Economics, Cooperation, and Employee Ownership: The Emilia Romagna model

John Logue

There are at least two European models for employee ownership that demand American attention. The one is the Mondragon cooperative group in the Basque region of Spain which has been frequently discussed (see *Owners at Work* XII:1 and XIII:1). The other is the much less well known complex of employee-owned companies in the Emilia Romagna region in Northern Italy around Bologna.

In some ways, Emilia Romagna and the Basque co-ops are very different. In the Basque region, the Mondragon employee cooperatives grew out of Catholic social teaching and Basque nationalism in the 1950s and 1960s. In Emilia Romagna, by contrast, the co-ops grew up with the 19^{th} century labor movement but split into three different partisan political federations -- Catholic, Socialist/Communist, and Social Democratic/Republican -- in the 20^{th} century. They have no link to ethnic or linguistic minorities.

In other ways, they are very similar. Both appear to owe their success today to a combination of small scale, flexible employee-owned firms which achieve economies of scale to compete globally through collaborative research and development strategies, cooperative export efforts, their own financial institutions, and other forms of collaboration and cooperation that are largely or completely missing in the employee-owned sector in the US.

There's a great deal we can learn in Ohio from what this one small region in Northern Italy has achieved over the last fifty years.

Promotion of small business

Emilia Romagna is roughly comparable to Northeast Ohio in population: 3.9 million vs. 3.8 million. Unlike Northeast Ohio, it has its own regional government – one of 20 in Italy.

By Ohio standards, firms are very small scale. Emilia Romagna has 420,000 firms – one for every 9 men, women and children -- vs. 110,000 in Northeastern Ohio. More than half the population are co-op members. Coops -- including employee-owned businesses -- employ 10% of the workforce and generate about 30% of the GDP in the region and up to 60% of the GDP in some cities like Imola, according to University of Bologna economist Stefano Zamagni. Flavio del Bono, the regional finance minister, tells foreign visitors point blank that "the massive presence of cooperative firms is a stabilizing factor in the regional economy."

"Emilia Romagna has 7% of the population of Italy," says del Bono. "But we account for 9% of the Italian GDP, 12% of Italy's exports, and 30% of Italy's patents." Unemployment is an enviable 3%.

It wasn't always this way. Emilia Romagna moved from among the poorest of Italy's industrial regions in 1950 to the richest in 2005. Today it's among the 10 richest of the European Union's 122 regions.

After the war it became part of Italy's so-called "Red Belt," the part of Italy that was in the front line of the Cold War because the Communists and Socialists won the elections there. The CIA poured money into the region to split the labor and co-operative movements. But lacking the large-scale industrial base of a Milan or a Turin, a funny thing happened: The left-wing government in Emilia Romagna embarked on a strategy of promoting small business for economic development.

At the core of the Emilian Romagna success story is the regional government's focus on support small businesses – employee-owned and family-owned owned alike. Crucially it encouraged the development of cooperative institutions for all small businesses to achieve economies of scale through creating "industrial sector service centers" that have supported small business clustering in the region. They provide shared services in research and development, purchasing, education and training, workplace safety, technology transfer, marketing and distribution, exporting and more for scores or hundreds of small businesses in industrial sectors like ceramics, textiles, footwear, construction, and agricultural machinery.

These service centers combine the economies of scale with the advantages and flexibility of small business. They have encouraged "flexible manufacturing" for which the region is famous in which small businesses in the same industry collaborate in joint bids for major contracts. The region is home to some very high value-added producers, including companies widely known in the United States like Ferrari, Lamborghini, Maserati, and Ducati, which use networks of small businesses to supply their inputs.

This general framework of activist government support for small business forms the policy context for the employee ownership.

The legal framework

Employee-owned companies in Italy fall under the general cooperative law that covers agricultural cooperatives, fishing co-ops, housing co-ops, consumer co-ops, and credit unions as well as employee-owned businesses.

With the restoration of democracy in Italy after World War II, parliament gave formal recognition to the role of cooperatives. Article 45 of the Italian Constitution (1947) states: “The Republic recognizes the social function of cooperation characterized by mutual aid and not private profit. The law promotes and favors the growth of these structures using the most appropriate means and guarantees that their character and purpose will be inspected accordingly.”

