International Cooperative Governance and Market Trends

A Credit Union Research Symposium at the University of Toronto

Executive Summary by Ben Rogers
Research Director
Filene Research Institute
Deeply embedded in the credit union tradition is an ongoing search for better ways to understand and serve credit union members. Open inquiry, the free flow of ideas, and debate are essential parts of the true democratic process.

The Filene Research Institute is a 501(c)(3) not-for-profit research organization dedicated to scientific and thoughtful analysis about issues affecting the future of consumer finance. Through independent research and innovation programs the Institute examines issues vital to the future of credit unions.

Ideas grow through thoughtful and scientific analysis of top-priority consumer, public policy, and credit union competitive issues. Researchers are given considerable latitude in their exploration and studies of these high-priority issues.

The Institute is governed by an Administrative Board made up of the credit union industry’s top leaders. Research topics and priorities are set by the Research Council, a select group of credit union CEOs, and the Filene Research Fellows, a blue ribbon panel of academic experts. Innovation programs are developed in part by Filene i3, an assembly of credit union executives screened for entrepreneurial competencies.

The name of the Institute honors Edward A. Filene, the “father of the US credit union movement.” Filene was an innovative leader who relied on insightful research and analysis when encouraging credit union development.

Since its founding in 1989, the Institute has worked with over one hundred academic institutions and published hundreds of research studies. The entire research library is available online at www.filene.org.
Credit Union Central of Canada (Canadian Central) is the national trade association for the Canadian credit union system. Incorporated in 1953 by a special act of Parliament, and regulated under the Cooperative Credit Associations Act (Canada), Canadian Central provides a National Forum, a National Voice and National Services to support and expand the Canadian credit union system. In support of these national initiatives, and to facilitate knowledge transfer, members from provincial/regional Centrals and individual credit unions work on committees to further the aims of the Canadian credit union system. These committees encompass Finance, Legislative Affairs, Risk Management, Payments and Lending.

Canadian Central offices in Toronto and Ottawa employ 50 staff members who support trade association services, financial management and payments-related services. The Toronto office is also home to CUSOURCE Credit Union Knowledge Network, the national learning and management facility for the credit union system. The Ottawa team is focused on increasing its policy and advocacy activities and influence in the area of Federal Government relations. Canadian Central’s Mission and Vision guide the organization and enable the Canadian credit union system to compete, excel and achieve.
This symposium was possible because of the fruitful collaboration between the Filene Research Institute and Credit Union Central of Canada. We would like to thank, for their vision and support, David Phillips, Brigitte Gouillard, and Marc-André Pigeon. And for their unflagging efforts in organizing the day’s events, we thank Veronica Feldcamp and Anna Morena from Credit Union Central of Canada and Monica Titley from Filene.

We would like to thank all our speakers for their attendance and their contributions to the important work of sharing cooperative insights. Cooperation among cooperatives is a guiding principle, and the worldwide movement is well served through exchanges like this.

And finally, we would like to acknowledge Vicky Franchino for her intelligence and precision in helping to compile this report.
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One of the international cooperative principles calls for cooperation among cooperatives. But we credit unions don’t always do a good job of practicing what we preach—for example, taking advantage of the combined knowledge and experience of our cooperative brethren. For every challenge that an individual credit union has faced, the odds are good to excellent that another credit union or cooperative bank has faced, and overcome, something similar.

With this in mind, the Filene Research Institute and Credit Union Central of Canada brought together experts from the United States, Canada, and “across the pond” to share their experiences with a host of challenging issues, like consolidation, governance, and efficiency—issues that many of us have faced in the tumult of recent years.

What Was the Symposium About?

Our discussions covered the changing face of credit union governance, the threat of demutualization, and the importance of integrity in credit union efforts to differentiate in a crowded marketplace. We also looked at a new cooperative paradigm that recognizes the powerful role loyalty plays in building long-term relationships, and we reached out to an expert in the field of behavioral economics to better understand something we see every day: consumers acting in not quite rational ways. With an eye toward regulation, we also re-examined the ever-popular “level playing field” in favor of a better sports metaphor: competitive balance.

A theme quickly surfaced: What we do must reflect a sincere effort to improve the well-being of our members. This means that we must have, as one presenter put it, “humility and sensitivity with respect to moments of truth,” and we must recognize that the best credit unions aren’t afraid to ask each other for help.

What Are the Credit Union Implications?

Building societies are cooperative organizations that strongly resemble the old US savings and loan model: They take in retail savings and make mortgage loans, says Andrew Gall, an economist at the Building Societies Association in the United Kingdom. From the 1980s through roughly 2000, building societies faced a rash of demutualizations, and, to a one, these demutualized entities either had to be taken over by a larger bank or were partly or completely nationalized during the financial crisis. The building societies that
remained mutuals have largely become stronger, more stable institutions and have been recognized by both the British government and the Independent Commission on Banking as role models for the financial services industry.

The UK isn’t the only nation to appreciate the value of the cooperative difference. In the Netherlands, Rabobank is a huge mutual (€665 billion) that’s been in existence for more than 100 years. Hans Groeneveld, senior vice president of strategic, governance, and organizational issues at Rabobank Nederland, discussed Rabobank’s federated structure, unique cooperative financial instruments, opportunities and challenges for the cooperative model, and how its inherent strengths, such as ethics and member engagement, are now being embraced by the banking industry.

Dilip Soman, Corus chair in communication strategy and professor of marketing at the Rotman School of Management at the University of Toronto, offered a guided tour of consumer thinking. If you’ve ever had a product or service failure, you’ve undoubtedly spent some long hours wondering why. What you might not have taken into account is that the average consumer doesn’t always act in a way that makes economic sense. This presentation on behavioral economics charted the decision-making process and suggested how to influence it.

This was the first airing for Donal McKillop’s research on credit union progression and governance in the United States and Canada. McKillop, a professor at Queen’s University of Belfast, is currently wrapping up a research project commissioned by Filene and Credit Union Central of Canada. The study delivered both governance trends and suggestions gleaned from interviews conducted throughout the research.

Does the traditional cooperative paradigm work in today’s world? Or is it time to look at the credit union difference in a slightly different way? Daniel Côté, a professor at HEC in Montreal and a Filene Research Fellow, showed how loyalty is the modern manifestation of the cooperative spirit and how this cooperative staple can create a stronger future for our industry.

Our final presentation threw water on the tempting argument that credit unions should aspire to a level playing field with other financial service providers. Rather than embrace a model that tends to penalize smaller players with burdensome regulation, Ben Rogers from Filene and Marc-André Pigeon, director of financial sector policy at Credit Union Central of Canada, showed us why competitive balance is actually a better goal.
Andrew Gall

Andrew Gall is an economist at the Building Societies Association, the trade body for building societies in the UK. In this role he provides economic analysis to support the association’s policy positions and also manages their research program. Andrew is currently overseeing the implementation of proposals made by the Independent Commission on Banking to promote financial security in the UK banking environment. He is also developing an index to measure diversity of financial service providers and is overseeing a research project designed to help mutuals more effectively differentiate themselves from their competitors.

Hans Groeneveld

Hans Groeneveld is senior vice president of strategic, governance, and organizational issues at Rabobank Nederland. He manages strategic projects and serves as an advisor to the organization’s executive board, and he previously held a variety of senior and managerial positions with the firm. Before joining Rabobank Group, Hans worked at the Dutch Central Bank in the monetary and supervisory departments. He is a board member of the Royal Society of Economic Affairs and a member of the Think Tank of the European Association of Cooperative Banks.

Dilip Soman

Dilip Soman is the Corus chair in communication strategy, a professor of marketing, and a Senior Fellow at Desautels Centre for Integrative Thinking at the Rotman School of Management at the University of Toronto. His background includes undergraduate work in engineering followed by an MBA with doctoral work in marketing and behavioral economics. Dilip has written dozens of articles across a wide spectrum of marketing topics and is the author of the book Managing Customer Value (World Scientific Publishing Company, 2009).
Donal McKillop

Donal McKillop is a professor of financial services at Queen’s University of Belfast, where he is program director for the undergraduate finance degree and the postgraduate degree in risk management and financial regulation. Donal’s research focus is in the areas of financial institutions and market and financial regulation; he has conducted research studies and published extensively in both areas. In addition to his academic role, Donal is a member of the research committee of the European Association of Cooperative Banks, advisor to the Irish minister of finance on credit union policy, and chair of the Irish Commission on Credit Unions.

Daniel Côté

Daniel Côté is an associate professor at HEC in Montreal. He has conducted research on cooperatives for more than a quarter-century, with a focus on agribusiness and finance and a commitment to helping cooperatives find more effective ways to compete. Daniel takes an action-based approach to research and has tested his hypothesis of the “new cooperative paradigm” with several existing cooperatives. He has published extensively on the subjects of loyalty, mobilization through values, the learning organization, and meaning and legitimacy.

Ben Rogers

Ben Rogers is research director at the Filene Research Institute. He manages and edits a large pipeline of economic, market, and policy research related to the consumer finance industry, always with an eye toward providing content that is useful and actionable. Ben has authored nearly 20 Filene reports, including much of the institute’s young-adult research. He also served as director of Filene’s CU Tomorrow projects and was previously editor of The CEO Report and chairman of the National Directors’ Convention. Ben has been cited in numerous publications including the Wall Street Journal, American Banker, the Credit Union Times, and Credit Union Journal.
Marc-André Pigeon

Marc-André Pigeon is the director of financial sector policy at Credit Union Central of Canada, where he is responsible for monitoring, researching, and advocating for credit unions on a range of issues. Prior to joining Credit Union Central of Canada, Marc-André worked as lead analyst for the Senate Banking Committee and the House of Commons Finance Committee, as a project leader at the Department of Finance, as an economics researcher with the Levy Economics Institute in New York state, and as a business reporter for Bloomberg Business News in Toronto.
The UK’s building societies have had their share of challenges over the past two decades, but with a new focus on the cooperative difference, they’re poised to regain lost market share. Andrew Gall, an economist with the Building Societies Association, shares key insights from the group’s recent past.
Building societies are similar to the former US savings and loan model—they take in retail savings and use those funds to make mortgage loans, and they have traditionally operated as cooperatives. In the UK the sector is quite large, with assets of roughly $500 billion, or about 20% of the UK’s household savings and mortgage market. There are currently 47 building societies in the UK with nearly 40,000 employees, 1,700 branches, and a huge range of sizes.

