and the other mega-banks in America while credit unions remain limited in their reach.

There are several explanations offered by economists for the tendency in credit union growth. A number of studies have found an inverse relationship between average operating expenses and credit union size.[107] Importantly, it appears that cost advantages of larger credit unions have grown with time, which suggests an increasing incentive towards consolidation and growth of credit unions into larger institutions, when possible.[108] Additionally, there is evidence that "larger credit unions have more opportunities for diversification into nontraditional product lines, such as business loans, credit cards, and mutual funds and that doing so has reduced the volatility of their earnings while providing their members with additional services."[109] Wheelock and Wilson (2011) find "substantial evidence of increasing returns to scale among credit unions of all sizes, suggesting that further consolidation and growth among credit unions are likely," but are careful to point out that further relaxation of legal restrictions on credit union membership and permissible activities will play a large role in the extent of this growth.[110]

This conclusion is supported by Goddard et al. (2002) who found that "the ratio of actual to potential membership available to the credit union given the coverage of its common bond is also an important determinant of growth…credit unions close to

contrast with the regulatory position of credit unions, the authors argue that this was a potentially positive change that might have allowed for a stable banking system that could offset losses in some regions with gains in others. I would like to suggest that credit unions could benefit equally from the ability to build such a national system, and would likely do so in a more responsible way than the commercial banks that failed in 2007 did.

[107] Wheelock and Wilson (2011). Also see Emmons and Schmid (1999)

[108] James A. Wilcox, "Performance Divergence of Large and Small Credit Unions," *FRBSF Economic Letter*, 2006, http://ideas.repec.org/a/fip/fedfel/y2006iaug4n2006-19.html.

[109] Wheelock and Wilson (2011) pg. 1344

[110] *Ibid.*

exhausting their potential membership face difficultly sustaining strong growth performance."[111] Goddard et al. conclude that "common bond coverage does appear to impose a significant constraint on credit union growth."[112] If credit unions are restricted by the common bond requirement from achieving the same type of economies of scale as their commercial bank competitors, it is unsurprising that they operate on a small and, thus, less convenient scale than those competitors.

Non-common bond regulations discussed in the previous section also demonstrates tangible limitation of credit unions. Restrictions on what financial products credit unions can offer limit their customer base. Above, the "permissible activities" referenced by Goddard et al. primarily pertains to the proposal to increase credit unions' abilities to lend up to 27.5 percent of their total assets rather than the current 12.25 percent. Indeed, Senator Mark Udall of Colorado has introduced legislation to do just that on several occasions with the intent of freeing up credit union lending. Proponents of the change argue that the current cap limits small business' access to necessary credit; they claim that passage of the bill would "free up credit unions to make up to $13 billion in new loans to small businesses in just the first year."[113] As of yet, although the bill has been introduced in the House as well, it has yet to garner the level of support necessary to become law and is heavily opposed by the ABA, as they view business lending as outside the proper functions of a credit union (despite the fact that credit unions have historically played an important role in small business finance.

[111] Goddard et al. (2002) pg. 2349
[112] *Ibid.*
[113] http://www.cuna.org/webassets/pages/newsnowarticle.aspx?id=68930

Conclusion

The influence of coercive isomorphism in privileging banks over cooperative alternatives is not new in American history, although it has not always been intentional. Due to extreme bank instability in the first half of the 19th century—largely due to information asymmetries leading to bad lending decisions—cooperatively owned mutual savings banks were more popular choices; by 1880 mutual savings banks held close to 90 percent of saving while commercial banks only held about 10 percent.[114] A remarkable shift took place in the last decade of the century, however, when "bank regulation was introduced to contain commercial bank risk-taking, and derivatively, to reduce depositor paranoia about risks to their deposits."[115] By 1925, this shift allowed investor-owned banks to increase market share to roughly half and in 1934 the Banking Act of 1933 granted commercial banks deposit insurance, making them preferable to cooperative banking options without such protection.[116] This regulation paired with the restrictiveness of the common bond until the 1970s undoubtedly played a role in the evolving composition of the financial market in the country. And, it is hard to make up lost ground, particularly in the face continual disadvantage.

Credit unions in the United States differ in very significant ways from the commercial banks that dominate the financial sector. While recent history has demonstrated the reckless ends for-profit banks will go to in attempts to profit maximize, it simultaneously demonstrated how effectively credit unions avoid such behavior by sticking to their mission of providing the best service possible to their member-owners. But, despite superior performance, credit unions are relatively scarce when compared

[114] Pozdena and Wilkerson (2013)
[115] *Ibid.* pg. 8
[116] *Ibid.*

with commercial banks and many fewer Americans use credit union services than commercial banking services. While some part of credit union scarcity is the result of characteristics endogenous to credit unions, it is more attributable to the consequences of public policy. Mechanisms of coercive isomorphism in the form of public policy function to both limit the size and scope of credit union operation while advantaging that of commercial banks; regulatory burdens unique to credit unions prevent them from taking advantage of economies of scale as well as commercial banks, often limiting their ability to offer the type of convenience commercial banks do, and disallow them from participating in potential markets.

In the wake of the financial crisis and commercial bank irresponsibility and failure, credit unions have gained prominence and popularity. They represent a favorable alternative in terms of rates, stability, and financial responsibility in the absence of heavy regulation and oversight (as a result of their nature and goals). But, without further relaxation of the common bond and increasing ability to offer greater financial services, credit unions will be forced to continue to be small, relatively inconvenient, and less full-service alternatives to commercial banks. In short, without a change in the mechanisms of coercive isomorphism, credit unions will likely continue to occupy only a small portion of the financial market in the United States.

Chapter 2:

Worker Cooperative Scarcity Part I: Coercive Isomorphism

An interesting paradox exists in the United States: while worker cooperatives are remarkably scarce, employee ownership is not. In the United States, before the mid-1970s, employee ownership was a rare event. A highly limited number of worker cooperatives existed as isolated incidences of such ownership arrangements. Since that time, a great transformation in the landscape of ownership took place. Today, more than one in 6 private sector employees in the US own shares in their company and more than one in 12 maintain their ownership in the form of participation in an Employee Stock Ownership Plan (ESOP). A remarkable 10 million employees participate in more than 9,000 ESOPs with the net value of employee holdings in excess of $600 billion.[117] The dramatic growth of employee ownership in the US, notably, is concentrated in the form of ESOPs, not in other organizational forms of employee ownership such as worker cooperatives. This pattern in the organization of employee ownership begs the question of why, despite clearly gaining popularity, employee ownership has so narrowly taken the form of ESOPs.

I argue that the answer to this query can be located within DiMaggio and Powell's theory of organizational isomorphism. Coercive forces of isomorphism in the form of government policy favor ESOPs over cooperative ownership. The spike in employee ownership began after the introduction of ESOPs in the Employee Retirement Income Security Act of 1974 (ERISA). Despite rewards of employee ownership being contingent on more than simple financial interest in a firm, employee ownership persists in taking

---

[117] Steven F Freeman,. *Effects of ESOP Adoption and Employee Ownership: Thirty Years of Research and Experience*. Working paper no. 07-01. University of Pennsylvania, 2007.

the form of ESOPs rather than worker cooperatives because ESOPs are institutionally privileged in ways which cooperatives are not. The chapter proceeds in the following manner: I first outline what Employee Stock Ownership Plans are and where they originated; I then take a close look at ESOP performance and compare their performance with that of worker cooperatives; next I explain the tax policy form of the coercive forces of isomorphism encouraging ESOPs; and, lastly, I compare US forces privileging ESOPs to similar forces in other countries that apply to cooperatives.

Defining Employee Stock Ownership Plans

Employee Stock Ownership Plans (ESOPs) are, most fundamentally, a form of pension plan for the employees of an enterprise. While ESOPs operate as a retirement fund in much the same way as other defined contribution pension plans articulated in the Employee Retirement Income Security Act (ERISA)—i.e. 401(k)s—do they also differ in several noteworthy ways. Generally speaking, defined contribution plans are characterized by individual employee accounts, which are funded by employee contributions, employer contributions, or some combination of the two. The contributions to these accounts are typically invested on the employee's behalf and upon cashing in on their personal account an employee will receive the balance of their account, which is based on contributions plus or minus investment gains or losses.[118]

One of the fundamental differences between ESOPS and other defined contribution pension plans is that ESOPS "invest primarily in the sponsoring corporation's equity securities, whereas other pension funds cannot hold more than 10%

[118] "Retirement Plans, Benefits & Savings." U.S. Department of Labor. Accessed April 5, 2014. http://www.dol.gov/dol/topic/retirement/typesofplans.htm.

of their assets in the sponsoring firm's securities."[119] A second important difference is that ESOPs can borrow funds for the purchase of the stock for the plan while other pension plans are prohibited from doing so under ERISA.[120] The latter, known as leveraged ESOPs, make up a substantial number of the ESOPs created since their introduction in ERISA. Leveraged ESOPs are popular because they can effectively be used for company financing; an ESOP trust is formed which can then borrow money from a lending institution for the purpose of acquiring the sponsoring firm's stock, which effectively amounts to a loan to the firm.[121]

An additional peculiarity of ESOPs is the particular nature employee ownership is required to take. During their employment, while employees have shares in the company, those shares do not come with control rights. The ESOP is held in trust and the controlled by an appointed trustee. Therefore, even if an ESOP constitutes majority employee ownership (which is atypical to begin with) the employees do not exercise majority control under ESOP provisions.

The Origin of ESOP Policy

The historical development of the ESOP is quite pertinent to our understanding of employee ownership. The concept of the ESOP originated with Louis Kelso, a securities lawyer with a prominent San Francisco law firm, and was brought to legislative fruition though Kelso's partnership with Senator Russell Long, the chairman of the Senate Finance Committee from 1966 to 1981.[122] Kelso authored an extensive body of economic

---

[119] Susan Chaplinsky and Greg Niehaus. "The Tax and Distributional Effects of Leveraged ESOPs." *Financial Management* 19, no. 1 (1990) pg. 30
[120] *Ibid.*
[121] Ibid.
[122] Michael E. Murphy. "The ESOP at Thirty: A Democratic Perspective." *Willamette Law Review*, 2005, 655-706.

theory that he considered a challenge to conventional economics of the time[123] —around the 1950s—and "the key to the survival of capitalism."[124] He identified two primary problems with the prevailing form of capitalism: the increasing concentration of capital in the hands of the few and the high level of taxation on productive members of society for distribution to nonproductive members. He attributed these afflictions of capitalism to "traditional capital financing methods that conditioned the acquisition of new capital on the ownership of existing capital, thus creating a 'spiraling concentration' of capital ownership and providing the political incentive for the New Deal welfare legislation."[125] He posited that the solution to these contingent problems was, thus, to restructure the system of capital financing; he envisioned a system in which ordinary workers would have the opportunity to become a capitalist himself, at least to a degree. And, by making the everyday citizen a capitalist, he believed capitalism would be revitalized.

