THE LAWS REGULATING CO-OPERATIVE BANKS AND THE CONTRIBUTION TO ECONOMIC GROWTH AND POVERTY ALLEVIATION IN SOUTH AFRICA

by

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ABSTRACT

The world, more especially countries in Africa are battling with the effects of poverty, unemployment and destitution. South Africa is one African country that succumbed to racial inequality brought about by apartheid wherein black people were denied participation into any form of income generating endeavours that would ensure their sustenance. The South African Government after attaining independence in 1994 put in place policies meant to emancipate and empower the Historically Disadvantaged People (HDP). In line with that approach, the government deemed it fit to empower the South African populace through Co-operatives. This study analyses and critiques the Co-operative Banks Act, 40 of 2007 as the focal instrument regulating financial co-operatives in South Africa and its contribution towards economic growth and poverty reduction. The study further exposes some of the imminent challenges experienced in the field of financial co-operatives as far as registration of such co-operatives is concerned. The Act since its inception has only managed to have only two co-operative banks established and the rest of the Co-operative Financial Institutions (CFI's) are not registered and are operating under an exemption notice. Therefore, this study brings to light some of the challenges leading to the failure to become co-operative banks, and also delves into the act itself to assess whether its provisions are the reason for this ultimate failure to register financial co-operatives. The challenges experienced by financial co-operatives in South Africa would be addressed by drawing lessons from countries such as Kenya and Canada which have managed to establish a strong and vibrant co-operative industry so as to suggest ways in which they may also improve and graduate to become successful Co-operative Banks.

DECLARATION

I declare that this mini-dissertation hereby submitted to the University of Limpopo, for the degree of Master of Laws (LLM) in Development and Management Law has not been previously submitted by me for a degree at this or any other university; that it is my own work in design and execution, and that all material contained herein has been duly acknowledged.

Gundani, SR (Mr) **Date**

DEDICATION

This mini dissertation is dedicated to my beloved parents, Patricia and Davies Gundani for their unwavering support and believing in me since birth. My gratitude for their sacrifices and undying love goes beyond words.

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This journey would not have been easy without the spiritual guidance I received from my church, University of Limpopo Assemblies of God Movement, their teachings allowed me to persevere.

LIST OF ABBREVIATIONS AND ACRONYMS

BBBEE	Broad-Based Black Economic Empowerment
CBDA	Co-operative Banks Development Agency
CFI	Co-operative Financial Institution
DoA	Department of Agriculture
DTI	Department of Trade and Industry
EU	European Union
GDP	Gross Domestic Product
ICA	International Co-operative Alliance
ILO	International Labour Organisation
NASASA	National Stokvel Association of South Africa
NGO	Non-Governmental Organisation
SACCO	Savings and Credit Co-operatives Societies
SAMAF	South African Micro-Finance Apex Fund
UN	United Nations
WOCCU	World Council of Credit Unions

LIST OF INTERNATIONAL STATUTES

Kenya Savings and Credit Cooperative Organization (SACCO) Societies Act of 2008

Canadian Banks Act S.C. 1991, c. 46

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Broad – Based Black Economic Empowerment Act 53 of 2003

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Co-operatives Societies Act 28 of 1922

Land Act 18 of 1936

Land Settlement Act 12 of 1912

Natives Administration Act 38 of 1927

Public Finance Management Act 1 of 1999

CHAPTER ONE: INTRODUCTION

1.1 Historical background to the study

The Co-operative movement in South Africa has been existent even before the advent of apartheid. Historically, the movement can be traced back to the start of the 19th century when farmers began to formulate agricultural societies in the four colonies of Natal, Cape Province, Transvaal and the Orange Free State.[1] A plethora of legislative frameworks and co-operatives that emerged during that period were not in compliance with the international co-operative principles. For instance, the 1922, 1937 and 1981 Co-operative legislations did not promote, nor encourage co-operatives to abide by the seven international co-operative principles.[2]

The co-operative sector began with the formation of the predominantly white agricultural co-operatives which were intended to develop and build the white farming community. These co-operatives ultimately established themselves into powerful business ventures which monopolised agricultural production, marketing and processing in rural areas[3]. In 1892, the earliest co-operative was established which was called the Pietermaritzburg consumer co-operative in the colony of Natal[4]. During that period co-operatives garnered Governments support and were incentivised through legislative frameworks and other means. In 1912, the Land Bank was established to give the newly formed co-operatives financial support to carry out their activities. The Bank extended loans to agricultural co-operatives at preferential rates and under less stringent conditions than commercial banks.[5]

In terms of legislation the Government enacted the following Acts in a bid to promote co-operatives; these included the Land Settlement Act of 1912; 1913 and Land Act of 1936; Co-operatives Societies Acts of 1922 and 1939; and the Natives Administration Act of 1936. In the year 1922, the Co-operatives Societies Act became law and thereby invalidating all the previous legislations that had been

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[1] Van Niekerk. 1994. *Cooperative Theory and Practice*. Pretoria: SAAU pp. 17-18.
[2] Department of Trade and Industry. 2012. *Integrated Strategy on the Development and Promotion of Cooperatives.*
[3] ibid.
[4] See Van Niekerk, at 1 opcit.
[5] Ibid.

enacted and was the first act that controlled co-operatives in the former four provinces of South Africa.[6]

The government promoted black-owned agricultural co-operatives around 1970 and 1980 as part of the apartheid economic grand plans for the so called 'homelands'. However, such co-operatives did not receive adequate state support as compared to the white co-operatives. As a result, black co-operatives remained weak and under-developed, most of them ultimately failing. The 1981 Co-operatives Act further encouraged the registration of agricultural co-operatives, even those owned by black people.[7]

It was a deliberate policy of apartheid to refuse black people access to enter the retail trade and emancipate themselves, this was achieved by confining them in the townships and 'homeland' areas. Black communities attempted to construct consumer-type co-operatives such as buying clubs, through a *stokvel*[8] system, which enabled communities to buy goods in bulk and at wholesale prices; and also allowed them to arrange decent funerals for their loved ones.