Industry-specific legislation governs the societies, and each must meet a number of set requirements:

- 50% of a society’s funds must be from retail savings—in practice the level is roughly 75%.
- 75% of the lending must be on residential property—this is typically closer to 90%.
- Few constraints on powers.
- Owned by their members.
- Can be converted to a public company or another type of mutual with member approval.

The Impact of Demutualization

In the 1980s and into the 1990s, a number of building societies decided to take advantage of the last requirement. While the most common reason given for doing so was the desire to raise additional capital, the reality was quite different. Recognizing that members could compel a society to convert to a public company and release profits to its owners, there was a rash of “carpetbagging”: people joining mutuals simply to force them to convert and cash out.

This epidemic ended around 2000 when building societies made new members sign an agreement acknowledging that if the society did convert, all windfall payouts would go to charity. It’s unlikely to happen again because demutualization proved to be a path to destruction. Of all the societies that converted, not one remains
They have either been taken over by large banks or were partly or fully nationalized during the financial crisis.

One of the UK’s national newspapers summed it up nicely:

The conversion of many of the building societies from mutual to shareholder ownership has been a catastrophe. Not one building society that converted remains an independent entity. They have either been taken over or gone bust. Those that remained mutuals have continued more or less successful, with the weaker ones taken over successfully and the biggest, the Nationwide, coming through the down-turn in good shape.¹

First, the Bad News

This isn’t to say that building societies came through the financial crisis unscathed. Some ran into trouble from 2007 to 2011, especially larger ones that lost sight of their mandate and tried to emulate the big banks. But, for the most part, the industry was able to support itself throughout this crisis with limited infusions of government funds.

Where does this leave building societies today?

On the plus side, a drop in bank rates to 0.5% helped borrowers stay in their homes and service their loans. There were unsurprising parallels between foreclosures and rising unemployment, but overall there were fewer forced sales than originally predicted. But this drop in rates has also hurt building societies’ profitability.

We’ve seen a huge drop in business volume. Gross residential mortgage lending is roughly half what it was in 2007, and the numbers for net lending are even worse—almost 90% lower. Out of

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**Figure 1: Demutualization: Where Are They Now?**

<table>
<thead>
<tr>
<th>Building society</th>
<th>Year of demutualization</th>
<th>Outcome</th>
<th>Year of outcome</th>
</tr>
</thead>
<tbody>
<tr>
<td>Abbey National</td>
<td>1989</td>
<td>Taken over</td>
<td>2004</td>
</tr>
<tr>
<td>C&amp;G</td>
<td>1995</td>
<td>Taken over</td>
<td>1995</td>
</tr>
<tr>
<td>N&amp;P</td>
<td>1996</td>
<td>Taken over</td>
<td>1996</td>
</tr>
<tr>
<td>Alliance &amp; Leicester</td>
<td>1997</td>
<td>Taken over</td>
<td>2008</td>
</tr>
<tr>
<td>Halifax</td>
<td>1997</td>
<td>Taken over, part nationalized</td>
<td>2008</td>
</tr>
<tr>
<td>Northern Rock</td>
<td>1997</td>
<td>Nationalized</td>
<td>2008</td>
</tr>
<tr>
<td>Bristol &amp; West</td>
<td>1997</td>
<td>Taken over</td>
<td>1997</td>
</tr>
<tr>
<td>Woolwich</td>
<td>1997</td>
<td>Taken over</td>
<td>1999</td>
</tr>
<tr>
<td>Birmingham Midshires</td>
<td>1998</td>
<td>Taken over</td>
<td>1999</td>
</tr>
<tr>
<td>Bradford &amp; Bingley</td>
<td>2000</td>
<td>Taken over, part nationalized</td>
<td>2008</td>
</tr>
</tbody>
</table>

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**Figure 2: Building Society Consolidation**

- Slow rate of strategic mergers before crisis
- Specific problems at certain societies, often can be traced back to failings of governance
- Sector supported itself—stronger societies remain
- Little direct support from the UK government

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¹ The conversion of many of the building societies from mutual to shareholder ownership has been a catastrophe. Not one building society that converted remains an independent entity. They have either been taken over or gone bust. Those that remained mutuals have continued more or less successful, with the weaker ones taken over successfully and the biggest, the Nationwide, coming through the down-turn in good shape.
a stock of about £1.2 trillion in UK mortgage loans, building societies held about £210 billion at the end of June 2011.

In tandem with these drops in purchases, we’ve also seen drops in savings. Before the crisis, we had about £70 billion in new deposits across all providers and now we’re at £25 billion. This is the result of multiple forces: the squeeze on household income, inflation, and the fact that low interest rates make it difficult to attract savings.

Figure 4 shows some even more revealing figures for the sector as a whole.

Let’s start with net interest income. As Figure 4 shows, societies have been steadily squeezing their net interest income in an effort to compete with banks. The most common way we’ve done this is through

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**Figure 3: Residential Foreclosures**

Note: f = forecast.

Source: Council of Mortgage Lenders.

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**Figure 4: Building Society Income and Expenditures (percent of mean assets)**

<table>
<thead>
<tr>
<th>Year</th>
<th>Net interest income</th>
<th>Other income</th>
<th>Provisions and losses</th>
<th>Management expenses</th>
<th>Retained surplus</th>
</tr>
</thead>
<tbody>
<tr>
<td>2000</td>
<td>1.45</td>
<td>0.42</td>
<td>0.00</td>
<td>−1.17</td>
<td>0.48</td>
</tr>
<tr>
<td>2001</td>
<td>1.42</td>
<td>0.34</td>
<td>0.00</td>
<td>−1.06</td>
<td>0.50</td>
</tr>
<tr>
<td>2002</td>
<td>1.26</td>
<td>0.40</td>
<td>−0.08</td>
<td>−1.04</td>
<td>0.39</td>
</tr>
<tr>
<td>2003</td>
<td>1.24</td>
<td>0.37</td>
<td>−0.09</td>
<td>−1.04</td>
<td>0.34</td>
</tr>
<tr>
<td>2004</td>
<td>1.13</td>
<td>0.43</td>
<td>−0.05</td>
<td>−1.02</td>
<td>0.36</td>
</tr>
<tr>
<td>2005</td>
<td>1.09</td>
<td>0.40</td>
<td>−0.08</td>
<td>−0.94</td>
<td>0.33</td>
</tr>
<tr>
<td>2006</td>
<td>1.04</td>
<td>0.46</td>
<td>−0.08</td>
<td>−0.94</td>
<td>0.33</td>
</tr>
<tr>
<td>2007</td>
<td>1.03</td>
<td>0.42</td>
<td>−0.08</td>
<td>−0.91</td>
<td>0.33</td>
</tr>
<tr>
<td>2008</td>
<td>0.99</td>
<td>0.32</td>
<td>−0.21</td>
<td>−0.88</td>
<td>0.16</td>
</tr>
<tr>
<td>2009</td>
<td>0.83</td>
<td>0.34</td>
<td>−0.31</td>
<td>−0.76</td>
<td>0.08</td>
</tr>
<tr>
<td>2010</td>
<td>0.85</td>
<td>0.33</td>
<td>−0.23</td>
<td>−0.75</td>
<td>0.15</td>
</tr>
</tbody>
</table>

Source: Financial Services Authority/Building Societies Association.
lower interest rates. By 2009, when the Bank of England cut interest rates dramatically, we were down to $0.83 of interest income for every $100 of assets.

Not surprisingly, other income—which we get from selling products related to mortgages, such as insurance and connected fees—also took a hit. Our provisions and losses stats reflect both loan losses and the cost of supporting the deposit insurance funds for failed banks, and these are roughly unchanged for 2011. One bright spot is management expenses: Over the last decade, building societies have made a concerted effort to cut their administrative costs, and that’s reflected here.

You may notice that taxes aren’t listed; that’s simply because this is an area that societies have very little control over. As shown in the last column, retained surplus has been hit severely due to competitive pressures before the crisis and the squeeze on margins and volumes and increased losses since.

**Regulations Are a Growing Burden**

Building societies are dealing with industry-specific issues as well as broad changes in general regulation—including new capital and liquidity requirements, new expansion guidelines, and more intense conduct-of-business regulation that’s hitting industries across the board. Our regulator, the Financial Services Authority (FSA), has been split in two and we now work with a prudential regulator and a conduct-of-business regulator.

The Independent Commission on Banking has made recommendations about splitting retail arms and subsidiaries, and we’re also faced with regulation coming from Europe and from international regulators such as Basel and the Financial Stability Board. Many of the capital instruments that we’ve relied on in the past will no longer count, and that will have a huge impact on us.

And, of course, in the past few years we’ve had to compete against banks that were partially or completely nationalized and were able to gain market share due to the veneer of stability this support provided. As the emergency measures of 2008–2009 wind down, we anticipate that this temporary advantage will disappear.

**The Picture Starts to Brighten**

Although the current picture might seem pretty gloomy, building societies have actually shown themselves to be quite resilient.

One critical area of difference between failed institutions and ourselves was our commitment to strategy. Not only did we have a
clear strategy, but we stayed focused and followed through. There’s no conclusive link between size and success and no one path to effective implementation: Some societies focused on high-quality, low-risk assets, while others took on more risk but priced it accordingly.

Other society strengths throughout the crisis have included good risk management, a commitment to member service, and strategic mergers. The sector has also benefited from the fact that we’re committed to working together. We have societies that are sharing costs on procurement and working together to create funding instruments and securities that they couldn’t issue on their own.

The sector has seen a decreased reliance on wholesale funding. Regulatory pressure and market reaction have driven this change to a large extent, along with the recognition that those societies that didn’t depend on this funding came through the crisis a lot more easily.

In the past few years, we’ve also gained a better understanding of the importance of good governance, including just how critical excellent boards are. Societies recognize that it’s vital to review their boards and are actively looking for assistance in this area.