More specifically, Kelso's endeavor to find a program for re-structuring the capital finance system to support new capitalists led him to produce and advocate employee investment plans "backed by the sponsoring employer's credit, which could borrow money to finance investment through the purchase of the employer's stock."[126] As the employer paid off the loan for the purchase of company stock, the employees in whose name the stock was purchased would become the beneficial owners of the stock allocated to their account in the investment plan. In 1957, well before ESOP legislation was enacted, Kelso crafted the first of these plans for Peninsula Newspapers, Inc., and the concept spread slowly.

---

[123] Kelso's argument is first and primarily laid out in *The Capitalist Manifesto*, which he co-authored with Mortimer J. Adler (1958).
[124] Murphy (2005) pg. 656
[125] *Ibid*. pg. 656-657
[126] *Ibid.* pg. 657

In 1973, Kelso became associated with Senator Long, the conservative chairman of the Senate Finance Committee at the time, which sparked the push for ESOP legislation. Meeting for dinner in Washington, Kelso articulated his vision for expanding capital ownership to ordinary workers. Reportedly, Long asked Kelso, "'Are you saying that [these financing methods] can make haves out of have-nots without taking it away from the haves?'" and, upon Kelso responding in the affirmative, stated "'That's the kind of populism I can buy.'"[127] Long's conversion to Kelso's proposal—which reconciled the Senator's populist origins with his capitalist convictions—brought the concept for the ESOP into the political arena at a time that could hardly have been better.

In the early 1970s, Congress was in the midst of dealing with questions regarding the future solvency of Social Security. A comprehensive survey conducted in the 1967 regarding the solvency issue "revealed that one out of 17 Americans were then eligible for Social Security benefits, but that by the year 2000 one out of every three Americans would be eligible and that by the year 2010 it would be one out of two."[128] What was to become ERISA was under consideration by the Senate to address this shortfall in Social Security benefits, and Kelso "argued that the proposed legislation presented a practical opportunity to engraft his financing scheme onto the existing statutory authorization for stock bonus plans."[129] Kelso and Long claimed that "employee ownership builds commitment, which leads to productivity and profits, and argued that legislation facilitating broader-based ownership would not only increase corporate performance, but also ease workplace tensions, reduce disparities of wealth, and help build a better

[127] *Ibid*. pg. 657 citing Rudy Maxa, *Can We All Own a Piece of the Rock?*, Wash. Post, Dec. 10, 1978
[128] Freeman (2007) pg. 3
[129] Murphy (2005) pg. 658

society."[130] Indeed, his argument for the inclusion of ESOPs in the legislation prevailed with the support and sponsorship of Long. The inclusion of the ESOP in the 1974 legislation is far from the end of its history. After its initial introduction in ERISA, "Senator Long secured the passage of some twenty-five bills promoting and elaborating upon this original ESOP legislation."[131]

The success of ESOP legislation, although largely attributable to the collaboration between Kelso and Long, certainly speaks to the rising popularity of employee ownership around the 70s and 80s; it reflects not merely the hard work of a few to enshrine their personal ideology in law, but the general support for mechanisms for increasing employee ownership. Importantly, while employee ownership enjoyed fairly widespread popularity, the specific form which employee ownership took in the ESOP is the work of Kelso and Long. And, their project was to create a "vehicle for broadening capital ownership, not a means of industrial democracy."[132] Thus, ESOP legislation focuses narrowly on ownership and is actually rather undemocratic in structure. For instance, the "ESOP provisions engrafted on ERISA place control of employer stock in the hands of a trustee who is ordinarily appointed by the employer's board of directors" rather than placing control directly in the hands of the employees.[133] Furthermore, while employed with the company in question, employees enjoy only beneficial ownership in the employer stock, meaning they do not receive typical shareholder rights.

[130] Freeman (2007) pg. 3
[131] Murphy (2005) pg. 658
[132] *Ibid.* pg. 658
[133] *Ibid*. pg. 659

Comparing ESOP and Worker Cooperative Performance

The prominence of employee ownership in the form of ESOPs, and my claim that this results from favorable public policy treatment, justifies an examination of ESOP performance both independent of and relative to that of worker cooperatives; could it be that ESOP use is simply highly effective, indeed more effective than worker cooperatives, and that this is the root of their dominance of employee ownership? The empirical evidence strongly suggests that this is not the case. As Murphy (2005) observes: “A central irony of the ESOP, thirty years after its recognition in the Employee Retirement Income Security Act of 1974, is that it has succeeded best where it has been used in participatory ways for which it was never intended and is poorly designed.”[134]

ESOPs have demonstrated to be effective in increasing firm performance, employee morale, and employee benefits, but primarily achieve such results when they constitute close to 100 percent employee-ownership and are employed in conjunction with employee participation schemes. In this sense, ESOPs appear to be most effective when they more resemble cooperative organizations than merely a form of pension plan.[135] And, cooperatives still tend to outperform their ESOP counterparts in many instances. A closer examination of the empirical research emerging out of the forty years of ESOP history helps clarify this generalization.

There are undoubtedly demonstrated gains possible from ESOP adoption for the employees, the firms, and even non-employee shareholders. With regards to employee benefits, for instance, “Blasi et al. (1996) found 8% higher average compensation levels

[134] Murphy (2005) pg. 655

[135] Throughout this chapter, I will refer to ESOPs that constitute majority ownership and are implemented in conjunction with participatory measures as “inclusive ESOPs” and I will refer to ESOPs that constitute a small percentage of ownership and are implemented without any additional participatory measures as “exclusive ESOPs” unless otherwise clarified.

among public companies in which broad-based employee ownership plans held at least 5% of company stock."[136] Additionally, studies conducted in both Massachusetts and Washington State measuring the relative levels of pay and benefits for ESOP and non-ESOP firms found no substantial differences in pay, indicating that ownership does not substitute for current income or benefits but rather acts as a bonus in addition to current pay and benefits.[137] Not only does compensation in ESOP firms reflect employee benefits, but Blair et al. (2000) found that "firms holding more than 17% of company stock over the 1983-95 period had significantly longer average employee tenure than matched firms without ownership," demonstrating greater job security among ESOP firms.[138] Finally, some studies demonstrate increased job satisfaction, organizational commitment, and motivation associated with ESOP adoption, but the evidence on the subject is mixed.

The consistent point of divergence about whether or not ESOP adoption influences these latter employee experiences is not the size of the ESOP, which one may expect, but rather the pairing of increased employee participation in the firms along with ESOP adoption.[139] Employee ownership in ESOPs does appear to positively impact employees, and thus may provide a partial explanation for ESOP dominance, but the evidence regarding employee experience at firms suggests that, besides compensation, other benefits are not primarily the result of ESOP adoption, but rather, associated with participatory policy adoption observed in inclusive ESOPs, not exclusive ESOPs. And, while employee considerations are important in understanding ESOP adoption, firm

---

[136] Freeman (2007) pg. 6, citing Blasi et al. 2006
[137] *Ibid.*
[138] *Ibid*. pg 7, citing Blair et al. (2000)
[139] *Ibid.*

consideration is almost inevitably more so; a look at the impact of ESOPs on firm performance may provide better insight into why ESOP adoption dominates employee ownership.

A great deal of ESOP research reveals “robust, positive, firm-level effects” associated with productivity, profitability, and longevity, but while the effects are well-established, the causal mechanisms by which the effects are produced are less certain.[140] Performing a meta-analysis of 11 studies evaluating comparison of firm performance before and after ESOP adoption, ESOP to non-ESOP firms, or post-adoption performance of ESOP firms to matched non-ESOP firms, Kruse and Blasi (1997) conclude that “on average in all the performance categories, ESOP companies do better per year than non-ESOP companies and that companies do better post-adoption than pre-adoption” by approximately 4 percent annually.[141] Employee ownership is not only associated with increased productivity, but also with greater firm stability. Park, Kruse and Sesil (2004) tracked the survival rates for all public companies in the US between 1988 and 2001 and found that companies that were 5 percent or more employee-owned were only 76 percent as likely to disappear as firms without employee ownership.[142] Blair et al. (2000) found corroborating results studying the survival rates for public firms with substantial employee-ownership between 1983 and 1995; their results revealed that substantial employee-ownership increased the survival rates by about 20 percent.[143] And, in an ongoing project, “Blasi and Kruse (2007) track all privately held companies with ESOPs in 1988, and found they had similarly higher survival rates than closely matched

[140] *Ibid*. pg. 10
[141] *Ibid.* pg. 11, citing Kruse and Blasi (1997)
[142] Park, Kruse, and Sesil (2004)
[143] Blair et al. (2000)

companies without ESOPs."[144] Employee ownership, although associated with better firm performance, does not appear to be enough on its own to explain the success of ESOP programs, for not all ESOPs are created equal.

Indeed, empirical evidence strongly supports the notion that employee participation, paired with ownership is determinate of benefits of employee ownership. Quarrey and Rosen (1993) found "significantly higher post-adoption growth for ESOP companies that had participation groups and for ESOP companies in which management perceived higher worker influence."[145] In line with this conclusion, a U.S. Government Accountability Office report in 1987 "found significant increases in productivity where the companies reported high levels of worker influence, but only when the companies reported an increase in employee voting rights or worker influence after adoption."[146]

Demonstrating that these conclusions are broadly true, Kruse (2002) reviewed the conclusions from 31 published studies on employee attitudes and behavior under employee ownership found one of the key conclusions to be that "increasing employee participation and influence can make greater use of employee skills and knowledge, and may be an important complement of employee ownership that can improve attitudes and performance."[147] Thus, it appears that ESOP benefits are not simply a result of giving employees a stake in the company that employs them—essentially correcting for any principle-agent problem—but rather the result of a combination of ownership and participation. While it is difficult to assess the relative importance of financial stake and employee participation, inclusive ESOPs demonstrate rewards from employee ownership

---

[144] Freeman (2007) pg. 12
[145] *Ibid.* pg. 14, citing Quarrey and Rosen (1993)
[146] *Ibid*. pg. 14
[147] *Research Evidence on Prevalence and Effects of Employee Ownership* (2013) (testimony of Douglas Kruse). pg. 5

that exclusive ESOPs do not because the latter neglect the importance of giving employees a voice in the workplace in conjunction with ownership.