The Stockvel Association of South Africa purports that, "Irrespective of the oppressive approach of the apartheid policies, there were at least 800 000 active *stokvels* in South Africa, with a total membership of approximately 10 million people, representing a strong and formidable economic force. The record of these *stokvels* has in itself been mixed; some collapsed due to conflict and fraud; however, many survived as models of communal trust, discipline and support, although they still remained informal".[9]

The promulgation of the new Co-operatives Act[10] brought about a series of registration of new co-operatives that was unprecedented in South Africa. The CIPC register records that, "19 550 new co-operatives were registered from 2005 to 2009 in various sectors, indicating a growth rate of 86%. Within a period of four years, the number of new co-operative registrations almost quadrupled the number of co-

[6] Ibid.
[7] Department of Trade and Industry. 2012. *Integrated Strategy on the Development and Promotion of Cooperatives.*
[8] Stokvels where mutual savings and credit schemes and burial societies.
[9] Stokvel Association of South Africa. 2006. Available online at http://nasasa.co.za/site/ accessed on 5/05/16.
[10] Act, No. 14 of 2005.

operatives that were registered over the previous 82 years (1922 – 2004). The bulk of these new co-operatives were black woman-owned. Youth-owned co-operatives have also begun to surface. However, most of these new entrants remain susceptible and are very weak and require high level of support".[11]

The Act then paved way for the enactment of the current Co-operative Banks Act[12]. The enactment of the Act enabled the establishment of the CBDA[13]. On the 15th of August 2008, in terms of section 58 of the Co-operatives Act, the Minister of Finance appointed 11 persons as members of the CBDA Board of Directors which would sit for tenure of two years; this was followed by the appointment of the existing board members[14]. The CBDA, is a schedule 3A public entity[15], which was created to support, promote and develop co-operative banks; accredit and regulate representative bodies; support organisations; and to supervise and regulate primary co-operative banks with deposits of R1 million to R20 million, and membership of at least 200.

The Act has been very fundamental towards regularising Cooperative Financial Institutions since its enactment in 2007; however challenges have been encountered with regard to the registration of co-operative banks. Since 2007, according to the South African Reserve Bank, only a total of two co-operative banks have been successfully registered. This shortcoming is exacerbated by the fact that the Co-operative Financial Institutions do not possess the required capital and also inadequate capital risk management. The challenges being experienced may be attributed to lack of awareness and lack of poor corporate governance by the spheres of government to offer the required support to co-operatives.

In other countries, co-operatives play a significant role in the economy and contribute immensely towards socio-economic growth and development. Internationally, statistics carried out by NEDLAC point out that, "countries which have achieved notable economic development also control a vibrant and dynamic co-operative sector, contributing significantly towards the growth of their economies. For example,

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[11] See Department of Trade and Industry at 7 opcit.
[12] Act 40 of 2007.
[13] Co-operative Banks Development Agency. 2016. Available online at http://www.treasury.gov.za/coopbank/ accessed on 5/05/16.
[14] Government Gazette No. 31336 dated 15 August 2008.
[15] Listed as a Schedule 3A public entity in terms of the Public Finance Management Act 1 of 1999.

in Kenya, co-operatives contribute 45% of the Gross Domestic Product (GDP) and 31% of the total national savings and deposits. Co-operatives control 70% of the coffee market, 76% of the dairy market and 95% of the cotton market. In New Zealand, 22% of the country's GDP is generated by co-operative enterprises. In addition, co-operatives are responsible for 95% of the dairy market and 95% of the export dairy market. They hold 70% of the meat market, 50% of the farm supply market, 70% of the fertiliser market, 75% of the wholesale pharmaceuticals and 62% of the grocery market. In Spain, the co-operatives movement produces more than €70 billion in turnover and the majority of these co-operatives are worker co-operatives".[16]

However, this is not the case in South Africa; this is because the government is failing to create a conducive environment for co-operatives to thrive by developing legislative instruments, supportive programmes and delivery institutions that grow rapidly and contribute positively to economic development, employment creation, economic ownership by local communities, and human resource development. Canada, Spain, Kenya, Italy, India and Bangladesh have proven to be successful in the development of co-operatives.[17]

The Co-operatives Act laid the foundation for the enactment of the Co-operative Banks Act[18] which was created to promote and advance the social and economic welfare of all South Africans by enhancing access to banking services under sustainable conditions. The Act aims to provide with a regulatory framework for the formation of Co-operative Banks, and protection of its members. It also goes on to set out the guidelines for the registration of such banks. The significance of the Act is to assist previously disadvantaged people with affordable loans and financial products. This would therefore go a long way towards revamping the economy and alleviating unemployment in South Africa.