Lastly, in order to be successful, societies need to develop some type of external capital instrument. We need to be prudent and conservative, but we also recognize that it’s necessary to have ways to raise capital quickly if market conditions or regulatory requirements change.

Staying Relevant in the Marketplace

Now that we’ve taken a look at our recent past and captured some of the critical ways that building societies have risen to the challenges of the marketplace, let’s focus on how mutual organizations can reassert their relevance in the financial services marketplace.

One topic that came up frequently throughout the financial crisis is that the general public does not trust banks. Once consumers understand how mutuals work, they have a strong affinity for them. We have consistent survey evidence showing that mutuals generate high levels of customer satisfaction and we also have strong third-party endorsements:

### Figure 5: Customer Satisfaction

<table>
<thead>
<tr>
<th></th>
<th>Mutuals</th>
<th>All other providers</th>
</tr>
</thead>
<tbody>
<tr>
<td>Savings satisfaction</td>
<td>+12%</td>
<td>59%</td>
</tr>
<tr>
<td>Mortgage satisfaction</td>
<td>+7%</td>
<td>70%</td>
</tr>
</tbody>
</table>

• UK Coalition Programme for Government: “We will bring forward detailed proposals to foster diversity in financial services, promote mutuals and create a more competitive banking industry.”

• Independent Commission on Banking: “The precedent in building society legislation appears to provide a particularly good basis for the risk management functions of ring-fenced banks. Building society regulations have operated effectively for a long time.”

Creating a Vision for the Future
Given this high regard for mutuals, we’ve come up with a bold vision for the sector: to be the financial service provider most trusted and valued by savers and homebuyers.

It’s a tall order, but here’s how we can accomplish it.

Return Value to Our Members
We must clearly communicate the mutual difference to members through:

• Better interest rates.
• Better service.
• More convenient branch access, especially in underserved areas.
• Community support—learn what is valued by a specific community and deliver accordingly.

Create Sustainable Businesses
Each society must work to explain how their efforts benefit members and help to ensure the long-term survival of the business:

• Build on the long-term nature of the society model.
• Balance capital maintenance and profitability to ensure survival.
• Focus on continual process improvement—actively promote organizational transparency and solicit member feedback.

Effective Member Governance
• Ensure member engagement strategy fits.
• Allow members to appoint the board of directors—use board effectiveness reviews to ensure effectiveness.

Cooperation
• Work together to achieve scale.
• Explore alternative mutual structures.
Delivering Results to Members
Through ongoing conversations with our members, we have come to see that they are looking for the following from us.

Provide Support for Aspiring Homebuyers
We want to create innovative products that support members’ dreams, especially those of first-time homeowners. Two recent products are shared equity loans and high loan-to-value loans. We’re obviously doing something right, as mutuals’ gross lending grew by 16% last year, while it was down 1% across the rest of the market.

Develop a Culture of Savings
This is another area where innovation is key. Mutuals are currently offering a number of products that banks aren’t—such as products for children—and we’re also working in the schools to improve financial literacy. Through these efforts, among others, we’re helping to create a more stable financial future.

Empower Consumer Control Through Trust and Transparency
After the past few years, we believe consumers have a strong interest in products they can control themselves and that they can trust to deliver as promised. We’re delivering in two ways: by creating innovative products and by providing competition to the for-profit banking model.

Support a Diverse Financial System
Lastly, because we operate using different incentives and a different business model, any future shocks will affect us in a different way than they affect the banks, thus adding to the overall stability of the financial system.

Our sector has remained strong throughout the financial crisis. Although huge challenges remain, if we’re able to communicate the value of our model and build on our long-term member relationships, we believe we can build that into a competitive advantage.
The financial crisis provided a good opportunity for cooperative financial institutions to prove the value of their time-honored differentiators: a moderate tolerance for risk, commitment to relationships, and a long-term outlook. Hans Groeneveld, senior vice president of strategic, governance, and organizational issues at Rabobank Nederland—one of Europe’s most stable and respected financial institutions—shows that cooperatives are an important alternative to the commercial banking model.
Since cooperative banks weathered the financial upheaval of the past decade better than our commercial rivals, governments and financiers have shown an increased desire to understand our model and mimic our strengths.

But effectively communicating our differences and our value can be tricky. Governance issues are complex—regulators outside of the industry don’t always “get” what makes us successful—and there aren’t always good data to support the worth of the cooperative model.

Figure 6: Losses and Writedowns of European Banks during the Great Recession

European cooperative banks, with 20% market share, were responsible for 8% of the losses and writedowns. These losses were principally from nontraditional products, typically abroad.

Source: Calculations by Rabobank based on press releases and Bloomberg.
Long-Term Impact of the Financial Crisis

As for-profit financial institutions are forced to adopt more prudent regulations, we are likely to face increased competition and a tougher market environment. Not only will banks be returning to our turf—local customers and retail banking will replace international markets and exotic financial products—but we’ll have to face additional supervision and regulation that are largely driven by problems in the shareholder model institutions. Policies will focus on the stability of the financial system and we’ll see a focus on external effects that could damage the financial industry.

Cooperatives—A Different Way to Bank

Before we delve into some of the benefits of our system, let’s define what we mean by “cooperative banking.” First, the banking part. As part of the financial system we have to be efficient, proficient, and competitive. We have to make profits as a necessary component of survival, but unlike other banks, that’s not our end goal. We have to do an effective job of offering desired products at fair prices; otherwise there’s no reason for a consumer to become a member.

Then there’s the cooperative aspect. What makes us different is our cooperative governance. We have members and each one gets a vote, a say in our operations. This doesn’t guarantee that we’ll do a better job than other banks, but it is a chance to operate in another way.

Proof That Cooperatives Are Effective

Although it isn’t always easy to show the value of cooperatives, there are some observable manifestations.
One is customer satisfaction. Surveys show that our members are happy with us, and continued growth in our market share is proof. Since 1997, there has been steady membership growth in the six European countries (the EU6) where cooperative banks have at least 25% of the market: Austria, Finland, France, Germany, Italy, and the Netherlands (see Figure 9). Notice that there’s a jump in the middle of the crisis: It might not look like much, but it represents millions of people.

Deposit and loan amounts for cooperatives in the EU6 have also gone up—again, recognize that even a 0.001 increase in market share is equivalent to billions of euros.

The fact that we continue to maintain very dense branch networks means that we are, literally, closer to our clients than other banks. This allows us to build meaningful, long-term relationships.

On the financial side, there’s a lot of evidence to prove our industry’s stability. Cooperatives didn’t need government support in the middle of the crisis, and we’ve been able to show increases in efficiency. We also have a very high-quality capital base—so high that even in the midst of the financial crisis, most cooperatives were able to continue to fund loans while other banks were not. In 2009, cooperatives
were able to grow their loan portfolios by more than 3%, while other banks decreased theirs.

Cooperatives in the EU6 have had Tier 1 ratios that equaled, or exceeded, those of banks. But Figure 11 only tells part of the story: We were able to achieve these numbers with far fewer losses than commercial banks.

Return on equity (ROE) levels did drop at both cooperatives and all other banks, but the drop was lower in cooperatives.

Our z-score also indicates our revenue stability, as evidenced by our revenue stream.
Figure 11: Financial Performance: Tier 1 Ratios, 2002–2010

![Average Tier 1 ratio for Cooperative banks and Entire banking system across EU6 countries from 2002 to 2010.]

Figure 12: Financial Performance: ROE

![Graph showing ROE (return on equity) for Cooperative banks (EU6) and Entire banking system from 2002 to 2010.]

Figure 13: Cooperative Banks and Financial Stability (Z-Score)

![Graph showing Z-score for Cooperative banks and Entire banking sector across EU6 countries from 2002 to 2010.]

Note: Z-score = \((\text{equity/assets} + \text{return on assets})/\text{variance of (return on assets)}\)
A Closer Look at Rabobank

Now that we have a good overview of European cooperatives, let’s focus on one in particular: Rabobank.

Rabobank has been around since 1896. One of the most critical reasons for our long-term success is the underlying Dutch culture. Given our physical location, we have historically had to work together to fight a strong and dangerous enemy: the sea. This has made us extremely effective at creating centralized support organizations, and cooperatives have benefited greatly from these.

There are a few milestones in the history of our organization that have also been critical to our success. One was the decision in 1953 to delegate the supervision of all local independent cooperatives—the Rabobanks—to Rabobank Nederland, our central institution. The Central Bank oversees our Rabobank Nederland, but it isn’t responsible for overseeing the individual banks.

To ensure that Rabo Nederland doesn’t wield too much power, we’ve created a governance system with some built-in checks and balances (see Figure 14).

The Rabobanks have 1.8 million members at 139 independent local banks. Each of these banks sends a delegate to a central delegates assembly, and it’s here that we make decisions affecting the entire organization. One interesting thing about our assembly is that two-thirds of the representatives are members of the cooperatives; this ensures that members are heard at the very highest level. These representatives elect the supervisory boards within Rabo Nederland—so

Figure 14: 139 Parents and One Daughter
while Rabo Nederland is supervising the Rabobanks, the Rabobanks are also supervising Rabo Nederland.

Other highlights from Rabobank history include the merger of the two central institutions in 1972 and the creation of a cross-guarantee system in 1980. This system helps cooperatives in two ways: (1) it protects the stability of each location by stepping in if a branch gets into trouble, and (2) if a branch wants to grow but doesn’t have the capital to do so, this system helps provide access to affordable funds.

Because of the cross-guarantee system, none of our banks failed during the financial crisis and we have a high credit rating. During this time we also eliminated compulsory membership for individuals and limited member liability.

These changes paved the way for what we call “The Great Cooperative Debate.” In 1998 we made some dramatic changes to our organization that, frankly, were a complete disaster. The corporate Rabobanks stopped paying attention to our members; we decided to try our hand at investment banking abroad and lost billions of euros.

The debate took three years to settle, but at the end of it we had a clearer vision of who we were and where our focus needed to be. We decided to remain a cooperative bank with a focus on the Netherlands and retail banking.