Cooperative enterprises ought to achieve, by their very nature, precisely this winning combination of ownership and participation. Given the similarity between inclusive ESOPs and worker cooperatives, we should expect worker cooperatives to outperform exclusive ESOPs as inclusive ESOPs do. The evidence on worker cooperative performance indeed supports this. Craig et al. (1995) demonstrated that worker cooperatives in the US plywood industry are between 6 and 14 percent more efficient than their more traditional counterparts with regard to output, holding inputs constant.[148] Bartlett et al. (1992) found higher value-added per worker, indicating higher productivity, among cooperative workers in a comparison of Italian worker cooperatives in light manufacturing with similar, similarly sized private firms in the same sector and region.[149] And, Doucouliagos (1995), studying labor-managed firms found that they maintain "stronger positive correlation with productivity than firms where workers only participate in control" supporting the notion that both ownership and participation are necessary for employee involvement to be most effective.[150] The more consistent productivity effects of worker cooperatives, relative to exclusive ESOPs that only incorporate ownership or firms without any employee ownership but with some employee control, suggests that the necessary wedding of ownership with decision-making control—the most direct, thorough participation possible—in cooperatives is responsible for gains from worker-ownership.

[148] Artz and Kim (2011)
[149] *Ibid.*
[150] *Ibid.* pg 17

Additionally, the employee benefits associated with both exclusive ESOPs—compensation—and inclusive ESOPs—compensation and job satisfaction—are equally or more pronounced with cooperatives. Case evidence for worker cooperatives often report higher compensation as compared with non-cooperative firms in the same industry. Hochner et al. (1988) present a grocery cooperative in Philadelphia that “maintained higher levels of full-time jobs at higher wages than competitors without decreasing profits.[151] At a worker-owned grocery in the San Francisco Bay Meyer (2006) showed that average compensation for employees was 40% greater than that of unionized grocery workers in California.[152] A number of additional American worker cooperatives report similar benefits; the Union Cab Cooperative in Madison, WI, Isthmus Engineering in Madison, WI, Alvardo Street Bakery in Petaluma, CA are a few cooperatives started in 70s and 80s which have experienced marked success and boast superior member compensation and satisfaction.

The overall performance of ESOPs relative to cooperatives does not appear to be the source of ESOP dominance in the arena of worker ownership. Instead, the institutionalization of ESOPs and the simultaneous exclusion of worker cooperatives from public policy work to privilege adoption of the former over adoption of the latter. The history of the development of ESOP legislation reveals the impetus behind their development, the extent to which they have been employed outside their original purposes, and the justification for making them a tax privileged entity.

[151] *Ibid.* pg. 20
[152] *Ibid.*

Coercive Isomorphism: Tax-favored ESOP Policy

The ESOP legislation ushered in by Senator Long provides numerous tax benefits derived from ESOP adoption. ESOPs not only enjoy the same tax benefits available to other qualified retirement plans—deduction of employer contributions to the plan, exemption of trust from taxation on earning, and employee tax deferrals upon ultimate distribution of their individual accounts—but also additional, ESOP specific tax advantages. Because they allow employers to pay off their ESOP loans with deductible contributions to the ESOP trust, ESOP adoption effectively provides the employer with funds from the sale of stock to their employees "which are financed by a uniquely tax-advantaged loan in which principal as well as interest payments are tax deductible."[153] During Senator Long's years in office, a number of other tax incentives for ESOP adoption were introduced. Some of these—i.e. tax credits, an estate tax deduction, and tax exclusion on interest from ESOP loans—were later repealed, but others continue to offer significant tax advantages; "the tax code allows employers to deduct payment of dividends to stock held by an ESOP and promotes the use of ESOPs as an estate planning device for retiring business owners by allowing a deferral of gain on the sale of qualified securities to the ESOP trust."[154] Although it is difficult to quantify precisely the advantage ESOP adoption provides, it is evident that consideration of tax advantage is an influential factor in ESOP adoption.

A survey of about half of all ESOPs in existence in 1985, conducted by the General Accounting Office, is very revealing of the extent to which tax favorable policy influenced ESOP adoption. 74 percent of surveyed ESOPs reported tax advantages as an

[153] *Ibid.* pg. 660
[154] *Ibid.* pg. 661

influence in their decision to adopt the plan.[155] At the time of the survey, tax-credit ESOPs were still available (introduced in 1974 and discontinued in 1986) and overwhelmingly dominated the form which ESOPs took. 6,391 tax-credit ESOPs existed in 1985, compared with a combined 692 leveraged, leverageable, and non-leveraged ESOPs.[156] This was largely the case because tax-credit ESOPs offered "a total subsidy, not a modest incentive such as the tax benefits for leveraged and non-leveraged ESOPs."[157] Tax-credit ESOPs were discontinued in 1986 because it became apparent that they were an excessive taxpayer expenditure that, due to the way they were structured, primarily benefited more highly paid employees. In the absence of that ESOP option, the more modest tax benefits of remaining ESOP types continue to encourage ESOP adoption. In the late 1980s, after the elimination of tax-credit ESOPs, leveraged ESOPs became very popular. Between 1974 and 1986, the cumulative borrowing for leveraged ESOPs was less than $1 billion; by the close of 1989, that number had ballooned to $30 billion.[158] The history of the tax-credit ESOP and the transition to leveraged ESOPs upon their discontinuance usefully illustrates the importance of tax favorability in informing firm adoption of employee ownership policy.

Several authors posit the potential for cooperative formation from employee-buyouts of retiring small business owners. Despite this potential, ESOP tax advantages related to estate planning for retiring business owners make them more attractive an option than cooperative structuring. Specifically, "owners of a business corporation can

---

[155] Joseph R. Blasi. *Employee Ownership: Revolution or Ripoff?* Cambridge, MA: Ballinger Pub., 1988. pg. 101

[156] *Ibid*. pg. 103

[157] *Ibid.* pg. 79

[158] Beatty, Anne. "An Empirical Analysis of the Corporate Control, Tax and Incentive Motivations for Adopting Leveraged Employee Stock Ownership Plans."*Managerial and Decision Economics* 15, no. 4 (1994)

receive a tax deferral on capital gains from stock sales when they sell their firm to employees."[159] The tax benefits from this process, known as a 1042 rollover, can more easily be achieved through conversion to an ESOP than to a cooperative. Notably, the advantage of conversion to an ESOP is the direct result of the fact that "conversion to a worker cooperative must be finished in a much shorter time period than conversion to an ESOP under cooperative incorporation statutes."[160] Thus, while the typical 1042 rollover ESOP is executed as a multistep transaction over five to ten years, conversion to a cooperative must be executed as a one time, 100 percent conversion, which is rather difficult to fund.[161] Furthermore, "commercial lenders who make loans to ESOPs are permitted to deduct half the interest from their earning as long as the firm is at least 50% employee owned," thus advantaging ESOP formation over cooperatives by incentivizing commercial lenders to grant loans for ESOPs and not for cooperatives (which lenders are already skeptical of due to lack of familiarity and misconceptions about cooperative viability).[162]

Interestingly, although it is tax-favored in a number of ways, ESOP conversion has been estimated to actually be more expensive that cooperative conversion. Northcountry Cooperative Development Fund (2006) estimates that the cost to establish an ESOP ranges from $20,000 to $35,000 on top of an annual maintenance cost between $7,500 and $15,000—largely due to the reporting requirements of ERISA—while they estimate establishment costs for cooperatives to be between $5,000 to $20,000 and are

[159] Artz and Kim (2011) pg. 27
[160] *Ibid.*
[161] *Ibid*, citing Logue (2006)
[162] Artz and Kim (2011) pg. 27, citing Martin (1994)

not subject to the same maintenance fees.[163] However, the legal codification of ESOPs creates a level of familiarity and ease favorable to their adoption, which combined with the time period advantages of adopting an ESOP appear to outweigh potential overall savings.

Beatty (1994) demonstrates that ESOP adoption is not exclusively the result of tax motivations. Indeed, she argues that ESOPs are primarily adopted for at least one of three reasons: “as a takeover defense, as a mechanism for providing incentives to employees, and as a vehicle for tax savings.”[164] The flexible nature of an ESOP makes it useful in accomplishing all three of these. Interestingly, of the three reasons for adoption, two—takeover defense and tax benefits—have very little to do with improving firm performance or employee benefits/satisfaction and do not reflect the original intent of ESOP legislation. It is reasonably clear that ESOPs have as substantial popularity as they do in large part due to their institutionalization and potential tax benefits, as well as their potential for additional firm and employee benefits.

Comparing ESOP Policy with Cooperative Policy Abroad

While in the U.S. the impact of coercive isomorphism is realized in employee ownership in the form of ESOPs, other countries have taken public policy approaches to enable and promote employee ownership in the form of worker cooperatives and effectively put coercive forces of isomorphism on the side of cooperatives. Dickstein (1986) reports that “cooperatives in Italy, France, and the kibbutzim in Israel have all received external government or political support that has helped them become

[163] *In Good Company: A Guide to Cooperative Employee Ownership.* Technical paper. 2006. Accessed 2013. www.ncdf.coop/documents/worker_coop_toolbox.pdf.
[164] Beatty (1994) pg. 299

established."[165] In much the same way that the U.S. privileges ESOPs, favorable legislation in Italy, France and Spain provides cooperatives with advantages in taxation and specialized financing, and also provides additional support for cooperative formation and survival. There is undeniably a problem of endogeneity in identifying the exact extent to which cooperatives are the consequence of policy or the policy the consequence of influential cooperative systems. But, despite uncertainty about precise extent, government support certainly contributes to making these some of the most cooperative-populated areas in the world. Italy is home to over 7,000 worker cooperatives employing roughly 400,000 people, while France boasts almost 2,000 cooperatives employing about 40,000 people and Spain maintains an estimated 18,000 cooperatives employing close to 300,000 people.[166] The diversity of the experience of cooperatives in the countries suggests that While the advantages for cooperatives in Spain are quite straightforward—they are taxed at a 10 percent rate rather than the corporate rate of 28 percent—a closer look at the cooperative public policy in Italy and France reveals the extent to which government support for cooperatives both enables and helps maintain cooperative presence in an economy.

The impressive cooperative sector in Italy is assuredly the product of both favorable government and broader environmental characteristics. Policy pertaining to cooperative development and maintenance is of the highest order in Italy; it is enshrined in the Constitution, indicating a noteworthy cooperative influence from the country's start. Corcoran and Wilson (2010) note that "Article 45 of the Constitution states that 'the

[165] Carla Dickstein. "The Roles of Support Organizations in Worker Cooperative Systems: A Comparative Case Study." PhD diss., University Microfilms International, 1986. pg. 71
[166] Hazel Corcoran and David Wilson. *The Worker Co-operative Movements in Italy, Mondragon and France: Context, Success Factors and Lessons*. Issue brief. 2010.