The Basevi Law of 1947 -- Italy’s basic co-op law -- fleshed out this constitutional recognition. It provided co-ops with special tax treatment to encourage their self-capitalization by creating the concept of “indivisible reserves” for the benefit of all (i.e., future generations of employees and the community). Earnings could be contributed to indivisible reserves tax free (saving 40% in taxes), but if the co-op dissolved or sold, its reserves by law went to another cooperative or to a cooperative federation, rather than being distributed among the members. Members received their returns in annual interest payments on their membership fees and in patronage dividends.

Curiously, the law extended the same advantages to co-ops in which all employees were members and those in which only a minority of employees were members provided members owned 100% of the business. As a consequence, some employee co-ops have a very low level of inclusion of employees as members

Cooperatives provided for members’ control through an annual meeting that reviews financial results, approves the budget, and makes decisions on distributions; and through an election of the board every third year.

There have been three major changes in co-op laws since 1947.

In 1991, “social cooperatives” were formally recognized with special goals and special tax advantages. Those are discussed below.

In 1992, co-op law was changed to require all cooperatives to contribute 3% of their profits to co-op development funds run by the three federations of cooperatives. These funds, discussed below, are earmarked for starting new cooperatives or growing existing cooperatives.

In 2001, the right-wing Berlusconi government in Rome staged a frontal legislative assault on the co-ops which all the co-op federations fought. The result was a compromise: tax advantages for co-ops were reduced and scaled to the proportion of employees or consumers who belonged as members. Contributions to indivisible reserves are now 70% tax exempt for co-ops that do at least 50% of their business with members; those that do less are now only 30% tax exempt. Not surprisingly, this has encouraged employee co-ops to enroll at least 50% of their employees as members.

In the last fifteen years, co-ops of all sorts have doubled their importance in the Italian economy. Today 121 of the 1400 largest Italian firms are cooperatives or 9%, up from 4%, and employment have doubled from ½ million to 1 million.

Employee cooperatives

The traditional employee-owned cooperative in Emilia Romagna is the artisan-style production cooperative that has grown into a significant business. Some were established to deal with shutdowns; others, with lockouts; others (particularly in construction), from craftsmen pooling their tools; and others, by benevolent management. The oldest we visited was set up in 1874; the newest was from the 1980s.

These employee co-ops have succeeded first in the local or regional market, then the national, and now the global market largely because of their focus on competitiveness and innovation. As in American employee-owned firms, competitiveness frequently stems from a niche – varying from short run, quick set up at ***Zappettificio Muzzi***, an agricultural implement part producer, to design and quality excellence at ***Cooperativa Ceramiche d'Imola***, Italy's 5th largest ceramics company, to technological leadership at ***Societa Cooperative Bilanciai***, one of Europe's leading scale producers which plows a remarkable 7% of revenues back into R& D in an otherwise mature industry. Occasionally, the competitive strategy is one of size and economies of scale, as it is for some of the Italian consumer co-ops like ***Coopitalia,*** Italy's largest retailer; this is the strategy of employee-owned ***CIR Foods,*** the country's third largest food service provider.

Employee ownership is itself seen as a competitive advantage. "The gift of the cooperative is to create a sense of collective entrepreneurship. Membership requires thinking about the business. Workers are more committed than in private firms," says Stefano Bolognesi, CEO of Cooperativa Ceramiche d'Imola,. "If that weren't true, I wouldn't have accepted the presidency."

The employee co-ops are 100% membership owned and operate with a membership-elected board that serves a three year term. In addition to the legally required annual membership meeting to review the annual financial report and budget, the co-ops we visited had quarterly or monthly membership meetings, and one provided small group meetings to review the financial report and budget before the membership meeting.

They varied tremendously requirements for membership: from six months' service and a $3000 membership fee to five years' service and a $112,000 membership fee. Not surprisingly, the proportion of employees who are members varies as well – from 172 members of 1350 employees at Cooperativa Ceramiche d'Imola to 230 of 265 at Bilanciai.

While Italian co-op experts describe employee co-ops as being "by definition undercapitalized," their tax-free "indivisible reserves" build over time into substantial permanent equity that dwarfs membership fees. Bilanciai, which became a co-op in 1963, for instance, has membership fee accounts of $1 million and indivisible reserves of $12 million. The indivisible reserves were universally seen as an advantage.