The Co-operatives Banks Act therefore forms part of the Governments objective to achieve socio-economic growth and development as mandated by the South African Constitution[19] in the Bill of Rights in Section 27(2) which provides that, "the State

[16] NEDLAC Study Tour Report, 2004.
[17] Department of Trade and Industry. (2016). (online) www.dti.co.za accessed on 23/11/16.
[18] Act 40 of 2007.
[19] The Constitution of the Republic of South Africa, 1996.

must take reasonable legislative and other measures, within its available resources, to achieve the progressive realisation of the rights". Therefore a critical assessment has to be undertaken to evaluate the role that has been played by the Cooperatives Banks Act since its inception in 2007, on whether it is advancing socio-economic growth and development as one of its main aims. The Act must also be scrutinised to evaluate its contribution towards encouraging the participation of poor black people who had no access to banking services in the past, and also a comparison with Kenya and Canada to assess if there is need for improvement in South Africa's law on co-operatives.

1.2 Statement of the Research Problem

The majority of people in the world are succumbing to the ravages of poverty and hunger and this is a global concern that also affects South Africa. It is estimated that half of the world is living on less than two US dollars a day; therefore the reduction of poverty has become a prime goal to every country. This is turn has made the international campaign against poverty gain momentum, with various key players suggesting the use of different methods to reduce poverty. Wanyama states that there is an overall agreement among many players, which include, "the United Nations (UN), the International Labour Organization (ILO), the International Co-operative Alliance (ICA) and the European Union (EU)", that the co-operative business model is one of the few forms of organizations that may meet all proportions of poverty.[20]

The enactment of the Co-operatives Banks Act is to promote and advance the socio-economic development and growth of South Africa, but however the reality is that since the coming into operation of the Act only two co-operative banks have been successfully registered under the ambit of the Act, the rest are still operating as Co-operative Financial Institutions (CFI) under an exemption notice[21] and will continue to be regulated by the self-regulatory bodies as designated in terms of the existing exemption notices. Therefore, there are still challenges as far as the registration of the CFI's is concerned which dwindles the efforts to emancipate poor people and to contribute significantly to socio-economic growth.

[20] Wanyama, F., Develtere, P., Pollet, I. 2008. Encountering the Evidence: Co-operatives and Poverty Reduction in Africa. Working Papers on Social and Co-operative Entrepreneurship WP-SCE 08-02.
[21] Banks Act Exemption Notice No 620.

Since 2007, the Act has made an insignificant impact towards its goal of promoting socio-economic development in South Africa. The main reason is that most Cooperative Financial Institutions fail to meet the requirements of the Act to qualify for registration as Co-operative Banks. There has been relatively low public awareness and the people most affected by the Act are mainly poor black people who are illiterate and do not understand the procedures to meet the registration requirements. The majority of the challenges are encountered at local levels, since there is insufficient knowledge about the co-operative concept by the administrators themselves. In addition, agencies at national and provincial levels are also involved in supporting co-operatives and the total number of staff members responsible for overseeing co-operatives does not exceed 100[22], moreover the Registrar's office is situated in Pretoria, which makes it difficult for co-operatives to get registered, owing to the high cost of travelling.

The other main challenge has been failure to register owing to the strict requirements amongst these includes insufficient capital levels, insufficient risk management practices, and feeble government structures. All these factors have contributed to the failure of Co-operative Financial Institutions to register as co-operative banks, to date only two co-operative banks have registered under the Act.

1.3 Research Question

What contribution has the introduction of Co-operative Banks in South Africa made towards socio-economic development and growth especially towards the goal of alleviating poverty, and are there any challenges encountered since the introduction of the Act[23] to regularise such institutions?.[24]

1.4 Literature Review

The International Co-operative Alliance defines a co-operative as:-

[22]Ibid.
[23] Act 40 of 2007.
[24] Cooperative Financial institutions under the purview of the Cooperative Banks Development Agency.

"…..an autonomous association of persons united voluntarily to meet their common economic, social, and cultural needs and aspirations through a jointly owned and democratically-controlled enterprise".[25]

Co-operatives differ from joint-stock companies primarily in their governance; this is because in the case of a co-operative, voting rights are based on membership as opposed to the size of shareholding. Co-operatives also differ from philanthropic foundations in that they are set up to benefit the needs of their members rather than the needs of others. Therefore, there are several types of co-operatives and most of them focus on a particular economic sector, but others focus on the nature of membership. Major types include agricultural cooperatives, financial cooperatives, housing cooperatives, health and social care cooperatives, consumer cooperatives, and worker cooperatives.[26]

According to Satgar, he states that, "co-operatives exist under various guises in South Africa. Sometimes they are referred to as 'projects', 'self-help groups', 'mutual societies', 'village banks', 'credit unions' , 'consumer store' and sometimes even the word 'association' is used to describe cooperatives. Essentially, cooperatives are member-owned and democratically controlled institutions. They are not-for-profit in the sense that voting in a co-operative is not based on the number of shares owned but instead on the universal principle: one member, one vote".[27]

The field of Co-operative Financial Institutions has been in existence in South Africa for decades[28], the Co-operative Banks Act[29] was enacted to regularise such institutions. The Preamble of the Act clearly states that:

> "To promote and advance the social and economic welfare of all South Africans by enhancing access to banking services under sustainable conditions; to promote the development of sustainable and responsible co-operative banks; to establish an appropriate regulatory framework and

[25] Birchall, J. 2004. "Cooperatives and the Millennium Development Goals." International Labour Office, Geneva.
[26] Nair, A, Todd R.K. 2007. Reaching Rural Areas with Financial Services: Lessons from Financial Cooperatives in Brazil, Burkina Faso, Kenya, and Sri Lanka. Agriculture and Rural Development Discussion Paper 35.
[27] Satgar, V. 2007. The State of the South African Cooperative Sector. Executive Director of the Cooperative and Policy Alternative Centre (COPAC).
[28] See Van Niekerk at 1 opcit.
[29] Act 40 of 2007.