As the last few years have proven, these choices have been a good fit for Rabobank. Our membership numbers are up—even if, due to needed efficiencies, we’ve seen a lot of mergers and the overall number of banks has dropped. Customer surveys show that Rabobank members are more likely to believe that their bank is acting with their best interests in mind than is the general population. And this was especially true during the crisis.

The financials also support our choice to stay a cooperative. We’ve continued to perform well
with no losses throughout the life of our organization, and our ROE has been much higher than that of the banks since the crisis—we had a 10% ROE in 2008 when banks were at −12%.

The Industry’s Future: Opportunities and Challenges

This isn’t to say that we don’t face challenges—we do. We’re working to balance the risks and rewards of domestic and international activities, and as traditional banks move back into the local/retail space, we face increasing competition. Funding can be a challenge because we don’t have access to external capital—but funding is a problem for all banks.

Although cooperatives typically tout the fact that their customers are members, as a percentage of clients our member numbers are quite low: about 12% of our entire client base. One thing we did to address this was to create financial instruments that can only be purchased by members.

We introduced membership certificates in 2001 with an interest rate that is 1% higher than that on the 10-year government bond. These helped to boost our membership levels and they also had additional value in that they are counted as Tier 1 capital.

We’re also working diligently to leverage cooperative advantages and educate the marketplace about the benefits of choosing us. The “new” ethical and moral requirements of recent legislation are quite familiar to cooperatives, and our strong asset base and member-focused mindset are important differentiators in the market place.

In 2011 we introduced convertible contingent capital, or a note. It’s a normal bond, but when our capital ratio hits a certain threshold, it becomes pure equity reserves. We were the first bank in the world to issue such a note. It’s quite expensive—I think we paid about 8% interest on it—but it also counts as Tier 1 capital, which makes it a worthwhile investment.

Our organizational structure helps us to run an efficient operation while still allowing for local decision making on some issues—for instance, we have centralized products and services, marketing, and strategy development, but each Rabobank can, within prescribed limits, make decisions about dividend distribution.
We’re also working diligently to leverage cooperative advantages and educate the marketplace about the benefits of choosing us. The “new” ethical and moral requirements of recent legislation are quite familiar to cooperatives, and our strong asset base and member-focused mindset are important differentiators in the marketplace. And, of course, our employees are essential. We are deeply committed to “walking the talk” when it comes to delivering on the cooperative promise, and our employees are a critical part of that.
Humans have a long history of saying one thing and doing another—even when the long-term benefits of one behavior greatly outweigh the perceived short-term benefits of the other. Why does this discrepancy exist and what can credit unions do to promote desirable behavior? Dilip Soman from the Rotman School of Management at the University of Toronto has done extensive research in this area and his work has uncovered some interesting findings.
Most people really do “know better” when it comes to everything from their health to their savings. So why do they routinely reach for the chocolate cake instead of the apple, drive when they could have biked, and spend their money on a big-screen television instead of preparing for retirement?

One important reason is what’s known as the “last mile problem.” This phrase traditionally refers to telecommunications and the fact that the last mile of connectivity is usually the most challenging. For our purposes we’ll use it to refer to the fact that we spend a lot of time and resources coming up with new products and ideas but very little energy getting people to use them. The fact that 96% of new products fail is good proof of this problem.

Using Defaults to Drive Desired Behavior

A great example of the last mile problem is organ donation. Research has shown a huge discrepancy in the acceptance of organ donation around the world. On one end we have countries like Denmark, the UK, and the Netherlands, where organ donation commitment ranges from 4% to 28%, and at the other end we have Austria, Belgium, and France, where more than 98% of the population are willing to be organ donors. There’s no middle ground—the numbers are either very low or very high.

Nothing seemed to explain these discrepancies until we started looking at how the organ donation system in each country works. In Canada, for instance, you have to opt in to become an organ donor and the process is very time-intensive. But in France, it’s just the opposite: Being an organ donor is the default and you have to go through a time-intensive process to opt out.
This default does two things: It suggests the norm and it recognizes that people are inherently lazy. In France, people perceive becoming an organ donor as the typical thing to do—and most people want to fit in and do what everyone else is doing. Unless they are extremely opposed to organ donation, they’re going to be too lazy to take the necessary steps to opt out.

The default is a powerful tool and it can work with lots of things, including finances. We’ve done programs in China and India where consumers could open an account online and used a drop-down menu to choose how much money they wanted to put in the account. In some experiments we listed the amounts from high to low and in others from low to high. Simply by changing the amount on the first line, we could get people to deposit more.

The Impact of Perceived Costs

Another example is the Canada Learning Bond. This program was designed to help eligible low-income Canadians save for their children’s education by giving them $500 of free money with no strings attached. This seems like a program that would be an incredible success, but only 16% of those who qualified said yes to the $500.

We tried to figure out why the numbers were so low. The first hypothesis was that people didn’t know about the program, but research showed that they did. Further analysis uncovered the catch: You had to have a bank account to participate.

Many of the intended participants were immigrants. They didn’t speak the language well, they felt uncomfortable with the forms and
complexities of opening an account, and many were working multiple jobs and didn’t have the time to get to a bank. We came up with a solution to help them: a mobile bank. Instead of waiting for them to come to the bank, the bank went to them. In one community, the participation rate jumped to 64%. This is an excellent example of a good product that was valued by its audience but had low initial acceptance because there was a perceived cost to access the product.

The idea of perceived costs is something that behavioral economists spend a lot of time on. My dissertation advisor, Dick Thaler, talks about mythical creatures that he calls “econs.” These creatures have amazing capabilities: They’re adept at performing complex mathematical equations, they always act rationally, they have infinite time horizons so they can always predict the future, they have infinite memories, and they have an exceptional understanding of the trade-offs involved in different types of behavior. In short, they’re nothing like real people!

Behavioral economists recognize that humans have limited cognitive capabilities and are likely to act irrationally. Humans are remarkably inconsistent, and a lot of these inconsistencies can be explained by a few simple principles.

Explaining the Inconsistency of Human Behavior

Context Influences Choice

My colleagues and I did a study on coffee that does an excellent job of illustrating the inconsistency of human behavior.

If you go into your average coffee shop and collect data on the most popular coffee size, you’ll find that 75% of customers order a medium-size coffee. If you ask people why, they’ll say that a small doesn’t have enough coffee, a large is too much, and a medium is “just right.” In our study we observed coffee purchases for a month among a fairly stable clientele and, yes, most of them ordered a medium.

After a month, we did something sneaky: We added two ounces to each coffee size. Now the small had the same amount as the old medium, and the medium was the same size as the old large. Most people continued to pick the medium, with the same rationale they had originally used in terms of the amount of coffee that was right for them. Then we cut each coffee size by two ounces and the same thing happened. The customers read the value of coffee as a function of context. They didn’t really know how much coffee was good for

Humans are remarkably inconsistent, and a lot of these inconsistencies can be explained by a few simple principles.
them, but there was a perception that both too little and too much weren’t good.

A similar example has to do with gas. In the past there were three choices—87, 89, and 91—and most people chose the middle, 89. Then, one day, a fourth choice appeared: 94 octane. Check with an engineer and you’ll find that only airplane engines need 94 octane, but the appearance of a new level pushed 91 to become the new middle. In fact, one gas company in the United States was accused of not even having 94 octane—the tank was empty but just placed there to bump the middle choice.

Because people have limited time and attention to devote to their day-to-day decision making, they end up using some sort of aid to help them. In the case of coffee and gasoline, the middle is their default.

**Attention Is a Scarce Resource**

Another reason for flawed decision making is that people don’t pay enough attention.

Here’s a test used to show this attention deficit. Look at each of the words in Figure 18 and quickly say what color the font is in.

The brain is using two processes: one to read the word and one to look at the color of the font. Most people get black correct because the word and font color are the same, but they get the second and third ones wrong. An exception is people whose first language is not English: They tend to get these right.

The point of this exercise is that when people are focused on a specific task—in this case, reading the word—they don’t have any attention to spare for a second task and rely on aids to guide them that may or may not actually help.

**Mental Accounting**

Another principle that illustrates the challenges people face in balancing their desires and their actions is mental accounting. Say you want to go to the symphony tonight. In the first scenario, you spend $100 on the ticket but you lose the ticket. In the second scenario, you lose the $100 before you buy the ticket.

In each scenario, do you buy another ticket?
The results show that of those who imagine losing the ticket, only 17% would buy another one, while 99% of those who imagine losing the money would. Why is that? People tend to segregate their money into different accounts, whether actually or mentally. If I’ve created a mental account for going to the symphony, the minute I buy the ticket, that budget has disappeared. If I lose the ticket, there’s nothing left in that account. On the other hand, if I lose money out of what I’ve categorized as a general fund, as long as there’s still money in that account I can buy another ticket. My grandmother used to do this with a series of tin cans. If there was money in the entertainment can, we kids could go to a movie. If there wasn’t, we couldn’t, even if there was, for instance, money in the food can.

Losses Hurt More Than Gains Make You Happy
Next, let’s talk about the power of loss aversion. People are loss averse. An example from my own life is cable television. When I first moved to Toronto, I received an offer to get 600 channels for only $50 a month. I said no to the offer but the company gave it to me anyway. For three months I had access to an amazing variety of television and I loved it. Then one day, I turned on the TV and I had one channel. I called and paid my $50 and got my cable back. At time zero, I was going to get cable for $50 and I didn’t value the offer. But when the company took something away from me, it suddenly seemed like a big loss and I paid to get it back.

Today Matters More Than Tomorrow
I also like to call this one the “Yes-Damn Effect.” In this one, people agree to a future action because they talk themselves into believing that in the future, life will be easier than it is right now—they’ll have more time, more resources, etc. We don’t ask someone to do something today, because they’ll have 20 reasons why they can’t say yes. Instead, we get them to commit to do it tomorrow. Of course, once they get to the point where they actually have to follow through, they’re likely thinking, “Damn, why did I agree to do that?” but there are locking mechanisms in place that force them to follow through. This can work for anything from exercise to savings.