"Part of our mission is intergenerational mutuality. What we see here is the fruit of generations of work," says Cooperativa Ceramiche's Bolognesi, a third generation co-op member. "We receive wealth from past generations [his co-op was set up in 1874], and we create it for future generations of members. Our objective isn't just to generate jobs for this generation but also for future generations."

Some of the older and better financially consolidated co-ops have expanded internationally through setting up holding companies in which the co-op owns a majority share with financial partners owning minority positions. The holding companies then owns the foreign subsidiaries and, sometimes, Italian non-cooperative subsidiaries as well. Bilanciai has become a major European player in this way, winning 34% of the European Union's truck scale market. Occasionally the employee co-op controls a public company; for example, the 8000-employee ***Manutencoop,*** a facilities management and janitorial cooperative, own 70% of each of three public companies in the same field, and they use funds raised on the stock exchange to finance their business.

Curiously, there seems little pressure from the co-op membership to convert subsidaries outside Italy into co-ops.

Employee co-op wages generally match the industry standard, because the co-ops are covered by the general industry-wide wage agreements that cover the private sector. Members receive both interest on their membership fee (typically about 9%) and "patronage dividends" annually. "Patronage dividends" are based on member labor input into the business, are frequently equal for all members, and varied from the equivalent of 1 to 4 months' salary in the co-ops we visited.

Managers, however, make less than the market - typically 75-80% of what they would make in comparable private sector jobs. Consequently they are largely recruited from within – – 80-90%. "You earn less money," says Bilanciai President Luciano Diacci, who came from the company's engineering staff, "but have more satisfaction, more job security, and a real sense of belonging."

Social cooperatives

The rapid growth in employee ownership in Italy in the last twenty years has been in the social cooperative sector.

Like most of the rest of the West, Italy has undergone an extensive debate about the role of government in providing public services. While the rapid Italian recovery and economic growth after World War II was driven by a very large state sector, in recent years Italy has moved farther than most other Western countries in seeking to privatize public services.

Unlike most of the rest of the West, however, Italy has done it with cooperatives. In Bologna, depending on whom you talk to, 60 - 85% of privatized social services are provided by social co-ops. Throughout Italy social co-ops employ 60,000 and account for 13% of social service expenditures. Their goal: to promote the public interest outside state sector.

There are two basic types of social co-ops. Type A is owned by the employees and provides social services to the usual social clients. Type B is owned by the members and also provides gainful employment for the marginalized, who must comprise at least 30% of members. Type B co-ops are similar to American non-profits which employee the hard-to-employ – handicapped, former substance abusers, etc. The difference is, in the Italian case, that the hard-to-employ have an ownership share in the business. They have additional tax advantages as well.

Social co-ops have low membership fees, typically $1000 or so, and short probationary periods. Wages meet private sector standards because of the industry-wide bargaining agreements, but are typically below wages paid previously to public sector employees to perform the same work – even after patronage dividends are added in.

They are often more political than the traditional employee co-ops. The strongest ideological motivation we heard was at ***CADIAI***, a Type A, 800 employee (including 420 members) diversified social care provider of home care, child care, residential care, and nursing home care services to 4,000. CADIAI's goals are to "improve and ensure the quality of personal care, and affirm the professional content and social value of care workers." Its founders specifically sought to legalize their grey-market jobs, supported women's rights including that to divorce (then contested in Italy), were strongly anti-clerical, and overtly "red" in their politics.

Similarly a Type A research cooperative, ***Centro di Ricerca sul Cancro*** (Center for Research on Cancer), which is incongruously located in a 16th century castle, did pathbreaking work on the industrial carcinogin benzine forty years ago. Now its researchers -- 35 employee members -- are analyzing the impact of electro magnetic fields and cell phones on health.

"You can wish to have a better world, but it's hard to build one," says CRC scientific director Dr. Morando Soffritti. "Our cooperative form gives us real freedom as a research institute: It allows us to be genuinely independent, to research freely and to speak freely."

The Type B co-op we visited was ***Giovani Rilegatori***, a co-op print shop set up in the early 1980s to do printing for other co-ops, which transformed itself in the 1990s into a Type B social coop. In addition to its professional printing of co-op annual reports, it provides work for the handicapped by taking in low skill, labor-intensive print work and by adding light assembly work. While we visited, several severely handicapped workers were putting together seat adjustment levers for Alfa Romeo. This co-op has 17 working members, 45% in the disadvantaged category. It recently moved to a modern industrial park, its building purchased with a 50 year, 2% interest loan from Imola's local development fund.