Republic recognises the social function of co-operation with mutual character and without private speculation purposes. The law promotes and favors its growth with the most appropriate means, and ensures, with appropriate controls, its character and purposes.'"[167] The specifics of cooperative public policy today include tax breaks, provision of regional economic development agencies, assistance in financing the conversion of traditional firms into cooperatives, and mandated inclusion in cooperative federations.[168] With regard to tax policy, Italian law exempts profits from taxation as long as they are reinvested in the cooperatives. Furthermore, legislation requires that cooperatives put at least 30 percent of annual net profit in an indivisible reserve fund for the cooperative, which effectively helps prevent undercapitalization in the long run; over time these indivisible reserves become quite large and are an important source of stability for the cooperatives.[169] Importantly, the Italian government provides these tax incentives because "co-operatives are seen as a public good that is available to future workers," and as a way to maintain stable sources of employment.[170]

In addition to tax benefits, public policy in Italy provides for the presence of regional economic development agencies. These agencies provide cooperatives with assistance in "the areas of 'research and development, education and training, workplace safety, technology transfer, marketing and distribution, and exporting' among others."[171] Typically, the economic development agencies provide services difficult for small businesses to perform in house.

---

[167] *Ibid*. pg. 7, citing the Italian Constitution, Article 45
[168] *Ibid.*
[169] *Ibid.*
[170] *Ibid*. pg. 7
[171] *Ibid.* pg. 8, citing Fici, A. (2009) The New Italian Cooperative Law and Cooperative Principles

Beyond tax advantages, the Italian government assists cooperatives with additional capitalization needs. Through the Marcora Act in 1985, the government established a cooperative fund specifically devoted to helping fund new cooperatives. New cooperatives may be formed in a number of ways. A number of cooperatives are founded upon the dissolution of a traditional firm; private firms "going through bankruptcy, moving overseas, or who [are] being sold by retiring owners" can seek assistance from the cooperative fund to enable transition into cooperatives.[172] Even more significantly, "since 1992, three percent of a co-op's profits have been placed into co-operative development funds. These funds are used to help create new cooperatives, develop existing ones, and to convert private firms into worker cooperatives."[173] Some of the largest cooperative federations, such as Legacoop, maintain capitalization of several million in U.S. dollars. A final noteworthy element of Italy's cooperative legislative agenda is the requirement, originating in the Basevi Law of 1947, for cooperatives to join one of three federations. This requirement creates the dual impact of increasing stability against financial problems and organizing cooperatives into politically influential units.[174]

While generally the Italian economy is not particularly strong and has a high rate of unemployment, the experience of the Emilia Romagna region provides support for the argument that enabling worker cooperatives strengthens the economy. In Emilia Romagna cooperatives boast a particularly robust presence; there are about 5,000 worker owned cooperatives, roughly 10 percent of the workforce is employed by cooperatives, and about 30 percent of GDP in the region is generated by worker cooperatives. The

---

[172] *Ibid.* pg. 8
[173] *Ibid*. pg. 8
[174] *Ibid.*

region has a per capita GDP 25 percent higher than the average in Italy and 36 percent higher than the average for the European Union. In 2006, the unemployment rate was 3 percent, compared to over 8 percent for Italy generally. Furthermore, the "region has one of the lowest rates of inequality in Europe, with a Gini coefficient of .25."[175] And, the region has weathered the financial crisis and economic recession remarkably well, which some attribute to the predominance of small-businesses and cooperatives in the region.[176]

Like Italy, France's vibrant cooperatives sector is strongly supported by public policy. Worker cooperatives in France primarily take the form of SCOPs, which legislatively require that workers have at least 51 percent of the capital and 65 percent of the votes in the organization.[177] While this structure differs slightly from a more traditional worker cooperative, it maintains primary tenets of the form insofar as majority control lies with the workers, who all maintain a stake in the company even if it is not a 100 percent stake. Importantly, this structure allows for SCOPs to obtain financing from outside investors rather than only from employees, which is a useful source of capital. SCOPs benefit from tax breaks through an exemption of the professional tax—about 1.5 to 2.5 percent of revenues—and an income tax exemption for income on worker shares.[178] In order to receive these tax benefits, the cooperatives must go under "co-operative review" periodically to ensure that the organizations are operating appropriately.[179] Additional SCOP legislation requires SCOPs to place a minimum of 15 percent of surpluses in reserves, although the actual percentage is closer to between 40

---

175 *Ibid.* pg. 6
176 http://www.presseurop.eu/en/content/article/3117441-unity-strength-emilia-romagna Accessed April 22, 2014
177 Corcoran and Wilson (2010)
178 *Ibid.*
179 *Ibid.*

and 45 percent on average. These SCOP "reserves are permanently owned by the co-operative, ensuring financial stability in the long run."[180]

In addition to tax planning legislation, France gives preference to cooperatives for government contracts and provides direct assistance for the conversion of private firms into cooperatives. France has policy to shelter markets for worker cooperatives through public sector purchase of goods and services and gives preference to worker cooperatives in bidding for public sector contracts when the price is equal to other bids. As discussed earlier, conversion to an employee owned firm from a more conventional form primarily takes the form of ESOPs in the U.S. as product of ESOP advantages and familiarity. Dickstein (1986) notes that in "1978 France passed a new law that gave a more coherent legal framework to cooperatives and made it much easier to convert conventional companies to cooperatives."[181] The institutional support for cooperatives in their development and maintenance in France, like in Italy, is quite foundational to their success.

Conclusion:

Worker cooperatives in the United States lack the type of government support visible in other countries where they develop and prosper. Rather than supporting employee ownership in the form of cooperatives, the government promotes the adoption of ESOPs. For historical political purposes—namely the collaboration of Senator Long and Louis Kelso—ESOPs gained legislative popularity. The ESOP friendly legislation that has existed and developed since their introduction in 1974 has inspired widespread adoption of such plans. Government policy acts as a mechanism of institutional

---

[180] *Ibid.* pg. 26, citing Lenancker, P. (2010, April 4). La France peut garder ses PME industrielles. Le Monde
[181] *Ibid.* pg. 71

isomorphism for the narrow realization of employee in ESOPs rather than cooperatives and offers useful explanatory value about the scarcity of worker cooperatives in the U.S.

Ironically, though, the plans have most succeeded when they deviate from a pure ESOP arrangement and more mimic cooperative organizational form. Gains from employee ownership are more consistently realized when employee ownership resembles the cooperatives form than when employee ownership exists in the form of an ESOP. Many ESOPs are adopted for the purpose of accessing tax privileged capital or for resisting hostile takeovers, not as a mechanism for increasing firm performance and employee benefits/satisfaction; and for those ESOPs adopted with the latter goals in mind, the ESOP structure is less apt than a cooperative model. Although employee ownership of company shares would certainly be smaller without ESOPs, perhaps more comprehensive employee ownership in the form of cooperatives would be more prevalent. As the experiences in Italy and France help demonstrate, public policy focused on cooperatives can help change the landscape of employee ownership; the incorporation of cooperative specific legislation contributes significantly to the development and support of cooperatives, which then allow for the realization of the benefits of comprehensive employee ownership.

Chapter 3:

Worker Cooperative Scarcity Part II: Mimetic and Normative Isomorphism

Although, as the previous chapter demonstrates, public policy factors are important in explaining cooperative scarcity, so too are other environmental factors. Lacking governmental support, cooperatives may proliferate as an organizational form due to non-governmental support. For instance, to a great degree, the success of the Mondragon Cooperative Corporation is attributable to the firm's remarkable success in building a massive support system for the development and continuation of cooperatives. Similarly, both Italy and France boast strong cooperative federations that, as private organizations, function to provide assistance in financing, training, development, and management for cooperatives. While DiMaggio and Powell's conception of coercive factors in organizational isomorphism is quite useful in understanding the public policy role in cooperative scarcity, their concepts of mimetic and normative factors in are useful in interpreting non-governmental reasons for scarcity. I argue that for mimetic and normative reasons, cooperative scarcity begets scarcity. Insofar as successful enterprises inspire mimicry and familiarity with an organizational form yields lower informational costs and greater access to funding the U.S. has little precedent for cooperative formation. Nor do norms prevailing in professional education, organizational networks, early education, and other areas of life in the U.S. cultivate propensity for cooperation.

Scarcity of the worker cooperative as an organizational form in the US economy has important consequences for the organizational form that new entrants in the economy take. A low density of worker cooperatives in the economy necessarily (re)produces uncertainty about the organizational form. While successful capitalist organization spread awareness of the success potential of hierarchical organization, in the United States, neither large nor numerous cooperatives exist to spread awareness of the organizational form and combat prevailing perceptions of the organizational form as inefficient. While one avenue for cooperative success was discussed in the previous chapter—government promotion and support—another avenue for cooperative success and proliferation is non-governmental support emerging out of cooperative success.

There is certainly a problem of endogeneity involved in disentangling the relative influence of government policy from the influence of a successful non-governmental support organizations who shelter and advocate for cooperatives. DiMaggio and Powell readily agree that the typology they propose "is an analytic one: the types are not always empirically distinct. For example, external actors may induce an organization to conform to its peers by requiring it to perform a particular task and specifying the profession responsible for its performance. Or mimetic change may reflect environmentally constructed uncertainties."[182] Still, in the same way that certain coercive factors are readily identifiable in government inclusion and support for capitalist firms and simultaneous exclusion of cooperative forms, certain mimetic and normative factors are identifiable that help explain cooperative scarcity as the product of uncertainty and normative exclusion often born of form scarcity. The chapter proceed in the following manner:

Mimetic Isomorphism: The Absent Cooperative Model

As a reminder, DiMaggio and Powell explain that mimetic isomorphism results from standard responses to uncertainty. They argue that "uncertainty…is a powerful force that encourages imitation. When organizational technologies are poorly

[182] DiMaggio and Powell (1983) pg. 150

understood…when goals are ambiguous, or when the environment creates symbolic uncertainty, organizations may model themselves on other organizations."[183] A modeled organization—the organization being imitated—"serves as a convenient source of practices that the borrowing organization may use" often without any intention to do so.[184] Thus, while the root of scarcity—governmental or non-governmental—may be unknown or difficult to isolate, its perpetuation can be understood as a standard response to uncertainty. Particularly in an environment in which hierarchical firm organization is as ubiquitous as it is in the US and in which perceptions of cooperatives remain so out of line with their empirical performance, it is easy to see how mimetic isomorphism helps to explain cooperative scarcity.