> regulatory institutions for co-operative banks that protect members of co-operative banks; to provide for the registration of deposit-taking financial services co-operatives as co-operative banks; to provide for the regulation and supervision of co-operative banks; and to provide for the establishment of co-operative banks supervisors and a development agency for co-operative banks; and to provide for matters connected therewith".[30]

According to the United Nations, the year 2012 was declared as the year of co-operatives and encouraged all member states and stakeholders to encourage them. Therefore, to ensure a success story in the co-operative sector, lessons from other countries must be taken into account to inform a proper strategy that will improve the co-operative sector.[31]

The co-operative industry has made great strides all over the world, and according to Sriram, "Canada has a well-established co-operative financial industry and the current menu of financial services include loan products for varying needs, banking services including checking accounts, term deposits, credit and charge cards, automatic teller machine counters and internet banking. Apart from banking, Desjardins Movement is involved in insurance, marketing of mutual funds, investment services for individuals and corporates, brokerage services and international services including export and import financing, currency accounts, travellers cheques and so on".[32]

Regionally, countries like Kenya have also noted growth in their co-operative industry. The Ministry of Co-operative Development and Marketing in Kenya contends that, "Co-operatives have occupied a special place in Kenyan economy from pre-independence days with the first Co-operative society being registered in 1908".[33] The ministry further states that, "Kenya has a long history of co-operative development that has been characterized by strong growth, thus making a significant contribution to the overall economy. Co-operatives are recognized by the

[30] Act 40 of 2007.
[31] The United Nations. 2010. Available online at www.un.org.
[32] Sriram, M.S. Financial Co-operatives in Quebec, Canada: A Study of the Desjardins Movement. Indian Institute of Management, Vastrapur, Ahmedabad.
[33] Ministry of Co-operative Development and Marketing, Kenya. 2012. During The Enhancing Financial Innovation & Access (Efina) Forum. Abuja, Nigeria.

government to be a major contributor to national development, as cooperatives are found in almost all sectors of the economy".[34]

Co-operatives also play a significant role towards economic growth and poverty alleviation. According to Nair and Todd, "access to financial services contributes to rural development and poverty reduction in several ways. The ability to save and borrow aids consumption by enabling better management of cash flows and promoting income-enhancing and vulnerability-reducing investments. However, access to financial services continues to be limited in most rural areas in developing countries. Several factors that increase transaction costs and risk constrain access in rural areas. Factors increasing transaction costs include remoteness and poor infrastructure, lower demand for financial services arising from lower levels of income and economic activity, and small size of transactions".[35]

The main legislation to regularise cooperatives in South Africa is the Co-operatives Act[36] which was enacted to recognise the importance of co-operatives in South Africa. The Act states that, "a viable, autonomous, self-reliant and self-sustaining co-operative movement can play a major role in the economic and social development of the Republic of South Africa, in particular by creating employment, generating income, facilitating broad-based black economic empowerment and eradicating poverty".[37]

The role played by co-operatives in South Africa is very significant, and plays a major role towards eradicating poverty and unemployment. Co-operatives have been promoted in many developing countries as a mechanism for driving agricultural growth and rural development.[38] Philip contends that, "Financial Co-operatives are regarded as the third-tier of banking in South Africa and are made up of member-based financial institutions; across a spectrum that includes stokvels, burial societies, savings and credit unions, Village Banks, and Mutual Banks. While not all of these would define themselves as co-ops, many in fact meet the essential criterion

[34] Wanyama, F.O. 2009. Surviving Liberalization: the cooperative movement in Kenya. CoopAFRICA Working Paper No. 10.
[35] Nair, A, Todd R.K. 2007. Reaching Rural Areas with Financial Services: Lessons from Financial Cooperatives in Brazil, Burkina Faso, Kenya, and Sri Lanka. Agriculture and Rural Development Discussion Paper 35.
[36] Act 14 of 2005.
[37] Ibid.
[38] Nganwa, L. Ferrer, O. 2010. What will South Africa's new Cooperatives Act do for small producers? An analysis of three case studies in KwaZulu-Natal, Vol 49, No 1 (March 2010).

– of member ownership and control. Much has been made of the role and potential of stokvels as forms of 'rotating savings and credit' associations".[39]

The National Stokvel Association of South Africa (NASASA) estimates that, "there are a total of 800,000 *stokvels*, burial societies and rotating savings and credit associations in South Africa, with about 8.25 million members, and an estimated R400 million a month in savings. While NASASA's membership of 15,000 *stokvel*s is significant, the formalisation of a wider membership network of *stokvel*s has proved elusive, making accurate data hard to come by".[40] The statistics demonstrate the economic potential of financial cooperatives in South Africa, once given proper corporate governance, skills development and research.