It's hard to beat – if you believe in an ownership society for those who otherwise are left out of ownership like unskilled women in home health care and the disabled.

Achieving economies of scale

Unlike the United States where the traditional cooperatives – agricultural cooperatives like Land of Lakes, mutual insurance companies like Nationwide, rural electric cooperatives, and credit unions – are completely separate from the employee-owned sector, in Italy the agricultural, financial, and consumer co-ops and the employee-owned companies are organized in the same associations. There are three main cooperative federations: the left-wing Legacoop, which is the largest group; the significant Catholic Confcooperative; and a far smaller Republican/Social Democratic group. While the political labels still have some residual meaning, they have lost their Cold War importance, and some of the co-ops belong to both the left-wing and the Catholic federations.

Each federation brings together employee-owned, consumer-owned, and agricultural producer-owned firms. This unity across sectoral lines has been useful for building second-tier cooperative structures.

The strength of the Italian co-ops stems largely from their creation of secondary co-ops, or "cooperation among co-ops." Like the Mondragon co-ops in Spain, they have set up financial institutions; insurance companies; and joint training, research, and development centers.

Co-op federation services. The three main cooperative federations provide many services to their members. The Legacoop, for example, provides tax preparation, accounting, payroll and legal services; training and development; occupational health and safety consulting; collective bargaining; waste disposal; and lending and equity investment from its development fund. It also charges a hefty 4/10 of 1% of sales for membership.

Because the Federations have regional, provincial and often even municipal associations, these services are provided locally and controlled locally.

Financial services. We visited Unipol, the insurance company, which was set it up in 1963 by a group of Bologna co-ops to insure their members. Today it is Italy's 3rd largest insurance company, and a major source of investment in the cooperative sector through the placement of its reserves there. It took over a small co-op bank in 1998, which it grew from 9 branches to 273 branches today and set up a merchant bank in 2003.

Collaboration on specific projects. Employee cooperatives collaborate extensively on specific business projects. Thus, for example, CADIAI is partnering with CIR, the food service co-op, and several other co-ops to build day care centers – managed by CADIAI with food provided by CIR. And CIR is backing the opening of Colors, the co-op restaurant set up by the employee survivors of Windows on the World in the World Trade Center.

Co-op development funds. Since 1992, 3% of profits of co-ops have been allocated to cooperative development fund to finance starting new cooperatives, conversion of existing businesses to co-ops, and the expansion of current cooperatives. Each of the three big co-op association has its own fund.

We visited with the management of Legacoop's fund – Coopfond. As of 2004, it had raised about $290 million and had invested about $340 million. Additionally, Coopfond has 14 regional funds. The other two national cooperative associations have smaller funds. Unaffiliated coops' contributions go into a government fund for the same purpose.

Between 1994 and 2001, Coopfond supported 109 co-op start ups with $48 million in equity and $17 million in loans leveraging $288 million in investment and creating 4640 new jobs. It also supported 82 expansion projects with $53 million in loans, leveraging $370 million in co-op investments and creating 2690 new jobs. That's not a bad record.

Imagine, if you will, the implications in Ohio if each employee-owned firm paid 3% of its profits into a fund to encourage the development of additional employee-owned firms in the state.

Challenges

Emilia Romagna faces the same challenges of globalization that the rest of us do. It has to compete against low income producers in Asia. “We have to play the quality game, innovating in products and processes,” says regional finance minister, Flavio del Bono, who was elected on the “Daisy slate,” a center-left Christian Democratic group, which is part of the leftist coalition government of the region.

“We can’t compete in every area, and we certainly can’t compete on price with the Chinese. But we can sell to the top 3% of Chinese consumers who have an income at the Italian level,” says del Bono. “That’s 30-40 million people. We can compete in ceramics, for example, and that’s why we’ve opened an office in China to help our firms export.” Again it’s an example of the way the regional government helps small firms achieve economies of scale.