This process acknowledges that people struggle with self-control and builds a self-control device for them. Piggy banks are a great example: We tell kids that they can save up for whatever they want by putting money into the bank, but if they break the bank, that’s too bad.

Figure 19: Mental Accounting

Mental accounting:
People categorize and spend money in narrow frames

Symphony tickets for $100
If you lost the ticket, would you buy another ticket?
17%
If you lost the cash, would you still buy a ticket?
99%
Combining Education and a “Nudge”

There’s a lot of discussion about whether you should educate people on why a particular action is good or give them a nudge in the right direction—and I use Dick Thaler’s definition of nudge, which is “any aspect of the choice architecture that alters people’s behavior in a predictable way without forbidding any options or significantly changing their economic incentives.”

It’s not an either/or and it’s important to think about both. We know that intent isn’t enough, so we have to do something to drive action.

Steps of Behavior Change

In order for people to change their behavior, three things have to happen:

- **Problem recognition and desire to act**—This step is largely driven by education.
- **Initiation of action**—This step typically requires a nudge.
- **Maintenance and nurturing**—Education is often what keeps them performing the action.

Initiation tends to be the hardest step, and to solve that problem we have to understand what’s stopping people.

A study was done in New Jersey that was very similar to the education funding program in Canada. To understand why low-income consumers weren’t opening bank accounts, researchers worked with a population at a soup kitchen in Trenton. Free financial workshops were held at the soup kitchen to educate the clientele about the importance of opening a bank account, but only 11% opened an account. The researchers decided to try something new: At the end of the workshop they started handing out a form that got people to say that they were interested in opening an account. Just filling out that form and indicating their interest pushed the account opening rate to 63%. It was a simple nudge, but it worked.

The Save More Tomorrow program, described in the book *Nudge*, uses many of the behavioral techniques that we’ve discussed. Employers that want to encourage saving help employees take simple automatic steps toward better savings behaviors:

- It’s an opt-out program: Employees are enrolled unless they choose not to be.
- It asks people to commit to a future action: saving a certain percentage of future raises instead of taking money out of their current salary, which would be perceived as a loss.
- The money is put into a separate bank account that will be used for a specific purpose.
This program was extremely successful and outperformed any other savings program.

This Year or Next?

A separate research study was done in India and was built around the idea of urgency: If we feel that something is happening soon, we know that we should start working on it now.

People were asked to commit to opening a bank account and saving 5,000 Indian rupees within six months. If they accomplished those goals, the government matched 20%.

The product was offered in two ways: June with a payoff of December (i.e., this year), or July with a payoff of January (i.e., next year). Our goal was to find out whether people were more motivated to act if they had a feeling of urgency.

We found that they were: If the deadline was this year, 30% of the people complied, but if it was next year only 8% did.

A Theory of Decision Points

Decision points are another important tool for influencing behavior. One test involved eating popcorn. People were given either one huge container of popcorn or the same amount of popcorn divided into six bags. The theory is that if you're going to eat popcorn, you make that decision but not necessarily the decision of how much. If people are given the large amount, they tend to eat it until it's gone. But if they're given the smaller amounts, each time they come to the end of a bag they have to make the conscious decision to start eating a new one. Most of the time they don't. Partitioning something decreases consumption.

Seeing how well this worked with popcorn and other foods, we decided to try it with savings. We tested this in India in a rural setting with a cash economy and limited access to banking. We had a very basic system of envelopes, and the program worked like this: We went to each house, set a target savings amount, and put it into a sealed envelope. This simple process doubled the savings rate.

Then we took it a step further and put pictures of the person's children on the envelope. Now they had a visual reminder that they were saving for their children's future, and savings rates quadrupled. Next, we used a clear plastic envelope, printed the children's picture on it, and put a perforated line through the picture. Now, in
order to get the money, they have to rip their children’s picture, and nobody touches those envelopes.

This technique has also been used in a digital setting: People create online savings accounts in multiple categories and use pictures to designate what the accounts are for. If they don’t meet the monthly goals for each of their categories, the pictures start to crumble. It’s been very successful.

Make Goals Vivid and Specific

The psychology of savings says that you have to give people a compelling reason to save and a mechanism to help them, whether it’s a physical envelope or the online system. There was another project where people put money into a piggy bank that required two people to open it. It’s a buddy system of support, plus the social norm that every time you want to take money out the other person will know that you’ve broken your commitment to save.

While these examples have focused on savings, we have seen similar results with borrowing. The general finding is that people are not cognitively sophisticated when trying to evaluate trade-offs and tend to focus on today. They still tend to sign up for the credit card with no annual fee, even if the interest rate is 50%. They can’t get past the benefit of “free.”

The traditional economic model is flawed because it assumes people will act in ways that they typically don’t; behavioral economics is more realistic. It’s a new science and we still need to do a lot of empirical work, but we have had some good examples of success.
In the aftermath of the economic crisis, governance has become an increasingly top-of-mind issue throughout the financial services industry. Donal McKillop, professor of financial services at Queen’s University of Belfast, recently completed a research study for the Filene Research Institute and Credit Union Central of Canada on three credit union segments: centrally affiliated Canadian credit unions, those in the Desjardins system, and US credit unions. Here’s what his work uncovered.
Before we look at the state of governance, I’d like to make a few points as a foundation for our discussion. First, a definition of governance:

*Corporate governance has been defined as a transparent decision-making process in which the leadership of a nonprofit organization, in an effective and accountable way, directs resources and exercises power on a basis of shared values.*

A key element to take away from that definition is that governance isn’t about managing the credit union—it’s about ensuring that it’s well run and operates in the best interest of the members. The job of the credit union’s management team is to make decisions that implement board policy; when the functions of the board and the management team are blurred, credit unions get into trouble.

And two other critical points:

*Sound corporate governance relies on compliance with all application legislation and regulation and also a healthy board culture that safeguards policies and processes and delivers strategy.*

*A board makeup that reflects knowledge, experience, expertise, and a willingness to challenge is also important in the development of good corporate governance.*

Effective corporate governance is a challenge for all financial services institutions, but credit unions must deal with a circumstance that other institutions don’t: the requirement that our board members be drawn from our membership. This means that we may not have access to the same level of expertise that other institutions do, especially at our smaller credit unions.

The typical governance structure for a credit union has three elements: the members, the board of directors, and the management. Where present, the supervisory committee brings the number to four (see Figure 20).
In order for the first three elements to work together effectively, management has to have a clear vision of the credit union’s direction and there has to be unambiguous accountability.

Our research was a combination of surveys and semi-structured follow-up interviews that brought additional depth to the project. For this study, we contacted 373 Canadian credit unions, all affiliated with one of the provincial central credit unions; 50% of the 451 Desjardins credit unions; and 3,500 US credit unions. We then broke respondents down according to the segment they are in and whether they have more or fewer than 10,000 members. One number to pay particular attention to is the average number of board members across the three groups. The empirical research suggests that 9–13 members is ideal, and most of these credit unions fall into that range. You can also see that there is a direct correlation between credit union size and board size (see Figure 21).

Other key information that we wanted to capture included the number of female directors and younger directors. As Figure 22 shows, there continues to be an imbalance between male and female directors and an even more obvious disparity based on age. If we want to capture younger members,
perhaps we should be more actively recruiting them to our boards.

In terms of tenure, the surveys show strong links to credit union size and length of time that board members serve: In both larger US and Desjardins credit unions, directors remain on boards for 11–15 years, while in smaller and centrally affiliated Canadian credit unions, 6–10 years is the norm. Here are some interesting thoughts that stood out from the interviews: Even though credit unions value diversity, they value skills and experience more; there's a tendency for nominating committees to replicate the current board makeup; and in smaller communities the same people seem to end up on a variety of boards.

We were pleased to see that a growing number of credit unions are using nominating committees, but there was a marked disparity: Most centrally affiliated Canadian credit unions and US credit unions have them but very few in Desjardins do. We also asked whether credit unions should go outside of their membership to look for board members with needed skills—which is against the credit union spirit—and there's evidence that credit unions are willing to do this.

Credit union directors have historically tended to be “enthusiastic amateurs.” There is value in attracting people who understand and value the heritage and philosophy of credit unions, but amateurs might lack the skills needed to ensure sufficient levels of business performance. A credit union’s position along the development scale might drive whether an enthusiastic amateur can be an effective board member—for instance, a nascent credit union that’s operating as a very simple savings and loan vehicle might be the place for an enthusiastic amateur.

Our surveys pinpointed some provocative thoughts about skills: Democracy might be overrated when it comes to picking board members; headhunting, not advertising, is what usually turns up candidates; and boards are placing increasing importance on business acumen, not just credit union knowledge and enthusiasm, and are willing to ask desirable candidates to join the credit union.

We also tried to get a better understanding of board members’ skills and qualifications as they relate to the functions of the credit union. If you were hiring a management team, these would be critical, but

<table>
<thead>
<tr>
<th>Jurisdiction</th>
<th>Number of female directors (average)</th>
<th>Number of younger directors (18–35 years old, average)</th>
</tr>
</thead>
<tbody>
<tr>
<td>Canadian (centrally affiliated)</td>
<td></td>
<td></td>
</tr>
<tr>
<td>Members &lt;10,000</td>
<td>2.4</td>
<td>0.8</td>
</tr>
<tr>
<td>Members &gt;10,000</td>
<td>3.1</td>
<td>0.4</td>
</tr>
<tr>
<td>Canadian (Desjardins)</td>
<td></td>
<td></td>
</tr>
<tr>
<td>Members &lt;10,000</td>
<td>2.8</td>
<td>0.9</td>
</tr>
<tr>
<td>Members &gt;10,000</td>
<td>3.7</td>
<td>1.6</td>
</tr>
<tr>
<td>US</td>
<td></td>
<td></td>
</tr>
<tr>
<td>Members &lt;10,000</td>
<td>2.3</td>
<td>0.3</td>
</tr>
<tr>
<td>Members &gt;10,000</td>
<td>2.4</td>
<td>0.3</td>
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are they with boards? The main takeaway is that credit unions largely do want their boards to possess these skills—with more than 70% of respondents agreeing that they are necessary—but as a board, not at the individual level (see Figure 23). Smaller credit unions and those in the Desjardins system don’t think minimum competency requirements are necessary, and nobody likes the idea of using regulation to ensure skill levels.