Lyne and Collins add that, "The availability of dedicated support suggests that cooperatives will also play an important role in the management of community-owned resources acquired through land reform, including reforms planned for the country's communal areas. The Cooperatives Act explicitly targets black people in rural areas. This study questions the decision to dedicate public support to cooperatives when the interests of their members might better be served by other forms of organisation".[41]

Cooperatives have assisted many people in remote rural areas in Africa and Mpalwha supports this by stating that, "African intellectuals and leaders favour co-operatives to empower marginalised communities because; African society is ideally suited to working in cooperatives". He further states that, "South Africa's 2003 Presidential Growth and Development Summit endorsed special measures to support development-oriented cooperatives. Following this commitment, government responsibility for cooperatives was transferred from the Department of Agriculture (DoA) to the Department of Trade and Industry (DTI). The DTI drafted a new policy

[39] Philip, K. 2010. Co-operatives in South Africa: Their Role in Job Creation and Poverty Reduction. South African Foundation.
[40] ECIAfrica. 2003. Third Tier Banking Report: A Review of the capacity, lessons learned and way forward for member-based financial institutions in South Africa commissioned by the FinMark Trust: www.finmark.org.za.
[41]Lyne, M & Collins, R. 2008. South Africa's new Cooperatives Act: A missed opportunity for small farmers and land reform beneficiaries, Agrekon, 47:2, 180-197, DOI: 10.1080/03031853.2008.9523796.

on cooperatives and a Draft Bill that was gazetted in 2003; this bill was enacted in August 2005".[42] This regulatory instrument is called the Cooperatives Act of 2005.

The Finance Minister, Mr Pravin Gordhan in the 2010/11 Combined Report of the Supervisors of the Cooperative Bank Agency and the South African Reserve Bank stated that, "Co-operative banks should not be seen as an appendage to the current banking sector, but as an alternative in providing access to sound financial services. The effective implementation and enforcement of the Act, through increased registration of co-operative banks, should not only promote access to finance, but also support the economic and financial empowerment of communities. Organic growth of co-operative banks has the potential to increase effective participation of community members in the economy resulting from responsible member-based funding of new economic activities".

The Minister went on and pointed the challenges being faced currently by the sector, in his address he stated that, "The level and quality of member participation, the skills of members of boards of directors and managers, and general knowledge of co-operative principles are relatively low at present. The extent to which co-operative banks' financial outreach will improve over time, and the level of interaction between communities and the broader economic sectors will largely depend on the success of the CBDA in achieving the development objectives of the Act, and on the Supervisors' role in ensuring that registered co-operative banks are appropriately and effectively regulated and supervised".[43]

According to the Supervisors of the CBDA[44] in their 2010-11 report stated that, "In view of the developmental objectives of the Act, the Supervisors have not yet initiated the winding up of any co-operative that failed to apply for registration in terms of section 92(2) of the Act. There is currently close co-operation with the CBDA Capacity Building Unit and the self-regulatory bodies to ensure that the outstanding applications are received in due course".

[42] Mpalwha, M. 2005. Untitled keynote address by the South African Minister of Trade and Industry, National Cooperatives Conference, 14-15 March, Benoni, South Africa.
[43] Combined Report of the Supervisors of the Cooperative Bank Development Agency and South African. Reserve Bank, Forward by the Minister of Finance, 2010/11.
[44] Cooperative Banks Development Agency hereafter referred to as the CBDA.

The Supervisors also point out that, “until a clear policy decision has been taken regarding the future regulation of deposit-taking CFIs not registered as co-operative banks, either by not being approved for registration as a co-operative bank or not meeting the minimum criteria to apply for registration, such CFIs will continue to operate under exemption notices and will continue to be regulated by the self-regulatory bodies as designated in terms of the existing exemption notices”.[45]

These challenges are still being encountered presently, thus a way forward has to be put forward to allow for the registration of Cooperative Banks. Internationally Cooperative Financial Institutions play a pivotal role towards the socio-economic development of their countries. According to Phillip, “a few international case studies of co-ops have been selected to give some context to the debates taking place here. These include the Italian *Lega Nazionale delle* Cooperative (Legacoop) – which is the largest co-op federation in Italy, where co-ops are sufficiently influential in the economy to be defined as ‘the third sector’; the Mondragon Co-operative Corporation, in Spain – probably the most famous success story of all; the role of co-ops and ESOP’s in China’s transition economy; and the case of Kerala, in India”.[46]

According to the Department of Trade and Industry, “International studies reveal that countries which have created an environment conducive to promoting co-operatives, by developing legislative instruments, supportive programmes and delivery institutions, grow rapidly and contribute positively to economic development, employment creation, economic ownership by local communities, and human resource development. Canada, Spain, Kenya, Italy, India and Bangladesh have proven to be successful in the development of co-operatives”.[47]

1.4.1 Co-operative Legislative Framework

The Co-operatives Banks Act[48] is the main legislation regulating Co-operative Financial Institutions (CFI) which are willing to register as Co-operative Banks under the ambit of the Act. The Act lays all the fundamental requirements for registration, a CFI which fails to meet this requirements does not register as a Co-operative Bank.