Perotin (2006) reinforces DiMaggio and Powell's theory of mimetic isomorphism specifically regarding cooperatives, asserting that "legitimacy may also be conferred by the density of existing cooperatives. The organizational ecology literature, e.g. Carroll (1984) and Carroll and Hannan (1989), argues that as the number of organizations of a given form grows, the form is regarded as more legitimate and this legitimacy in turn results in more organizations of the same kind being created."[185] Elster (1989) corroborates Perotin's interpretation of the impact of cooperative density on cooperative development, articulating: "It is a truism, but an important one that workers' preferences are to a large extent shaped by their economic environment. Specifically, there is a tendency to adaptive preference formation, by which the actual mode of economic

[183] *Ibid*. pg. 151
[184] *Ibid*.
[185] Virgine Pérotin. "Entry, Exit, and the Business Cycle: Are Cooperatives Different?" *Journal of Comparative Economics* 34, no. 2 (2006)pg. 299

organization comes to be perceived as superior to all others."[186] Not only is there strong theoretical reasoning to support the notion that, despite efficiency concerns, prevailing organizational norms precipitate imitation even when preferable organizational forms exist, there is also some empirical support. Countries with larger cooperative sectors—i.e. Italy, France, and Spain—all witness greater cooperative development than the US, despite differing levels of government support, suggesting that the cooperative density in the economy plays some role. Furthermore, Perotin (2006), studying cooperatives in France, demonstrates that "the density of cooperatives has he expected quadratic effect; the size of the [worker cooperative] population acts as a legitimizing and resource-generating factor."[187]

The scarcity of cooperatives simultaneously leaves unchallenged the legitimacy effect of hierarchical firm dominance in the economy, but also creates tangible costs as a result of uncertainty. Specifically, scarcity induced uncertainty creates additional costs for cooperatives by introducing costs associated with researching non-traditional firm organization rather than simply mimicking prevailing organizational forms and by making financing more difficult to procure and often more expensive when it is procured.

There are real costs associated with the need to research and study cooperative organization in face of uncertainty due to organization scarcity. Doucouliagos (1995) notes that organizational conformity can stem "from costs incurred in searching for information about labor-managed firms."[188] Cooperative scarcity produces a lack of familiarity with the organizational model that is costly to overcome; it is simpler and less

[186] Jon Elster. "From Here to There; Or, If Cooperative Ownership Is So Desirable, Why Are There So Few Cooperatives?" *Social Philosophy and Policy* 6, no. 02 (1989): pg. 110
[187] Perotin (2006) pg. 304
[188] Doucouliagos (1995) pg. 50

costly to mimic a successful hierarchically organized firm. Doucouliagos argues that this is particularly true for entrepreneurs endeavoring to start a new business because they already "face enough problems with setting up, meeting legal requirements, technical specifications, marketing and distribution and quality control" much less searching "for an alternative way of organizing the whole show" and courting additional costs.[189] However, in countries with strong cooperative sectors, the costs associated with organizational unfamiliarity are greatly mitigated by the assistance of support organizations.

Compounding the cost of uncertainty shouldered by the prospective cooperative firm due to its own uncertainty are costs induced by financial organizations' uncertainty about cooperatives. In economies with greater cooperative density, financing institutions are familiar with the form and have a superior understanding of the actual risk cooperatives face, making them more willing to grant loans to such organizations as reasonable rates. Perhaps more importantly, economies with a strong cooperative sector are likely to maintain both governmental and non-governmental support organizations that help lessen the costs of attaining information on cooperative organizations and organizational form and provide assistance for establishing cooperatives. Conte (1986) explains that the US lacks a network of supporting organizations present in some other countries. He notes that the central roles of these organizations involve providing informational and institutional support, assisting with the arrangement of financing—although very rarely through subsidization—and lobbying for the "adoption of legislation

[189] *Ibid.*

defining cooperatives in the context of their country's corporation laws."[190] The practical effect of these activities "is to decrease the uncertainty surrounding the founding and operation of cooperative corporations."[191]

Financing worker cooperatives in the US is uniquely difficult; it is far more difficult than financing cooperatives in countries with more hospitable public policy and/or with a strong cooperative sector—i.e. Spain due to the Mondragon presence. Levin (1984) explains that "one of the major difficulties faced by worker cooperatives and worker-owned firms has been access to financial capital. Without the ability to borrow for purposes of meeting shot-term cash flow needs or long-term expansion, these firms have faced substantial difficulties in surviving and competing in the marketplace."[192] Indeed, an important result of cooperative scarcity in an economy is that "the organizational form of [cooperatives] is relatively unknown to financiers and hence seems to bear greater risk to financiers."[193] Uncertainty about the cooperative form, and the prevalence of perceptions of cooperative inefficiency in the US make lending institutions skeptical of granting loans to cooperative organizations; when granting loans, moreover, financiers are inclined to set the loan rate higher than they would for more traditional capitalist firms. Without numerous or prominent cooperative organizations in the US and a dearth of cooperative incorporation legislation, there is little to combat uncertainty lending institutions maintain about the cooperative form.

[190] Michael A Conte. "Entry of Worker Cooperatives in Capitalist Economies."*Journal of Comparative Economics* 10, no. 1 (1986): pg. 45
[191] *Ibid.*
[192] Henry M. Levin. "ESOPs and the Financing of Worker Cooperatives." In *Worker Cooperatives in America*, edited by Robert Jackall and Henry M. Levin. Berkeley: University of California Press, 1984. pg. 245
[193] Dougouliagos (1990) pg. 52

It is important to note that in addition to the possibility of discrimination against cooperative firms explicitly created by uncertainty, there are other reasons cooperatives may experience greater difficulty obtaining loans than more conventional firms. One such reason is that "financial lenders prefer to have some measure of control over the affairs of their borrowers, in order to assure that the borrower is following prudent practices with regard to its financial condition."[194] Oftentimes this concern is dealt with through the placement of members of the financial community on the board—which is clearly out of the question in a worker cooperative—or, in the case of small businesses, assessment of the credit worthiness of the owner—which is very difficult considering the multiplicity of ownership in a cooperative.[195] Additionally, cooperatives are unable to provide collateral in the form of company stock (as it is all owned by the workers), making lending institutions even more wary of granting a loan. Certainly, the lack of familiarity with cooperatives compounds the negative impact of the inability of cooperatives to meet these financier preferences; it there was less uncertainty about the cooperative form and cooperatives success, discrimination against cooperatives by the banking industry would pose less of a barrier to cooperative formation. And, less uncertainty ought to lead to less mimetic isomorphism.

Normative Isomorphism: Professional Education and Networks

In addition to coercive and mimetic explanations for organizational isomorphism, DiMaggio and Powell's notion of normative pressures for isomorphism helps illustrate why worker cooperatives are scarce in the US. As a reminder, they argue that isomorphic organizational change of the normative variety "stems primarily from

[194] Levin (1984) pg. 246
[195] *Ibid.*

professionalization" which they define as "the collective struggle of members of an occupation to define the conditions and methods of their work, to control 'the production of producers'…and to establish a cognitive base and legitimation for their occupational autonomy."[196] In particular, they outline two aspects of professionalization as important sources of isomorphism: "one is the resting of formal education and of legitimation in a cognitive base produced by university specialists; the second is the growth and elaboration of professional networks that span organizations and across which new models diffuse rapidly."[197] The role of both of these is visible in the US context.

Professional economics and business education and training in the US overwhelmingly teaches to a conventional, hierarchical firm organization. Professional and vocational training is geared towards preparing individuals for positions within a hierarchical organizational form—i.e. entrepreneur, manager, office assistant, etc.—rather than towards preparing them for working in a cooperative institution. In "today's economics and corporate governance discourse, shareholder primacy is taken as obvious" and investor-owned, for-profit businesses competing to maximize shareholder wealth are almost taken for granted as preferred organizational form. A strong indication of the primacy of capitalist organization over cooperative organization in education is the infrequency with which cooperative forms of business structure are covered in economics and business texts designed for educational purposes. Lynch et al. (1989) reported that introductory economics textbooks used in the United States deemphasized

[196] DiMaggio and Powell (1983) pg. 152
[197] *Ibid.*

cooperatives.[198] Hill (2000) revealed that "the typical textbook does not even recognize cooperatives as a form of business organization."[199] A survey of introductory business texts held in the United States Library of Congress corroborated the two above findings.[200] Interestingly, Kalmi (2007) also found evidence of a neglect of cooperatives in economics texts, but discovered that the paucity of cooperative mention has grown markedly since after World War II; he attributes the coincidence of decreasing attention to cooperatives in textbooks with a "paradigm shift from institutional to neoclassical analysis, which led to a neglect of the potential of cooperatives in addressing social problems."[201]

The extreme dominance of investor-owned, for-profit, hierarchically structured businesses over cooperative businesses in educational texts likely has an impact on the perception and consideration of cooperatives as a viable business form. Parnell (1996) posited that the exclusion of cooperatives from primary, secondary, and post-secondary texts leaves cooperatives as a "much maligned and often neglected option."[202] Indeed, neglecting to teach cooperative models creates barriers for participation in cooperative organizations. A certain set of norms are cultivated through traditional education and training in the US, norms which align with hierarchical firm organization rather than cooperative organization. Alternative or additional training is often necessary to cultivate

[198] John Chamard "Management Education and Development. Co-operatives and Credit Unions in Economics and Business Texts: Changing the Paradigm."*INTERNATIONAL JOURNAL OF CO-OPERATIVE MANAGEMENT*, 2004. citing Lynch et al. (1989)
[199] Panu Kalmi. "The Disappearance of Cooperatives from Economics Textbooks."*Cambridge Journal of Economics*, 2007, 625-47. referencing Hall (2000)
[200] Chamard (2004)
[201] Kalmi (2007) pg. 625
[202] Parnell (1996) Parnell, Edgar (1996) *Reinventing the Co-operative: Enterprises for the 21st Century* from International Cooperative Information Centre (www.wisc.edu/uwcc/icic/orgs/ica/pubs/review/ICAReview-Vol—88-No-4—19951/Book-Reviews1/reinventing- the-Co-operative1.html), cited in Chamard (2004) pg. 34

the cooperative organizational norms crucial for cooperative success. For instance, Dynavac, a highly successful Australian cooperative, invests at least three years of training in democratic management in all new members because they do not generally have appropriate training prior to joining the cooperative.[203] Normative processes of isomorphism certainly operate through the education of business professionals to cultivate a preference for investor-owned, hierarchically organized, more traditional firms and a skepticism of cooperative models. And, given the prevailing organizational and professional training norms, it is unsurprising that professional networks work to reinforce those norms and give them greater ability to travel. DiMaggio and Powell's category of normative isomorphism is, in the above way, quite applicable to understanding some of the source of cooperative scarcity in the US, but I believe that their concept can be extended further to offer greater explanatory value.