In the interviews we had a range of beliefs in this area, including those who feel that board members need to be strategic thinkers, not credit union managers; those who feel financial skills are required; and others who feel it is simply a matter of luck whether the board is able to carry out its duties. The middle ground: Boards should be strategists with a vision for the credit union but also need to possess a basic understanding of the credit union’s business model.

One point that came up throughout the research is the challenge of finding board members with necessary skills. Respondents widely value training, but there are mixed feelings about whether current training is meeting board members’ needs (see Figure 24).

Training is provided by both internal and external resources and is strongly correlated to size: Smaller credit unions tend to go outside for training. Most credit unions don’t require large amounts of training: 0–5 hours per director is most common, except at centrally affiliated Canadian credit unions with more than 10,000 members, which provide 11–15 hours of training per director.

The “whys” behind these low numbers include credit unions that are just starting to allocate funds for training, those that largely feel that “common sense” should be the key qualification for board membership, and those that say it is hard to expect largely volunteer/low-paid board

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**Figure 23: Skills and Competencies of Directors (Summary Findings)**

<table>
<thead>
<tr>
<th>Jurisdiction</th>
<th>The board must possess the skills and qualifications relating to the functions of the credit union</th>
</tr>
</thead>
<tbody>
<tr>
<td></td>
<td>Agree completely</td>
</tr>
<tr>
<td><strong>Canadian (centrally affiliated)</strong></td>
<td></td>
</tr>
<tr>
<td>Members &lt;10,000</td>
<td>5 (9.3%)</td>
</tr>
<tr>
<td>Members &gt;10,000</td>
<td>17 (34.7%)</td>
</tr>
<tr>
<td><strong>Canadian (Desjardins)</strong></td>
<td></td>
</tr>
<tr>
<td>Members &lt;10,000</td>
<td>18 (25.4%)</td>
</tr>
<tr>
<td>Members &gt;10,000</td>
<td>25 (35.7%)</td>
</tr>
<tr>
<td><strong>US</strong></td>
<td></td>
</tr>
<tr>
<td>Members &lt;10,000</td>
<td>9 (10.8%)</td>
</tr>
<tr>
<td>Members &gt;10,000</td>
<td>31 (23.5%)</td>
</tr>
</tbody>
</table>

**Figure 24: Training of Directors**

<table>
<thead>
<tr>
<th>Jurisdiction</th>
<th>Existing training provides directors with the skill sets necessary to fulfill their duties</th>
</tr>
</thead>
<tbody>
<tr>
<td></td>
<td>Agree completely</td>
</tr>
<tr>
<td><strong>Canadian (centrally affiliated)</strong></td>
<td></td>
</tr>
<tr>
<td>Members &lt;10,000</td>
<td>12 (22%)</td>
</tr>
<tr>
<td>Members &gt;10,000</td>
<td>8 (16%)</td>
</tr>
<tr>
<td><strong>Canadian (Desjardins)</strong></td>
<td></td>
</tr>
<tr>
<td>Members &lt;10,000</td>
<td>14 (20%)</td>
</tr>
<tr>
<td>Members &gt;10,000</td>
<td>11 (16%)</td>
</tr>
<tr>
<td><strong>US</strong></td>
<td></td>
</tr>
<tr>
<td>Members &lt;10,000</td>
<td>26 (31%)</td>
</tr>
<tr>
<td>Members &gt;10,000</td>
<td>48 (36%)</td>
</tr>
</tbody>
</table>
members to find the extra time to commit to training.

We next looked at member participation, especially at the annual general meeting (AGM). As credit unions, we tout the idea of one member, one vote and the valuable role that members play. The research shows that this doesn’t tend to be the reality. Attendance at the AGM is very low, with the worst numbers in the United States (see Figure 25). Even if we provide electronic and proxy voting, very few members are weighing in.

There are also relatively low numbers when it comes to member participation in the credit union board. Although the majority of credit unions have an equal number of nominees and open slots, there are some credit unions that have fewer nominees than open positions. In general, this seems to suggest a low level of member involvement.

We next looked at whether credit union boards evaluate their own performance. The majority of Canadian credit unions do; most US credit unions do not (see Figure 26).

Among those that do evaluate their performance:

- Desjardins credit unions tend to evaluate against the board’s business plan.
- Centrally affiliated Canadian credit unions and US credit unions use criteria developed by the board.

Feedback we got from the interviews shows boards that develop their own criteria tend to use a balanced scorecard that includes credit union financials and member satisfaction—not how well the board complies with the credit union’s philosophy—and that it is important to evaluate the board as a whole, not individually. One CEO commented that they assess the board’s strategic role,
provide oversight, and bring in a facilitator as needed.

We were curious to see what forces drive change at credit unions. In the survey, respondents had nine options; Figure 27 shows the top three—credit union management, board, and members. The total adds up to 200%, which is why the percentages seem a bit off here.

The key catalyst for change at Desjardins is the board, while at both centrally affiliated Canadian and American credit unions, it’s the management. Members are a distant third, which isn’t surprising given the low level of member participation.

The last section of our research focused on the big questions that credit unions throughout the United States and Canada continue to ask themselves: Do members understand and value the cooperative difference, and is the credit union business model appropriate for today’s world?

As we’ve seen elsewhere, most consumers don’t understand and don’t appreciate our model, especially in the United States, which means that credit unions have to do a better job of getting the message out.

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Figure 27: Drivers of Change—The Key Three

<table>
<thead>
<tr>
<th>Jurisdiction</th>
<th>Please assess the importance of the following in driving the change process in your credit union. Rank in order of importance: 1st, 2nd, 3rd, 4th, 5th, 6th, 7th, 8th, and 9th</th>
</tr>
</thead>
<tbody>
<tr>
<td></td>
<td>A (% ranked 1st or 2nd)</td>
</tr>
<tr>
<td>Canadian (centrally affiliated)</td>
<td></td>
</tr>
<tr>
<td>Members &lt;10,000</td>
<td>79.6</td>
</tr>
<tr>
<td>Members &gt;10,000</td>
<td>89.8</td>
</tr>
<tr>
<td>Canadian (Desjardins)</td>
<td></td>
</tr>
<tr>
<td>Members &lt;10,000</td>
<td>73.0</td>
</tr>
<tr>
<td>Members &gt;10,000</td>
<td>74.3</td>
</tr>
<tr>
<td>US</td>
<td></td>
</tr>
<tr>
<td>Members &lt;10,000</td>
<td>77.1</td>
</tr>
<tr>
<td>Members &gt;10,000</td>
<td>83.3</td>
</tr>
</tbody>
</table>

Note: A: Management of the credit union; B: Board of directors; F: Members.

Figure 28: Changing Times

<table>
<thead>
<tr>
<th>Jurisdiction</th>
<th>To what extent do you agree that the majority of the membership of your credit union continues to value the cooperative principles upon which the credit union is based?</th>
</tr>
</thead>
<tbody>
<tr>
<td></td>
<td>Agree completely</td>
</tr>
<tr>
<td>Canadian (centrally affiliated)</td>
<td></td>
</tr>
<tr>
<td>Members &lt;10,000</td>
<td>4 (7%)</td>
</tr>
<tr>
<td>Members &gt;10,000</td>
<td>5 (10%)</td>
</tr>
<tr>
<td>Canadian (Desjardins)</td>
<td></td>
</tr>
<tr>
<td>Members &lt;10,000</td>
<td>7 (10%)</td>
</tr>
<tr>
<td>Members &gt;10,000</td>
<td>5 (7%)</td>
</tr>
<tr>
<td>US</td>
<td></td>
</tr>
<tr>
<td>Members &lt;10,000</td>
<td>7 (8%)</td>
</tr>
<tr>
<td>Members &gt;10,000</td>
<td>8 (6%)</td>
</tr>
</tbody>
</table>
In today’s competitive marketplace, the cooperative business model is in the midst of an identity crisis. Is the model still relevant to consumers and can it survive? Or will cooperatives be forced to demutualize? Daniel Côté, professor of business strategy at HEC in Montreal, has uncovered some encouraging links between loyalty and cooperatives that lay the foundation for a new cooperative paradigm.
About 15 years ago, I held a six-day workshop with 300 credit union managers from Desjardins that was designed to examine the relevance of the cooperative management structure. During that workshop we focused on these overarching questions:

- What is the cooperative difference today? Does it still exist?
- Do our members view themselves as cooperative partners?
- Have we let the ball drop?

We discovered that credit unions in rural areas still felt there was relevance in the cooperative message, but that for the most part urban organizations didn’t. There was a sense that credit unions had lost their core ideology and were becoming increasingly irrelevant in a globalized world—that credit unions were on the path to becoming banks.

Most of these credit union managers were asking themselves if they had any autonomy left, if there was any advantage to staying a credit union, and if the model needed to change.

They weren’t ready to give up on the cooperative model, but they needed help.

After hearing that message again and again, I became increasingly intrigued and started to look for a way to assist these credit unions. I came up with a model based on two axes: the intensity of cooperative rules and the intensity of market rules (see Figure 29). As credit unions

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Figure 29: Mapping the Cooperative Identity Crisis

![Figure 29: Mapping the Cooperative Identity Crisis](image)
move from point A to point B, they’re in a period of identity crisis. If they don’t find a way to reaffirm the cooperative difference, they move from Point B to Point D, and demutualization starts to look like their only option.

Creating a New Cooperative Paradigm

How can we stop this progression? The world is a very different place than it was 70 years ago when the cooperative financial movement was first taking root in North America. We can’t just return to our past; we have to reinvent the cooperative organization and come up with what I call a new cooperative paradigm, or NCP.

When I started doing research on the NCP, I looked at the traditional cooperative paradigm and came up with four areas that we need to consider in creating a new one: loyalty, the mobilization of values through employees, being a learning organization, and meaning and legitimacy (see Figure 30).