[45] ibid
[46] See Satgar at 26 opcit
[47] See DTI at 7 opcit
[48] Act 40 of 2007

The Act clearly defines what a Co-operative Bank is[49], and goes further to highlight the fact that such institutions are meant to advance the socio-economic growth and development of the Republic. The Act provides that its main purpose is, “promote and advance the social and economic welfare of all South Africans by enhancing access to banking services under sustainable conditions”.[50]

The Act also contains provisions meant to promote efficiency and sustainability of co-operative banks. The Act provides for, “establishment of Supervisors to ensure appropriate and effective regulation and supervision of co-operative banks, and to protect members and the public interest; and the establishment of a Development Agency for Co-operative Banks to develop and enhance the sustainability of co-operative banks”.[51] The provision led to the establishment of the Co-operative Banks Development Agency (CBDA), which has the primary responsibility of overseeing all co-operative banks in the Republic to ensure compliance, and proper registration of such banks.

1.5 Aim and Objectives of the study

- This mini-dissertation is aimed at analysing the state and nature of Co-operative Banks in South Africa and challenges in the application of the Co-operative Banks Act[52] as a tool to drive socio-economic development and growth in South Africa.
- It will go further to pave a way forward and provide solutions to allow for the registration of more Cooperative Banks in South Africa by relaxing the regulations imposed by the Cooperative Banks Act on Cooperative Financial Institutions, which are making it difficult for them to register.
- The mini-dissertation will also expose the economic potential of Cooperative Banks once effective and applicable legislation is put in place as a powerful

[49] Section 1(1) of Act 40 of 2007, which provides:
‘‘co-operative bank’’ means a co-operative registered as a co-operative bank in terms of this Act whose members—
(a) are of similar occupation or profession or who are employed by a common employer or who are employed within the same business district; or
(b) have common membership in an association or organisation, including a business, religious, social, co-operative, labour or educational group; or
(c) reside within the same defined community or geographical area.
[50] Section 2(a) of Act 40 of 2007.
[51] Section 2(c)(ii) and (iii) of Act 40 of 2007.
[52] Act 40 of 2007.

drive for development in South Africa by providing with employment, alleviation of poverty and increased participation of Historically Disadvantaged South Africans (HDSA) in the commercial business sector.

- The study will also make a comparison with other jurisdictions on how they regularise Cooperative Banks to ensure maximum output. Clear examples have already been set by countries like Kenya, Canada and also how the Government may assist the slowly developing industry.

1.6 Research Methodology

The research methodology used in this study is qualitative as opposed to quantitative. This research is library based and reliance is on library materials such as textbooks, reports, legislations, regulations, case laws and articles. Consequently, a combination of legal comparative and legal historical methods, based on jurisprudential analysis was employed. A legal comparative method was used to find solutions, especially on how other jurisdictions regularise co-operatives in order to achieve economic growth and development.

1.7 Scope and Limitation of the study

The mini-dissertation consists of five chapters, chapter one will be an introductory chapter which is an overview of the whole study. Chapter two will deal with legislative and policy frameworks. Chapter three will deal with issues and challenges meanwhile, chapter four deals with comparative study with other jurisdictions. Finally the last chapter will deal with conclusions drawn from the whole study and make some recommendations.

CHAPTER TWO: LEGISLATIVE AND POLICY FRAMEWORKS

2.1 Introduction

This chapter will deal with legislative and policy frameworks in South Africa that regulate the institution of co-operatives, especially cooperative banks. The socio-economic contribution of co-operatives has led to the promulgation of specific Acts that govern and control co-operatives to ensure that they reach their full potential. Therefore this section will analyse such acts and the regulations issued in respect of co-operative banks in South Africa.

2.2 Co-operatives Act

The Co-operatives Act[53] was promulgated to regularise the registration and management of co-operatives in South Africa. It further provides with a platform for black owned co-operatives including women and youth to get involved with the co-operatives.

The Act[54] states that it is meant to:

- "ensure that international co-operative principles are recognised and implemented in the Republic of South Africa;
- enable co-operatives to register and acquire a legal status separate from their members; and
- facilitate the provision of targeted support for emerging co-operatives, particularly those owned by women and black people".[55]

The Act also provides with the co-operative principles[56] that every co-operative must comply with in South Africa. This provides with uniformity as far as the code of

[53] Act 14 of 2005.
[54] Ibid.
[55] Preamble of Act 14 of 2005.
[56] Section 3(1) of Act 14 of 2005, which provides:
For the purposes of this Act, a co-operative complies with co-operative principles if—
(a) membership of that co-operative is open to persons who can use the services of that co-operative and who are able to accept the responsibilities of membership;
(b) in the case of a primary co-operative, each member has only one vote;
(c) to the extent feasible, members provide the capital required by that

practice for co-operatives in the whole Republic is concerned, and this allows for co-operatives to align their policies with that of the Act, and Section 3(1) (f) states that one of the principles is to provide training and education, which allows upcoming co-operatives to at least have an understanding of how to operate a cooperative, when it comes to deposits and investments in the case of a financial cooperative.

The Act also specifies the forms of co-operatives that may be registered in the Republic[57] and further outlines the kind of co-operatives[58] that exist in South Africa, which means that it is the main legislative framework regulating co-operatives. Therefore people have a choice when it comes to the form and type of co-operative they wish to register, for as long as they comply with the statutory requirements for the type of co-operative they wish to register.