While del Bono is reasonably sanguine about the ability of local firms to compete internationally, he is concerned that “foreign firms investing in Emilia Romagna have apparently reduced innovation.” This is a major concern because the region’s competitiveness in a global economy depends on continued innovation reflected in its extraordinary record in patents (30% of Italy’s patents for 7% of its population). Employee cooperatives provide an edge: “Co-ops are tough for foreign firms to purchase,” he says, since their “indivisible reverses” automatically revert to the various co-op development funds.

Partly to stay on the cutting edge of innovation, the regional government is providing the fiber-optic backbone for the entire region.

Internally, employee co-ops focus on a different set of challenges. A major one is inclusion of foreign workers. Italy is awash in foreign workers from Eastern Europe, the Balkans and North Africa. Some are legal; many are not. They also make up an increasing portion of co-op employment: 10% at CADIAI, for example, up from none three years ago. But they lack the co-op tradition. Though immigrants make up 30% of workers at the agricultural implement parts co-op we visited, none are members.

A second is the challenge of making large size compatible with democratic structure. From an American perspective, the Italian co-ops have dealt well, but it remains an issue of concern, especially in the consumer co-ops which have had to federate to remain competitive.

A third, and perhaps most serious, has been a sea change in values. As Guiliano Poletti, the national president of Legacoop, put it, “We teach children in school about coops, but today’s “get rich quick” values conflict with those that made cooperatives strong.”

What can we learn?

There are a number of lessons for Ohio policy makers and the employee-ownership community in Emilia Romagna that we should take to heart.

Promotion of small business. The regional government's focus on promoting small and medium-sized enterprises through creating economies of scale for them goes far beyond what we are used to in Ohio. The industrial sector service centers appear to have had a tremendous impact on clustering of businesses, flexible manufacturing, innovation, and exports. Small business organizations, including the various cooperative associations, provide additional services -- especially inexpensive professional services -- to their members. The consequence: higher wages in the small business sector, more patents and innovation, more employment growth, and more exports.

Access to capital. Much of the strength of the Emilia Romagna model stems from access to capital from large pools dedicated to cooperative development. Consider the insurance company Unipol. Established and controlled by other cooperatives, Unipol has strengthened the cooperative sector through its investment policies, and through its pioneering work in social accounting as well as through underwriting insurance for cooperatives and their members. Or consider the co-op development fund structure which "taxes" otherwise tax-advantaged co-ops to develop new co-ops seems to be an effective mechanism both to create new co-ops and new jobs.

Not least, the Italian co-operatives' "indivisible reserves" – which revert to the co-operative development funds at the sale or liquidation of cooperatives -- give them a staying power that American cooperatives and employee-owned businesses lack. They pay out part of the profits to members, but not their tax-advantaged retained earnings which guarantee that the capital created with tax advantages benefit future generations and the community. We basically turn those tax advantages into pensions for the current generation of employees.

Cross-sectoral collaboration between cooperatives – consumer-owned, agricultural producer-owned, and employee-owned firms – strengthens all three groups, especially through the provision of common services for their members. The cooperative councils at the regional, provincial and municipal levels give co-ops an independent voice in decision making, especially in the privatization of social services.

Imagine, for a moment, a similar model in Ohio. Imagine a state government with a proactive strategy of encouraging the development of small business and creating economies of scale in export, research and development, and provision of professional service through sectoral service centers as a centerpiece for economic development. Imagine that capital was pooled for starting and expanding employee-owned companies and that mutual insurance companies put a substantial portion of their placements back into growing the employee-owned and cooperative sectors. Imagine that employee-owners' investment of sweat and capital were anchored in the community for a longer term. And imagine cross-sectoral collaboration between farm co-ops, credit unions, mutual insurance companies like Nationwide, and employee-owned companies that strengthened them all.

Imagine, in short, that employee-owned companies in Ohio were not individually islands unto themselves but part of a larger whole.

John Logue is director of the Ohio Employee Ownership Center and professor of political science at Kent State University. *Thanks to Bob Giel and the Cooperative Charitable Trust for initiating and supporting the study tour; to Matt Hancock and Bruce Herman for setting up the visits; to Hancock for his suggestions on improving this piece; and to our Italian hosts for their the openness in discussing their experience. For a more extensive version of this article, see www.kent.edu/oeoc/*

John Restakis of the British Columbia Co-operative Association organizes an annual trip to Emilia Romagna. He can be contacted at restakis@bcca.coop.

words: 4116