Figure 30: From Cooperative Specificity to Competitive Advantage

The Value of Loyalty

As I shared these ideas with others, I began to see that loyalty was the critical element. Why loyalty? Because of a range of external pressures that include:

- International competition.
- Weaker growth rates and mature markets.
- Increased pressure on prices plus more challenges in cutting costs.
- A smaller number of customers and more competitors chasing them.
What incentivizes key stakeholders?

Cooperative rules

Relevancy of cooperative identity via a new cooperative paradigm (NCP)

Market rules

Competition, deregulation, globalization

Figure 31: The 10 Principles Essential for Loyalty

1. Partnership based on ethics and integrity . . . without compromise
2. Added value—world-class business proposition
3. Mutual trust
4. Open books—access to information and transparency
5. Enterprise “coached” by its clients—mutual help
6. Acting on what excites the client
7. Focus on the unexpected
8. Proximity with clients
9. True interest after sales
10. Anticipation of future needs and expectations

Values as central to the management of loyalty


Figure 32: Loyalty and Cooperative Identity: A Convergence

<table>
<thead>
<tr>
<th>Principles</th>
<th>Loyalty</th>
<th>Cooperative identity</th>
</tr>
</thead>
<tbody>
<tr>
<td>First bloc</td>
<td>1. Ethics and integrity</td>
<td>1. Ethics and integrity</td>
</tr>
<tr>
<td></td>
<td>3. Transparency and access to information</td>
<td>3. Transparency and access to information</td>
</tr>
<tr>
<td>Second bloc</td>
<td>4. Proximity with clients</td>
<td>4. Usership-ownership status, i.e., market relationship + ownership relationship</td>
</tr>
<tr>
<td></td>
<td>5. Coach the enterprise</td>
<td>5. Democratic structure, i.e., general assembly + board</td>
</tr>
<tr>
<td></td>
<td>6. True interest toward buyer long after the transaction</td>
<td>6. Cooperatives’ raison d’être: to reinforce the member’s status</td>
</tr>
<tr>
<td>Third bloc</td>
<td>7. Business proposition and added value</td>
<td>7. Easier access to the consumer’s mind (association and enterprise)</td>
</tr>
<tr>
<td></td>
<td>8. Focus on the unexpected</td>
<td>8. Easier access to the consumer’s mind (association and enterprise)</td>
</tr>
<tr>
<td></td>
<td>9. Anticipate future needs</td>
<td>9. Easier access to the consumer’s mind (association and enterprise)</td>
</tr>
</tbody>
</table>

Figure 33: Path to the New Cooperative Paradigm
I also discovered a book called *Loyalty Management* by Frederick Reichheld, and many of his case studies revolve around the high level of loyalty shown in cooperative organizations. Reichheld’s work includes 10 critical principles of loyalty (see Figure 31).

As we looked at the key principles of effective loyalty and the key principles of the cooperative identity, it quickly became apparent that there was a high level of convergence (see Figure 32).

If we could figure out a way to increase the level of loyalty members felt toward their credit union, perhaps we could move to a stronger position.

## Earning Loyalty

Loyalty is never a given. Both customers and employees choose to give their loyalty on a voluntary basis, and management needs to understand the role it plays in creating loyalty.

Loyalty requires:

- A strong, shared vision.
- Trust.
- Complete commitment—every level of the organization and every aspect of management, business, and transactions has to be implemented on the basis of loyalty.
- Delivery of constant, superior value.

Of course, most companies believe they’re delivering superior value, but do their customers? A consulting firm, Bain & Company, did an interesting study a while back. They surveyed senior management and asked if they were delivering superior value to their customers. The answer was “yes” from 80% of the group. But when Bain went to the customers of these organizations, customers at only 8% of the companies thought they were receiving superior value (see Figure 34). The delivery gap was huge and certainly limited the ability of these companies to earn their clients’ loyalty.

## Member-Oriented Missions and Values

Recognizing that there were likely to be strong links between loyalty and performance, we started looking at credit unions with highly loyal members. We found that these credit unions each had a strategic profile that stressed their missions and values and that both were member-oriented.
The missions:
- Focused on member well-being.
- Made decisions that benefited members.
- Contributed to the well-being of the community.
- Worked to build a more just and humane society.

Regarding values and coherence:
- Decisions were based on core values.
- Behavior was perceived to conform to values held by members, employees, and the public.
- Values were integrated into the business practices.

Understanding Why Members Might Value the NCP

We conducted a research study and looked at how members want to do business with their financial services provider. Nearly 50% want a relationship vs. just 9% who want to focus on transactions. This was in line with what we were hoping for: After all, if most members only want to cash a check, there’s not much opportunity to build a long-term relationship with them.

They also told us that they want good service and perceived value and that they have to trust their provider. No surprises there!

We also weren’t too surprised to learn that they feel cooperatives:
- Listen better.
- Understand better.
- Have products/services more in line with their needs.
- Are inclined to develop long-term relationships.
- Are easier to trust.
- Have distinct values and practices.
- Are geographically closer to and more engaged with the community.

But the members shocked us when we asked whether they value the cooperative model. Cooperative status is very important to 70% of the respondents, and 85% rate it five, six, or seven on a seven-point scale. This was completely unexpected and it seems to be an important antecedent to loyalty: The consumer values the cooperative model and they are more likely to be loyal to a financial institution that can offer it.

And not only are they loyal; they take things one step further and voluntarily deliver reciprocal behavior, such as promoting the credit
union, providing the resources to help improve service quality and productivity, and coaching us to better performance. As both users and owners, they are in an excellent position to do this well and to benefit from having done so.

In the past, cooperatives were created when people with common goals, values, or resources came together to build a collective solution. The new cooperative paradigm turns this equation on its head. First, we attract a consumer who perceives us as being trustworthy, listening to them, and offering products and solutions in line with their needs. Over time we build loyalty and later, reciprocal behavior, which both improves performance and creates a cooperative group. The cooperative model now becomes the tool that creates the group, rather than vice versa.

Figure 35: Loyalty: Cooperative Status as Antecedent, Reciprocity as Consequence
Keeping an Eye on the Ball: Credit Unions, the Level Playing Field, and Competitive Balance

The “level playing field” has been widely embraced for its connotation of objectivity and fairness for all. But unless players bring the same strengths and assets to that field, it’s highly unlikely that a one-size-fits-all approach will yield equal benefits. Instead, Marc-André Pigeon of Credit Union Central of Canada and Ben Rogers from the Filene Research Institute recommend looking to competitive balance to redress the flaws of the level playing field and deliver not means, but ends.
The metaphor of the level playing field is extremely powerful because it comes with language that’s inherently democratic and good. After all, who can argue with the ideas of equal opportunity and fairness? But the problem is that the level playing field really isn’t. Too often it leads to one-size-fits-all regulations that favor bigger, more entrenched players and create burdens for new and smaller ones. And it’s a means that doesn’t accomplish the desired ends.

A better alternative in many situations is competitive balance. This is already used in a number of regulatory situations—such as effective tax rates for different income levels—and it’s very common in sports.

Handicapping in golf is an example of competitive balance, as is revenue sharing in Major League Baseball. If your baseball team is in a large market like New York, you know you’re helping to support more competitive play throughout the league and contributing to the overall health of the sport.

Other sports-related examples include variable player drafts—where the worst team one year gets the first pick the next—and travel schedules that reflect the distance a team has to go to play. Although this metaphor is very powerful, we have to recognize that we can’t take it to extremes: For instance, everyone still plays with the same bat.

Competitive balance has also been common in industry, especially in telecommunications and banking. The examples that follow are all from the Canadian market.

Let’s start with telecommunications. Historically this has been a regulated monopoly. In the past the government guaranteed certain rates of return to the top five players as long as they did things like provide

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Figure 36: Major League Baseball

In the context of baseball, proper competitive balance should be understood to exist when there are no clubs chronically weak because of MLB’s financial structural features. Proper competitive balance will not exist until every well-run club has a regularly recurring hope of reaching postseason play.
rural service and adjust prices to ensure cheap local calling. There was something similar in banking, too, called the Grand Bargain. This helped establish a certain level of stability in the industry, again focusing on the top five institutions, by guaranteeing markets and limiting competition.

Protective measures started to unravel in the 1980s and 1990s when these industries became deregulated. The telecoms still had a certain level of security because they controlled the Internet and the smaller providers had to tap into the resources of the larger ones to get online. But the regulator, the Canadian Radio, Television, and Telecommunications Commission, was also able to insert some requirements that helped to improve competitive balance. These included requiring the big providers to deliver access to the smaller ones and setting aside part of the spectrum for smaller providers to bid on.

The banking industry didn’t have the advantage of a must-have service, but it kept the benefits of size, geographic reach, and, often, a regulatory bias, whereby federal policymakers tended to write regulations with large banks in mind. The financial services industry has made some attempts at competitive balance. These have included linking the intensity of supervision to the size of an institution and eliminating the goods and services tax on transactions between cooperative credit union–type organizations—in the banking environment these would typically be internal, nontaxed transactions and it was only logical that a similar transaction in the credit union space be treated equally.

The Benefits of Competitive Balance

If we want regulators to consider the use of competitive balance instead of falling back on the level playing field concept, we need to help them understand the benefits. Fortunately, they’re quite straightforward.
Competitive Pressure and Price Discipline
Having players of a variety of sizes helps to ensure that the oligopolistic players—in this case, the big banks—can’t fix product prices. Being linked to the price offerings of smaller, fringe players keeps the pressure on the larger players.

Helps Ensure Choice
Fringe players also help to ensure that consumers will have more product and service options to choose from.

Drives Innovation at the Edge
The vast majority of innovation doesn’t happen at the big organizations; it happens in the stereotypical inventor’s garage. Google wasn’t always Google; Apple wasn’t always Apple. A wide variety of products and services that are now offered across the marketplace were first delivered by small credit unions that could afford to take risks and serve niche markets.

The Red Tape Reduction Commission
Small businesses are so important to the overall economy that a study was recently commissioned to determine how regulations impact small businesses; many credit unions fit into this category.

The Red Tape Reduction Commission study showed that the federal government needs to be more cognizant of how its regulations affect small businesses and how they can compromise the competitive benefits, choice, and innovation that small businesses deliver.