I find it pertinent to add to this understanding of the sources of normative isomorphism the importance of other areas of social interaction—i.e. early education, religion, and family structure—in creating hierarchical, rather than horizontal, democratic, norms that reinforce the normality and prevalence of traditional hierarchical firm organization. The common culture of the workplace in the US can be understood as "the common set of norms, values, and expectations about organizational functions and operations that are accepted by all or most of the members of an organization."[204] And, in the US this common culture largely "assumes that workers compete as individuals with other workers for wages and promotion; that the place of workers in the hierarchy of the

---

[203] Doucouliagos 1995

[204] Zelda F. Gamson. And Henry M. Levin "Obstacles to the Survival of Democratic Workplaces." In *Worker Cooperatives in America*, edited by Robert Jackall and Henry M. Levin, 219-44. Berkeley: University of California Press, 1984. pg. 223

firm determines their degree of relative autonomy; that the interpersonal relations among workers are matter-of-fact relations designed to facilitate control and productivity rather than based upon traditional social relations such as those of family or kinship; that the main rewards for work activity are extrinsic ones such as wages, salaries, vacations, pensions, and promotions to higher status rather than the rewards of a high degree of control over one's work activities and of the ability to express one's human and creative potential on the job."[205] While this iteration of common culture in the workplace is not all-pervasive in every workplace, it does reflect the ethos of most hierarchically organized businesses and, as such, most firms in the United States. These rather ubiquitous workplace norms certainly produce and reproduce hierarchical firm organization, but perhaps more interestingly, they reflect norms cultivated outside of the workplace or professional training organizations.

The contrast between the saliency of democratic ideals in the political sphere of life relative to the personal sphere of life—the lived day-to-day experience—is quite stark in the United States. There is a remarkable dearth of democratic decision-making practiced in much of daily life; from a young age, individuals in the US are ensconced in largely hierarchical institutions, such as education, religion, and family life, which engender norms consistent with hierarchical firm organizational norms. Research demonstrates that the schooling experience is greatly responsible for preparing individuals for later participation in hierarchical workplaces.[206] Gamson and Levin (1984) observe that "schools tend to be impersonal, bureaucratic, and hierarchical, like

---

[205] *Ibid.*

[206] *Ibid.* referencing Bowles and Gintis (1976); Carnoy and Levin 1976a; Dreeben (1968). See Inkeles and Smith (1974) *Becoming Modern* for a cross-country analysis supporting the argument that schooling strongly influences fitness for hierarchical workplaces (factories).

the typical workplace."[207] They note the parallels between schools and workplaces, students and workers, in the similarities between grades and grade advancement and salaries and job advancement, expulsion for poor or disorderly school performance and job loss for unsatisfactory job performance, a dearth of autonomy, and supervision and evaluation by superiors who control the content of the work activity and any rewards/sanctions. Similar to school, both family and religion tend to be organized hierarchically rather than democratically, further reinforcing non-democratic norms. While this type of hierarchical experience is not necessarily unique to the US, there are few institutions of an alternative, cooperative structure to challenge their normalcy; even if those alternative institutions are found in the business world in other countries, they offer some greater diversity. In the US, conditioning to hierarchical structures from a young age, unsurprisingly, makes the acceptance of such organization easier and seemingly natural later in the workplace. And, when movements toward more democratic—perhaps cooperative—firm organization fail to gain traction either through professionalization and trade organizations or through cultural norms, the scarcity of cooperatives can likely be expected to persist.

As the above explanations of firm organizational landscape allude to, there is certain endogeneity involved in the scarcity of cooperatives; without the support of government or the independent success of a cooperative creating a support network or shelter organization (which is unlikely within a capitalist economy for the reasons stated above) the landscape is rather inhospitable to cooperative success. While the last chapter explored the governmental role—or lack thereof—in encouraging and enabling cooperative formation, the role of non-governmental shelter organizations and networks

[207] *Ibid*. pg. 224

are as, or perhaps more, important for the success of a cooperative sector. The development of the Mondragon Cooperatives in Spain helps illustrate how important non-governmental support can be. And, to a lesser degree, so does the development of cooperatives in Italy and France.

Lessons from Mondragon, Italy, and France

The formation of structure and support organizations for cooperatives, although necessarily emerging from the success of cooperatives in the absence of government provision, operates to reinforce and perpetuate the success of the cooperative sector. The history of cooperatives in Mondragon (Spain), Italy, and France all highlight the importance of non-governmental support for the development and success of cooperatives and cooperative systems. The Mondragon Cooperative Corporation, as it came to be called, "arose out of conditions of severe economic depression and political repression during the Franco regime in Spain."[208] The first cooperative was started in 1956 by "students of a young Basque priest, Father Jose Maria Arizmendi, who taught about workplace democracy and cooperatives based on Catholic Social Doctrine as well as on his readings about the nineteenth-century cooperative communities of Robert Owen and the Rochdale pioneers in Britain."[209] The success of this initial start-up prompted growth and expansion, and, after some time, the development of new cooperatives designed to deal with organizational and training interests (rather than production). Of particular importance was the strategic approach pursued by Mondragon in this process. Mondragon created a particularly united, well-integrated system by establishing secondary cooperatives as support organizations; "as specific needs arose, key personnel

---

[208] Dickstein (1986) pg. 70
[209] *Ibid.* pg. 71

from the cooperatives moved over to the second degree cooperatives to share their skills with newer cooperatives."[210] In this way, the new cooperatives had the knowledge-based support for the cooperative form they needed to both operate as a cooperative and provide support for present and future cooperatives. Among the support organizations are: the League of Education and Culture, which coordinates educational centers and manpower planning; the Caja Laboral Popular, which is a cooperative bank and cooperative development agency; Ikerlan, which acts as a research and development institute; Lankide Export, which is responsible for export trading; Lagun-Aro, which is essentially and internal social security system; Ikasbide, which is a management and training center that provides courses on cooperative, socioeconomic, and technical management subjects; and a number of cooperative federations representing various industrial sectors.[211]

Although rather different, Italy also maintains—and has for much of its history—a strong cooperative support system. And, while worker cooperatives are strongly incentivized in Italy (as the previous chapter explains) there is also a very important non-governmental support system of shelter organizations that helps explain cooperative success in the country. Primarily responsible for acting as shelter organizations are the three cooperative federations in Italy. These three cooperative federations represent all of the different types of worker, consumer, and agricultural cooperatives in the country.[212] Each of the three federations—Lega Nazionale delle Cooperative e Mutue, Confederazione Cooperative Italiane, and Associazione Generale delle Cooperative

[210] *Ibid*. pg. 78
[211] *Ibid.*
[212] *Ibid*.

Italiane—are backed by one or more political party in Italy.[213] In practice, the federations are all similarly structured and "cooperate at the national level to represent the interests of the cooperative 'movement.'"[214] Internally, the federations each have sub-organizations to perform specific support functions (similar to the secondary cooperatives within the Mondragon system). For example, Lega Nazionale delle Cooperative e Mutue is constituted of a number of such sub-organizations such as a consortium to serve worker cooperatives at the regional and national level (ANCLP) and trade organizations representing cooperative sectors. A financial intermediary (Fincooper), an import/export arm (Intercoop), and two insurance companies (Unipool and Unifina) grew out of ANCLP.[215] The Lega structure is quite similar to that of the other federations. The three shelter organizations offer important assistance in the start-up and support of cooperatives. It is important to note that in Italy's case, the problem of endogeneity regarding whether cooperative success engendered government support or vice versa is quite pronounced. There is striking "cross-sector co-operative solidarity (worker, consumer, producer, financial)" in Italy based in a strong ethical norm of mutual aid and dependent on the "strong system of informal networks and formal federations" found in the country.[216] The historical popularity and mutual support of worker cooperatives in Italy suggests that cooperative success and organizing is responsible for the extremely favorable government policy towards cooperatives, which further reinforces the organizational form's strength in the country.

---

[213] Corcoran and Wilson (2010)
[214] Dickstein (1986) pg. 78
[215] *Ibid.*
[216] Corcoran and Wilson (2010) pg. 10

France, too, must attribute some of the vibrancy of its cooperative sector to the role of support organizations. The primary organization, the French General Confederation of SCOPs (CG-SCOP) is composed of numerous sub-organizations responsible for providing cooperatives with assistance in their formation and their continued success. Among the resources provided, "CG-SCOP has a support network of professionals in each region to help create and develop worker co-operatives, as well as supportive financial services, industry sector federations in construction, communication and manufacturing, and representation at the regional, national and international levels."[217] More specifically, this overarching support organization has a general confederation for representation at the national level, twelve regional unions that deal with day-to-day development of SCOPs and provide representation at the regional and local levels, and three professional federations—sectioned into building and public works, communication, and manufacturing, metallurgy, and technologies—to "represent member SCOPs in dealing with authorities in their respective fields and provide economic, technical and legal advice as well as support in the development of their activities."[218] While the CG-SCOP network is rather similar to the network present in Italy and the internal system of Mondragon, France has a unique additional network; the Association for the Promotion of Enterprise and Takeover of Enterprise (APERE) specializes in succession planning. The organization incorporates "senior volunteer business advisors (e.g., retired CEO's), expert professional consultants, and national

[217] *Ibid*. pg. 27
[218] *Ibid*. pg. 28

partners," such as cooperative financiers and insurance companies, to provide assistance in converting failing firms to cooperatives.[219]

Conclusion

The important similarity in all the above scenarios is the development of strong non-governmental support organizations for cooperatives. The relative importance of governmental and non-governmental support is certainly difficult to discern, but it seems clear that the presence of at least one is, if not necessary, rather important for the widespread success of cooperatives. Despite a surprisingly rich history of worker cooperatives in America, no strong support organizations have developed and maintained a presence in the country. Curl (2009) produced an exhaustive history of cooperative movements in the United States. He asserts that the history of cooperatives in the country "documents how cooperatives were an integral part of numerous American communities in many time periods" and that their role has been sorely neglected in written history.[220] Curl identifies the National Trades' Union of the 1830s, which boasted at least eighteen production cooperatives, as "the first impetus of worker cooperatives as a serious social movement" in the States.[221] Throughout the ensuing years of the 1800s, the cooperative sector grew substantially and peaked at about 300 worker cooperatives in the 1880s. At the heart of this group of cooperatives was the Knights of Labor, who were responsible for the organization of approximately 200 cooperatives.[222]

The Knights of Labor organized with the goal "to secure to workers the full enjoyment of the wealth they create, to harmonize the interests of labor with capital" and

---

[219] *Ibid.*
[220] Curl (2009) pg. 4
[221] *Ibid.*
[222] *Ibid.*

stated publicly their endeavor to "associate [their] own labors, to establish co-operative institutions, such as will tend to supersede the wage-system, by the introduction of a co-operative industrial system."[223] The Knights, and those worker groups they allied with, a brief but formidable opposition to traditional firm organization in American history. Indeed, "almost all of the Knights' worker cooperatives were destroyed in the wake of the 'Great Uprising,'[224] the monumental confrontation between labor and capital that had been building for the entire century, and that resulted in the collapse of the Knights by the end of the 1800s."[225] Since that time, the absence of a strong worker cooperative support organization has undoubtedly impacted the presence of cooperatives in the US. Although cooperative organizations hardly disappeared altogether at the end of 1880s, the rapid and strong expansion the Knights initiated ceased. Had the cooperative movement maintained or even gained momentum, perhaps the type of support networks described in other countries would have emerged in the US; perhaps the presence of a strong cooperative network would have produced mimetic and normative isomorphism towards cooperative organization in some sectors.