The Act further states that, “the registrar must register a co-operative and issue a certificate of registration with a registration number, if the registrar is satisfied that the application has been made in accordance with this Act; the constitution of a co-operative complies with this Act and with the co-operative principles referred to in section 3; and the proposed name of that co-operative complies with section 10”.[59] The effect of such registration means that the co-operative assumes legal personality on the day of registration, and the registration certificate is issued.

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co-operative;
(d) the return paid on member capital is limited to the maximum percentage fixed
in accordance with the constitution of that co-operative;
(e) at least five per cent of the surplus is set aside as a reserve in a reserve fund and
is not divisible amongst its members.
(f) it provides education and training to its members and employees

[57] Section 4(1) of Act 14 of 2005, which provides:
This Act provides for the registration of the following forms of co-operatives:
(a) a primary co-operative;
(b) a secondary co-operative; and
(c) a tertiary co-operative.

[58] Section 4(2) of the Act further provides:
Without limiting the number and variety of different kinds of co-operatives, a
co-operative registered in terms of this Act may be, but is not limited to, a—
(a) housing co-operative;
(b) worker co-operative;
(c) social co-operative;
(d) agricultural co-operative;
(e) co-operative burial society;
(f) financial services co-operative;
(g) consumer co-operative
(h) marketing and supply co-operative; and
(i) service co-operative.

[59] Section 7 of Act 14 of 2005.

Therefore a co-operative has rights and duties, meaning it may enter into contacts and sue or be sued in its own name.

A duly registered co-operative must have a constitution.[60] The Act specifies that, “The constitution of a co-operative must include the name of the co-operative; whether it is a primary co-operative, a secondary co-operative, or a tertiary co-operative; the main objectives of the co-operative; a description of the business of the co-operative, including any restrictions on the business of the co-operative; a provision stipulating that each member has one vote in all meetings of the co-operative except in the case of secondary or tertiary co-operatives; the minimum period of notice of general meetings; the place where the registered office of the co-operative is located; the minimum and maximum number of directors”.[61] These are just some of the aspects to be contained in the constitution of the co-operative, which must comply with Section 14.

2.3 Co-operative Banks Act

The Cooperatives Banks Act[62] is the main legislation regulating Co-operative Financial Institutions (CFI) which are willing to register as Co-operative Banks under the Act. The Act lays all the fundamental requirements for registration, a CFI which fails to meet this requirements does not register as a Co-operative Bank. The Act clearly defines what a Co-operative Bank is[63], and goes further to highlight the fact that such institutions are meant to advance the socio-economic growth and development of the Republic. The Act provides that its main purpose is to, “promote and advance the social and economic welfare of all South Africans by enhancing access to banking services under sustainable conditions”.[64]

[60] Section 13(1) of Act 14 of 2005.
[61] Section 14(1) of Act 14 of 2005.
[62] Act 40 of 2007.
[63] Section 1(1) of Act 40 of 2007, which provides:
‘‘co-operative bank’’ means a co-operative registered as a co-operative bank in terms of this Act whose members—
(a) are of similar occupation or profession or who are employed by a common employer or who are employed within the same business district; or
(b) have common membership in an association or organisation, including a business, religious, social, co-operative, labour or educational group; or
(c) reside within the same defined community or geographical area.
[64] Section 2(a) of Act 40 of 2007.

The Act also contains provisions meant to promote efficiency and sustainability of co-operative banks. The Act provides for the, "establishment of Supervisors to ensure appropriate and effective regulation and supervision of co-operative banks and to protect members and the public interest; and the establishment of a Development Agency for Co-operative Banks to develop and enhance the sustainability of co-operative banks".[65] The provision led to the establishment of the Co-operative Banks Development Agency (CBDA), which has the primary responsibility of overseeing all co-operative banks in the Republic to ensure compliance, and proper registration of such banks.

The Co-operative banks Act applies to, "co-operative banks registered under this Act and to any co-operative registered under the Co-operatives Act[66] that takes deposits and has 200 or more members; and holds deposits of members to the value of one million Rand or more".[67] This means that any co-operative that meets the above criteria qualifies to register under the Act. The section further provides that, "such a co-operative bank must apply for registration within 2 months after meeting the criteria in section 3(1) (a) and (b). The Act also acknowledges the application of the Co-operatives Act[68] unless the application of a provision thereof has specifically been excluded or amended in this Act. It however also states that in the case of inconsistency between the two acts, the Co-operative Banks Act prevails".[69]

The Act also lays some strict requirements for registration, firstly that a potential co-operative bank must demonstrate to the Supervisor that the business it proposes to conduct is that of a co-operative bank of the type to which the application relates[70] and this means that the mission statement of the co-operative bank must be clear to the satisfaction of the Supervisor of co-operative banks. The Act further states that the co-operative bank must also prove that it has sufficient human, financial and operational capacity to function efficiently and competently as a co-operative bank.[71]

[65] Section 2(c)(ii) and (iii) of Act 40 of 2007.
[66] Act 14 of 2005.
[67] Section 3(1) of Act 40 of 2007.
[68] Act 14 of 2005.
[69] Section 4(2) of Act 40 of 2007.
[70] Section 7(a) of Act 40 of 2007.
[71] Section 7(b) of Act 40 of 2007.