If Canadian and American credit unions want to approach regulators about the benefits of competitive balance, we’ve come up with a list of areas that we feel would be good to start with (see Figure 39).

Figure 38: Red Tape Reduction Commission

“When the design and implementation of regulations do not take into consideration the capacity of small businesses to meet requirements, the result is a one-size-fits-all bias that does not work.”

Figure 39: Competitive Balance: Future Applications

CANADA
- Deposit insurance
- Merger review fees
- Capital requirements and leverage ratios

UNITED STATES
- Regulatory burden
- “Too big to fail” policies
- Consumer Financial Protection Bureau

Too many of these regulations are currently written with no regard to the impact they'll have on smaller institutions. Too often the idea of the level playing field has been used as a distraction and compromised government’s ability to deliver good policy. We need to keep reminding them to look to what they’re actually trying to accomplish and continue to show them that competitive balance will deliver the competition, the choice, and the innovation that they claim to want.
The concluding session was a panel discussion among the presenters and the moderators from Credit Union Central of Canada and the Filene Research Institute.
Some of our speakers have discussed the fact that a desire to tap into the capital surplus can drive demutualization. Is there a mechanism to ensure this doesn’t happen?

**Groeneveld:** At Rabobank, members don’t get a benefit from the results of the entire group—there’s no dividend or payout whatsoever. Each bank puts 1%–5% of their profits into a fund and then can spend these funds on cooperative dividends in the working area. The members can decide which projects these funds will be spent on, but an individual member can’t get a payout. So, if one bank wanted to opt out, the members couldn’t cash in because the equity is inside the entire organization.

**What are some warning signs that can indicate you’re in danger of demutualization?**

**Groeneveld:** We went through a tough period about 15 years ago, and for us the warning signs were that we were focusing too much on other activities—about 40% of our revenues were coming from foreign activities, insurance, and private equity. We had a point of crisis between the executive board and the rest of Rabobank around 2001. This occurred both because of the costs we were incurring to enter these new areas and because there was a clash of cultures in strategic direction between the board and the rest of the organization.

**Gall:** You’re in trouble when the focus becomes too diluted. In the building societies’ experience that’s become clearer since the demutualization episode in the late ’90s and up to the exercise we did last year. When it comes to effective governance, you have to be sure that the focus is on meeting members’ needs.

**McKillop:** In terms of warnings, look at the Irish credit unions. They’re in significant difficulty at present and I suspect that part of their problem is the general state of the European and Irish markets. But in general, one of the key problems is when credit unions lose their focus and want to become more like other financial organizations, like banks. The loan-to-asset ratio over the last 10 years has
dipped and dipped at Irish credit unions so that now it’s sitting at 40%. To a large extent, their focus is on investments—they’re targeting safe investments, but they’re also targeting equities. The warning sign is when you look at something outside of what you’re good at.

Côté: When the members start talking about the co-op instead of my co-op, you need to listen to that. It’s also a concern when cooperatives are simply copying the business practices of private corporations. If your managers feel that cooperation is, at best, a board governance issue, you need to address that. Cooperation is supposed to be what your organization is all about and that sense has to permeate at every level.

Soman: There’s a simple rule of thumb: If more than a third of your activities are not in your core business, then that’s a warning sign that there’s too much dilution going on. Another is member satisfaction. If you’ve always seen this level going up and now it’s going down, pay attention.

Have there been attempts in other countries to create other types of cooperative enterprises (those discussed included housing, retail, agricultural, and financial)?

Groeneveld: In the Netherlands, cooperative banks got their start because everyone didn’t have access to financial services. Now that that is no longer the case, we’re focusing on introducing the cooperative model in emerging countries and in nonfinancial applications. We’ve found that cooperatives linked to agriculture or food are a good place to share the benefits of the cooperative model.

Soman: In India a lot of agricultural cooperatives are working with co-op banks. Co-op banks have also been successful working with microfinance organizations and have helped farmers through quasi-government agencies.

Gall: In addition to building societies, we also represent cooperative banks, the largest of which is called the Cooperative Bank. This bank is part of a larger cooperative group that owns farms and a large retailer and a travel management company and they all brand themselves together. Building societies themselves might not have direct links to other cooperatives, but we do meet occasionally to try to shape policy.

Does cooperation have a downside for some industries—does it sometimes lead to self-supporting malaise?

McKillop: That could be an issue with, for instance, limited board turnover. If you don’t have board renewal, then you start doing the same old things over and over again. This illustrates why it’s
important to have board succession plans and to make concerted efforts to reach out to younger members.

Groeneveld: In recent years, the number of people on the average credit union board has increased quite a bit and it’s getting more challenging to monitor what’s going on. How can a member really monitor what’s happening? The same issues are happening in the for-profit world, but they’re becoming our problems, too.

What were some of the issues that forced different credit unions into demutualizing and what helped turn things around?

Gall: The government did a study after our demutualization and it showed that much of the push came from the directors. The motivation seemed to range from greed to empire building to being freed from previous constraints.

In the example of Northern Rock, one of the building society constraints was that they had to have at least 50% of their funding from retail sources. At the time Northern Rock failed, only 25% of its funding came from this source. Roughly 75% was from the wholesale market—wholesale, short-term funding—which is the direct opposite of what the cooperative currently has. The so-called freedom to operate without constraints meant that a lot of cooperatives tried to expand too quickly without the controls or expertise to manage it. Focusing on your long-term member relationships can help you to maintain your cooperative’s relevance.

Groeneveld: Our roller-coaster experience in investment banking was actually approved by the local Rabobanks and they gave the board the mandate to explore this area. But we went wrong by getting too far away from the cooperative nature of our organization. There wasn’t an active membership to keep us on track and we found ourselves drifting away from everything that we traditionally valued.

When the situation started to turn in the middle of the 1990s, due to the debates, we started to realize that it didn’t make sense for us to be in these investment services. The cultural differences meant that we couldn’t be a big player and these activities didn’t benefit our members.

I was struck by Professor Côté’s statement that the malaise seemed to be strongest in the urban regions. Given that urbanization isn’t a trend that’s going to stop anytime soon, what role can the broader credit union system play to help create successful urban economies?

Côté: The malaise is definitely not just urban. I think the most important thing that credit unions can do is to be world-class
organizations. You have to rediscover the competitive advantage that's gained from being a cooperative and leverage that.

I was interested in the panelists’ reaction to the low attendance at annual general meetings. Is this something that’s also happening in the UK and the Netherlands? And do people feel that indicates a lack of loyalty, or something else?

**Groeneveld:** We have 1.8 million members and 1%–2% of them are very active. It would be extremely inefficient if all of these members wanted to have a say in the operations of your organization, and that’s why we have representation. Are these numbers disappointing? No, because they’re chosen—elected—by other members, which means there are actually many more people involved in the organization indirectly. And they’re involved in the decision making at the very highest levels. You do need to have very active members, but it’s important to organize your decision making in a way that is effective and efficient.

**Gall:** It’s very similar in the UK—and the numbers are sometimes even lower at the annual general meeting (AGM). But we do have a higher number who cast their vote—about 14% of eligible members vote by proxy. At the height of the crisis, that rose to 19% because people were a lot more concerned about having their say. We’ve taken a number of steps to encourage members to vote: We make a charitable donation for every vote we receive, we let them vote online, we provide prepaid envelopes to facilitate proxy voting. Our goal is a representative democracy.

**McKillop:** I would just add that I don’t think the lower numbers are a reflection of anything; I think it’s just the way of the world. There’s less physical attendance at meetings and as organizations become larger, it’s less efficient to be at the AGM. Maybe what it does mean is that you need to establish other mechanisms that can help you to get membership input. When we surveyed people about what they felt to be desirable attendance levels at the AGM, they talked about anywhere from 1% to 10%.

**Côté:** At one credit union (Caisse de St. Roch de L’Achigan) their attendance at the AGM is about 10%, but the main reason they’re getting together is social. Certainly they have business to attend to, but the overriding reason that people come is to celebrate. My approach is about participation and perhaps if we can reinvent ourselves and get back to that, we’ll be able to rethink the whole concept of democracy in the cooperative.

I did work with one cooperative—Agropur, a dairy cooperative in Canada—in the 1980s and 1990s, and what they do in terms of democracy is amazing. They’ve made a strong investment in
education for more than 70 years that’s geared to both business issues and the cooperative message. They also stress the importance of representatives: One out of every seven members is a representative. I don’t know if this model would work for credit unions, but it’s certainly interesting.

In the United States and Canada, we’re operating within the context of high household debt. How do thoughts about choice architecture apply in this environment?

Soman: There’s been a lot of interest in choice architecture in economies around the world. The government of South Korea launched a series of programs to better understand how to present information about banking and savings products so that people will actually invest in them. There’s been a growing interest in behavioral economics, and in Canada more people understand that success isn’t just about the product, it’s about framing the message in a way that makes the desired course of action appealing.

What are some of the financial institutions in Canada doing that might be of interest to our audience?

Soman: Canadian organizations have been a lot more interested in experimentation. From behavioral economics we know that there is no one right answer. There is no one model that maximizes savings; we just have to try something. Given that credit union markets aren’t typically that large, it makes it easier to experiment. I think that’s been hugely positive: The cost of making a mistake isn’t that high.

If each of our presenters were to pick a few words that you feel best describe the ideal characteristics of a credit union or cooperative director, what would they be?

Soman: Customer-focused; something that’s deeply connected with the interests of your clients but also has a societal impact.

Groeneveld: Connecting: with your clients, society, and your employees.

Gall: Member-focused and constructively challenging.

McKillop: Member-focused.

Côté: Humility and sensitivity that allow you to capture moments of truth. The whole idea of loyalty is impossible if you don’t have that humility and sensitivity. Yvonne Poirier has been a champion in this area and he’s been able to say when he’s wrong, and I think that’s critical to building loyalty.
1. Hamish McRae, “We Must Nurture the Not-for-Profit Sector,” *The Independent*, June 8, 2011.


International Cooperative Governance and Market Trends
A Credit Union Research Symposium at the University of Toronto

Executive Summary by Ben Rogers
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