[223] *Ibid*. pg. 87, citing Powderly (1889), *Thirty Years of Labor*
[224] See Chapter 5 of Curl for greater detail on the Great Uprising
[225] *Ibid*. pg. 5

Conclusion

On September 15, 2008, Lehman Brothers declared bankruptcy and struck the match that truly ignited the recession beginning in December of 2007 into the worst economic recession in 80 years. The unemployment rate before the Great Recession, as it has come to be known, was 4.4 percent; it peaked at over 10 percent in October of 2009.[226] Interestingly, in the latter half of 2009, while overall economic activity, as measured by GDP, rebounded, unemployment continued to rise.[227] And, while unemployment continued to slump and the economy suffer, Wall Street posted its best performance since taxpayers bailed out the too big to fail banking industry. These events, in large part, kick-started the Occupy Wall Street movement. Emerging from the movement, demands for greater responsibility and democratic organization in the economy revealed a discontentment with what businesses had been doing in the economy. Occupy members, and others, expressed their sentiment that the role of business in society has to do with more than just producing a high GDP and jobs in flourishing economic times; they have an obligation to treat employees as more than fungible inputs and to work to serve the entire economy, not just the 1%. And, the crisis has not only inspired the everyday worker, but also economists to “question the orthodox approach to production and capital/labor relation over the last two to three decades.”[228] The time may be ripe for change. Cooperative organizations offer an alternative to both the commercial banking organizations responsible for the crisis and to the hierarchical, profit-driven firm organization Occupy Wall Street railed against.

---

[226] Michael Elsby, Bart Hobijn, and Aysegul Sahin. *The Labor Market in the Great Recession*. Working paper no. 15979. National Bureau of Economic Research, 2010.
[227] *Ibid*.
[228] Alex Bryson. "The Times Might Just Be A-Changin'" Introduction to *Advances in the Economic Analysis of Participatory and Labor-managed Firms*, edited by Jed DeVaro, Xv-Xix. Bingley: Emerald, 2012. pg. xv

Despite conventional wisdom, cooperative scarcity is not exclusively, or perhaps even primarily, the consequence of economic inefficiency. Institutional forces—coercive, mimetic, normative, or some combination of the three—function to influence firm structure. Certainly, cooperative enterprises are relatively more or less appropriate business models depending on sector and a number of other factors. But—the pronounced scarcity of cooperatives (particularly worker cooperatives) in the United States cannot simply be explained in terms of economic efficiency. While the current cooperative landscape is not thriving, the scarcity of cooperatives need not be endlessly perpetuated by the cyclically reproduced preferences for hierarchical firms evidenced in the body of this work. Indeed, perhaps the current moment offers a unique opportunity for cooperatives to gain institutional support—both governmental and non-governmental—and proliferate.

Despite the—admittedly—formidable barriers to cooperative enterprises explored throughout the preceding pages, I would like to devote the closing pages of this work to discussing the potential for cooperatives to grow in both size and scale in the United States. For, while the barriers are formidable, they are not indestructible. Both governmental and non-governmental measures can be, and in some ways already are being, pursued to create a more hospitable environment for cooperative formation and success. As discussed in the introduction, cooperatives take a number of forms, but here I will continue to focus narrowly on credit unions and worker cooperatives.

Credit Unions

As the first chapter argues, the Common Bond, lending, and financial services requirements for credit unions hinder the organizations' growth and ability to provide as accessible and convenient services as their commercial bank competitors. Because the largest cause of scarcity is situated in the policies that dictate their allowable behaviors—that is, coercive, governmental force—it is reasonable to expect that changes in policy would be instrumental to credit union expansion. While the American Bankers Association is, as discussed, a powerful source of opposition to easing restrictions on credit union, the gradual softening of the Common Bond and financial services restrictions upon credit unions gives reason for optimism about further relaxation of such restrictions. In particular, the multi-bond Common Bond interpretation and residential understandings of the Common Bond could potentially be combined to expand the potential market for credit unions and allow them to take greater advantage of economies of scale.

In 2013, bipartisan legislation was introduced in the House and the Senate that proposed to increase the member business lending cap from 12.25 percent to 27.5 percent. In March 2014, another piece of bipartisan legislation was introduced in the House to exempt certain residential loans from credit unions' statutory cap on member business loaning, which would make it possible for credit unions to lend more to small business without running up against the current cap.[229] Although neither proposal has at this date been passed, the presence of such legislation is promising for the future of credit union growth. Surely, the ABA will continue to staunchly oppose the expansion of credit union market and/or lending abilities, but the presence of such movement is encouraging. And, in the wake of the financial crisis when sentiments about commercial banking are rather negative, perhaps support for alternatives will be substantial. I focus here on potential sources of change originating in public policy because credit union scarcity is

[229] "Member Business Lending." Accessed April 18, 2014. http://www.nafcu.org/Tertiary.aspx?id=2814.

overwhelmingly the consequence of public policy. Mimetic and normative pressures do not appear to impact credit union share in the market as they do worker cooperatives, perhaps because a somewhat substantial—at least visible—credit union sector exists in the US that acts as model and maintains professional networks that offer support, while worker cooperatives are all but invisible in the economy.

Worker Cooperatives

As the second chapter argues, there are substantial coercive forces at play in the form that employee ownership takes in the United States. Specifically, the federal endorsement and preferential treatment of Employee Stock Ownership Plans (ESOPs) operates to privilege ESOPs over worker cooperatives as a means for employee ownership. Unfortunately, ESOPs less reliably capture the worker and firm benefits offered by worker cooperative and are, by and large, a messy tool for comprehensive worker ownership that involves substantial ownership and worker participation. Because most states do not maintain worker cooperative specific statutes, worker cooperatives are often complicated to organize and must be organized along formally incorporated business guidelines—i.e. an LLC, C-Corp, or S-Corp. In 1982, Massachusetts passed the Massachusetts General Law Chapter 157a, a statute specifically for Employee Cooperative Corporations. The state's law has recently served as a guide for the development of worker cooperative corporation statutes in several other states.[230] Beyond creating a ready-made legal structure for establishing a worker cooperative, such statutes ensure that worker cooperatives organize around fundamental cooperative principles, such as one worker, one vote. The introduction of a federal law modeled after the popular

[230] Those states are Connecticut, Maine, Vermont, New York, Oregon, and Washington. California recently considered a similar statute.

Massachusetts model could provide important legal endorsement and guidance for the structuring and establishment of worker cooperatives. Although the Massachusetts model offers a guide for government incorporation of worker cooperatives, it does not tackle the privileges ESOPs enjoy in the form of tax incentives. Perhaps similar advantages could be extended to worker cooperatives.

As the third chapter demonstrates, mimetic and normative forces also contribute to the scarcity of worker cooperatives in America. Historically no non-governmental support system or shelter organization for worker cooperatives has emerged and maintained a strong presence in the United States to act as a model and mentor to emerging cooperatives. However, there is interesting progress on that front taking place in the United States. In 2009, Mondragon's global expansion reached America. In Cleveland, Evergreen Cooperative Laundry (ECL) began operations "with some guidance from Mondragon and using its model."[231] Since 2009, ECL has successfully expanded to become a three-part network under the name Evergreen Cooperatives. Following the example set by Mondragon, and implementing best practices have helped the cooperative grow and will likely enable Evergreen Cooperatives to support further cooperative development.

Even more noteworthy, Mondragon, also in 2009, and the United Steelworkers union established a working relationship "whose goal is to move in the direction of building manufacturing co-ops in the United States and Canada."[232] The working relationship soon produced promising results, and in March of 2012, the United Steelworkers and Mondragon, in collaboration with the Ohio Employee Ownership

---

[231] Knoedler, Sackrey, and Schneider (2010) pg. 284
[232] *Ibid.* pg. 284

Center, engaged in an endeavor "to spread the word about worker owned co-ops and how to build them" in a publication entitled "Sustainable Jobs, Sustainable Communities: The Union Co-op Model."[233] Leo Gerard, the President of the Steelworkers, explains that "this new public domain template…offers a road-map primer for competitive and equitable employment creation based on fifty-five years of Mondragon principles put into marketplace practice."[234]

The union co-op model outlined by this collaboration strives to provide guidance "to create social and economic justice and worker dignity through the creation of good, sustainable jobs in viable, sustainable businesses that are accountable to both its workers and the communities in which they operate."[235] The model promotes the ten core Mondragon values—open admission, democratic organization, sovereignty of labor, instrumental and subordinate nature of capital, participation in management, wage solidarity, inter-cooperation, social transformation, universality, and education—as a natural corollary to union goals. The collaboration seeks to reinvigorate the spirit of labor union principles in America through a cooperative business model that has demonstrated itself to be remarkably successful and has already been successfully adapted to use within the US. Following this model, independent cooperatives may be able to successfully scale up and, in turn, support the formation of other cooperatives.

I stressed throughout the second and third chapter the interrelatedness of policy with norms and mimicry. Ultimately, the policy changes I just discussed will likely emerge only if norms change and imitation of cooperative models is contingent upon the

---

[233] *Ibid*. pg. 285
[234] *Ibid*. pg. 285
[235] Rob Witherell Chris Cooper, and Michael Peck. *Sustainable Jobs, Sustainable Communities: The Union Co-op Model*. United Steel Workers, Ohio Employee Ownership Center, and Mondragon International USA, March 26, 2012.pg. 2

presence of strong model institutions. These changes are more likely to occur if the institutional mechanisms that have prevented them in the past are shaken. I highlighted the impact of the Great Recession at the opening of this conclusion because, although far from certain, it just may have shaken the system enough to open it up to the start of some change.

In an interview in 1995, Jaroslav Vanek, one of the foremost economic scholars of worker self-management and ownership, was asked why cooperatives do not work in America to which he responded: “If you go to a bank and ask for a loan to start a co-op, they will throw you out. Co-ops in the West are a bit like sea water fish in a freshwater pond. The capitalist world in the last 200 years has evolved its own institutions, instruments, political frameworks etc. There is no guarantee that another species could function if it had to depend on the same institutions.” To a large degree this rings true. Applying DiMaggio and Powell’s formulation of sources of institutional organizational isomorphism provide an analytical lens for teasing out the types of institutions Vanek is referring. Cooperative scarcity in the United States has traditionally been, unsatisfactorily, explained by economic inefficiency arguments. And, while it is important to keep in mind the importance of sectoral and competitive differences that advantage one organizational model over another, an institutional approach supplements this understanding quite well, particularly when the empirical evidence on cooperatives comes into direct conflict with broadly applied inefficiency arguments. My hope is that this project has succeeded in providing that supplement.

Bibliography

Accessed April 25, 2014. http://www.ncua.gov/about/history/Pages/CUHistory.aspx.

Allred, Anthony T., and H. Lon Addams. "Service Quality at Banks and Credit Unions: What Do Their Customers Say?" *Managing Service Quality* 10, no. 1 (2000): 52-60. doi:10.1108/09604520010307049.

Artz, Georgeanne M., and Younjun Kim. *Business Ownership by Workers: Are Worker Cooperatives a Viable Option?* Working paper no. 11020. Iowa State University, 2011.

Blasi, Joseph R. *Employee Ownership: Revolution or Ripoff?* Cambridge, MA: Ballinger Pub., 1988.

Bryson, Alex. "The Times Might Just Be A-Changin'" Introduction to *Advances in the Economic Analysis of Participatory and Labor-managed Firms*, edited by Jed DeVaro, Xv-Xix. Bingley: Emerald, 2012.

Calomiris, Charles W., and Stephen H. Haber. *Fragile by Design: The Political Origins of Banking Crises and Scarce Credit*. Princeton: Princeton University Press, 2014.

Chaddad, Fabio. "Advancing The Theory Of The Cooperative Organization: The Cooperative As A True Hybrid." *Annals of Public and Cooperative Economics* 83, no. 4 (2012): 445-61. doi:10.1111/j.1467-8292.2012.00472.x.

Chaplinsky, Susan, and Greg Niehaus. "The Tax and Distributional Effects of Leveraged ESOPs." *Financial Management* 19, no. 1 (1990): 29. doi:10.2307/3666034.

"CICOPA." What Is a Cooperative? -. Accessed February 21, 2014. http://www.cicopa.coop/What-is-a-cooperative.html#workers.

Conte, Michael A. "Entry of Worker Cooperatives in Capitalist Economies." *Journal of Comparative Economics* 10, no. 1 (1986): 41-47. doi:10.1016/0147-5967(86)90117-4.

"Cooperatives Around the World." Home. Accessed January 25, 2014. http://usa2012.coop/about-co-ops/cooperatives-around-world.

Corcoran, Hazel, and David Wilson. *The Worker Co-operative Movements in Italy, Mondragon and France: Context, Success Factors and Lessons*. Issue brief. 2010.

Craig, Ben, and John Pencavel. "The Objectives of Worker Cooperatives." *Journal of Comparative Economics* 17, no. 2 (1993): 288-308. doi:10.1006/jcec.1993.1027.

Cuevas, Carlos E., and Klaus Peter Fischer. *Cooperative Financial Institutions: Issues in Governance, Regulation, and Supervision*. Washington, D.C.: World Bank, 2006.

Curl, John. *For All the People: Uncovering the Hidden History of Cooperation, Cooperative Movements, and Communalism in America*. Oakland, CA: PM Press, 2009.

Dickstein, Carla. "The Roles of Support Organizations in Worker Cooperative Systems: A Comparative Case Study." PhD diss., University Microfilms International, 1986.

Dimaggio, Paul J., and Walter W. Powell. "The Iron Cage Revisited: Institutional Isomorphism and Collective Rationality in Organizational Fields." *American Sociological Review* 48, no. 2 (1983): 147. doi:10.2307/2095101.

Elsby, Michael, Bart Hobijn, and Aysegul Sahin. *The Labor Market in the Great Recession*. Working paper no. 15979. National Bureau of Economic Research, 2010.

Elster, Jon. "From Here to There; Or, If Cooperative Ownership Is So Desirable, Why Are There So Few Cooperatives?" *Social Philosophy and Policy* 6, no. 02 (1989): 93. doi:10.1017/S0265052500000650.

Emmons, William R. and Frank A. Schmid, “Credit Unions and the Common Bond,” Federal Reserve Bank of St. Louis *Review* 1999.

Estrin, Saul and Derek C. Jones, “Viability of Emplyee-Owned Firms: Evidence from France, The,” *Industrial and Labor Relations Review* 45 (1992 1991): 323.

Fountain, Wendell V. *The Credit Union World: Theory, Process, Practice--: Cases & Application*. Bloomington, IN: AuthorHouse, 2007. Kindle.

Freeman, Steven F. *Effects of ESOP Adoption and Employee Ownership: Thirty Years of Research and Experience*. Working paper no. 07-01. University of Pennsylvania, 2007.

Goddard, John A., Donal G. Mckillop, and John O.s Wilson. "The Growth of US Credit Unions." *Journal of Banking & Finance* 26, no. 12 (2002): 2327-356. doi:10.1016/S0378-4266(01)00203-5.

Hansmann, Henry. *The Ownership of Enterprise*. Cambridge, MA: Belknap Press of Harvard University Press, 1996.

Hesse, Heiko and Martin Cihak. *Cooperative Banks and Financial Stability*, IMF Working Paper (International Monetary Fund, 2007), http://ideas.repec.org/p/imf/imfwpa/07-2.html.

In Good Company: A Guide to Cooperative Employee Ownership. Technical paper. 2006. Accessed 2013. www.ncdf.coop/documents/worker_coop_toolbox.pdf.

Kalmi, Panu. "The Disappearance of Cooperatives from Economics Textbooks." *Cambridge Journal of Economics*, 2007, 625-47.

Klinedinst, Mark. "Going Forward Financially: Credit Unions as an Alternative to Commercial Banks." In *Advances in the Economic Analysis of Participatory and Labor-managed Firms*, edited by Jed DeVaro, 3-23. Bingley: Emerald, 2012.

Kruse, Douglas L., Joseph Blasi, and Margaret M. Blair. "Employee Ownership: An Unstable Form or a Stabilizing Force?" In *The New Relationship: Human Capital in the American Corporation*, edited by Margaret M. Blair and T. Kochan, 241-98. Washington, D.C.: Brookings Institution Press, 2000.

Kruse, Douglas, Richard B. Freeman, and Joseph R. Blasi. *Shared Capitalism at Work: Employee Ownership, Profit and Gain Sharing, and Broad-based Stock Options*. Chicago: University of Chicago Press, 2010.

Lee, Jinkook et al., “Consumer Use of Banks and Credit Unions,” Product Page, 2009, http://www.rand.org/pubs/technical_reports/TR672.html.

Levin, Henry M., and Zelda F. Gamson. "Obstacles to the Survival of Democratic Workplaces." In *Worker Cooperatives in America*, edited by Robert Jackall and Henry M. Levin, 219-44. Berkeley: University of California Press, 1984.

Levin, Henry M. "ESOPs and the Financing of Worker Cooperatives." In *Worker Cooperatives in America*, edited by Robert Jackall and Henry M. Levin. Berkeley: University of California Press, 1984.

"Management Education and Development. Co-operatives and Credit Unions in Economics and Business Texts: Changing the Paradigm." *INTERNATIONAL JOURNAL OF CO-OPERATIVE MANAGEMENT*, 2004.

Martin, Andrew, and Ron Lieber. "Alternative to Banks, Now Playing Offense." The New York Times. June 11, 2010. Accessed April 25, 2014. http://www.nytimes.com/2010/06/12/business/12credit.html?pagewanted=all.

McKelly, Michael. *The Secret War on America's Credit Unions*. 2012.

Mckillop, Donal, and John O.s. Wilson. "Credit Unions: A Theoretical and Empirical Overview." *Financial Markets, Institutions & Instruments* 20, no. 3 (2011): 79-123. doi:10.1111/j.1468-0416.2011.00166.x.

"Member Business Lending." Accessed April 18, 2014. http://www.nafcu.org/Tertiary.aspx?id=2814.

Murphy, Michael E. "The ESOP at Thirty: A Democratic Perspective." *Willamette Law Review*, 2005, 655-706.

Park, Rhokeun, Douglas Kruse, and James Sesil, "DOES EMPLOYEE OWNERSHIP ENHANCE FIRM SURVIVAL?," *Advances in the Economic Analysis of Participatory & Labor-Managed Firms* 8 (July 6, 2004): 3–33, doi:10.1016/S0885-3339(04)08001-9.

Podivinsky, Jan M., and Geoff Stuart. "On the Choice Between Capitalist and Labour-Managed Production: Evidence from a Panel of Entrant into UK Manufacturing Industries." In *Advances in the Economic Analysis of Participatory and Labor-managed Firms*, edited by Jed DeVaro. Bingley: Emerald, 2012.

Pozdena, Randell, and Michael Wilkerson. *Credit Unions vs. Banks: The Myth of the Uneven Playing Field*. Issue brief. Portland: ECONORTHWEST, 2013.

Pérotin, Virginie. "Entry, Exit, and the Business Cycle: Are Cooperatives Different?" *Journal of Comparative Economics* 34, no. 2 (2006): 295-316. doi:10.1016/j.jce.2006.03.002.

Research Evidence on Prevalence and Effects of Employee Ownership (2013) (testimony of Douglas Kruse).

"Retirement Plans, Benefits & Savings." U.S. Department of Labor. Accessed April 5, 2014. http://www.dol.gov/dol/topic/retirement/typesofplans.htm.

Sackrey, Charles, Geoffrey Eugene. Schneider, and Janet T. Knoedler. *Introduction to Political Economy*. 6th ed. Cambridge, MA: Dollars and Sense, Economic Affairs Bureau, 2010.

Vanek, Jaroslav. *The General Theory of Labor-managed Market Economies*. Ithaca: Cornell University Press, 1970.

Walter, John. *Not Your Father's Credit Union*, SSRN Scholarly Paper (Rochester, NY: Social Science Research Network, 2006), http://papers.ssrn.com/abstract=2186135.

"What Is a Worker Cooperative?" US Federation of Worker Cooperatives. Accessed November 7, 2013. http://www.usworker.coop/about/what-is-a-worker-coop.

"What's a Co-op?" ICA: International Co-operative Alliance. Accessed February 21, 2014. http://ica.coop/en/whats-co-op.

Wheelock, David C., and Paul W. Wilson. "Are Credit Unions Too Small?" *Review of Economics and Statistics* 93, no. 4 (2011): 1343-359. doi:10.1162/REST_a_00121.

Wilcox, James A. “Performance Divergence of Large and Small Credit Unions,” *FRBSF Economic Letter*, 2006, http://ideas.repec.org/a/fip/fedfel/y2006iaug4n2006-19.html.

Witherell, Rob, Chris Cooper, and Michael Peck. *Sustainable Jobs, Sustainable Communities: The Union Co-op Model*. United Steel Workers, Ohio Employee Ownership Center, and Mondragon International USA, March 26, 2012.

Worthington, Andrew C. "Determinants of Merger and Acquisition Activity in Australian Cooperative Deposit-taking Institutions." *Journal of Business Research* 57, no. 1 (2004): 47-57. doi:10.1016/S0148-2963(02)00283-7.