The Act also stresses the importance of training stuff so that they know and understand the complex way in which the banks operate, it states that every person that is to be a director, managing director or executive officer of the proposed co-operative bank has the necessary experience, knowledge and qualifications to operate the proposed co-operative bank[72] and is a fit and proper person.[73]

The Co-operative Banks Act also provides with instances whereby the Supervisor may de-register or suspend a co-operative bank. The Supervisor must be satisfied that the co-operative bank has failed to commence operations 6 months after the date of registration. It further provides that it was to be de-registered if it has ceased to operate and has not, for a continuous period of three months, met the criteria referred to in section 3(1)[74] and is unlikely to meet the criteria in the future. The Act further states that de-registration would also occur if the co-operative bank obtained registration through fraudulent means, and failed to comply with a provision of this Act or the Co-operatives Act.[75] Therefore if a co-operative bank is under one or all the circumstances above, the Supervisor has to de-register or suspend it.[76]

The Act, in section 14 also outlines the banking services that are provided by co-operative banks. The services that a co-operative bank undertakes includes, "taking deposits from its members and also open savings accounts in the name of each member into which that member may deposit or withdraw money. It further states that the bank may borrow money from the Agency and members, other than deposits referred to in paragraph (a), up to a percentage of the assets held by it as prescribed by the Minister. The Co-operative bank also has to open a savings account or

[72] Section 7(c) of Act 40 of 2007.
[73] Section 9 (1) defines fit and proper person as:
The supervisor may, for purposes of assessing whether a director, managing director or executive officer of a proposed co-operative bank is a fit and proper person, have regard to—
(a) the competence and soundness of judgment of the person for the fulfilment of the responsibilities of the particular office and class of co-operative bank;
(b) the diligence with which the person concerned is likely to fulfil those responsibilities;
(c) previous conduct and activities of the person in business or financial matters.
[74] Section 3(1) provides that:
This Act applies to all co-operative banks registered under this Act and to any co-operative registered under the Co-operatives Act that takes deposits and—
(a) has 200 or more members; and
(b) holds deposits of members to the value of one million Rand or more.
[75] Act 14 of 2005.
[76] Section 11(1) of Act 40 of 2007.

cheque account in the name of that co-operative bank with any banking institution. It may conduct any additional banking services as may be prescribed by the Minister, as well as investments".[77]

The Co-operative Banks Act also specifies the duties of directors. The duties of directors are derived from common law which dictate that they must act in good faith and with due diligence and skill. The Act provides that, "directors, managing director and executive officer of a co-operative bank must be appointed in accordance with the conditions provided for in the constitution of such co-operative bank, Section 13 of the Act states that every co-operative bank must have a constitution. Each director, managing director and executive officer of a co-operative bank owes a fiduciary duty and a duty of care and skill to the co-operative bank of which such a person is director, managing director or executive officer; must act *bona fide* for the benefit of the co-operative bank; must avoid any conflict between the interests of the co-operative bank and the interests of such director, managing director or executive officer, as the case may be".[78]

Chapter 3 of the Act provides with the prudential requirements according to the prescriptions of the Minister. The Act states that, "the bank must meet and maintain a minimum of capital requirements; asset quality; liquidity to be held in addition to any surplus reserves held in accordance with paragraph (d); and surplus reserves as required by section 46 of the Co-operatives Act, as may be prescribed by the Minister".[79]

2.3.1 Co-operative Banks Development Agency

The Co-operative Banks Act also makes provision for the establishment of an Agency in the Republic, which is known as the Co-operative Banks Development Agency (CBDA), which is a juristic person and must exercise its functions in accordance with the Act and any other relevant law.[80] The sole purpose of the agency is to develop and promote co-operative banks in South Africa.

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[77] Section 14 of Act 40 of 2007.
[78] Section 16(3) of Act 40 of 2007.
[79] Section 20(1) of Act 40 of 2007.
[80] Section 54(1) of Act 40 of 2007.

The general functions of the CBDA are to ensure that co-operative banks receive all the necessary support to ensure that they are successful. Therefore, with that mandate in mind the CBDA aims to offer assistance in terms of providing financial support to such banks in form of loans and grants. The Agency also ensures the promotion of the establishment of representative bodies and support organisations, and the regulation and registration of such organisations. Since co-operative banks are still developing, the Agency must also support the banks with liquidity management, to ensure that they do not get liquidated.[81]

The Act states that, "the agency must also facilitate, promote and fund education, training and awareness in connection with, and research into, any matter affecting the effective, efficient and sustainable functioning of co-operative banks".[82] This provision entails that the agency must recommend ways to allow for the registration of more co-operative banks in South Africa, and should provide guidance to the existing Co-operative Financial Institutions on how to meet the requirements for registration.

The Act also provides with the general powers conferred on the agency. It states that, "the CBDA may determine its own staff establishment and may appoint a managing director, subject to the approval of the Minister, and employees in posts on the staff establishment on such conditions, including the payment of remuneration and allowances, as it may determine in consultation with the Minister".[83]

The Act further provides that, "CBDA may also collect fees and invest funds; finance publications; acquire, hire, maintain, let, sell or otherwise dispose of movable or immovable property for the effective performance and exercise of its functions, duties and powers; enter into and decide upon the manner in which agreements must be entered into; obtain the services of any person, including any organ of state or institution, to perform any specific act or function; determine where its head office must be situated; confer with any organ of state; open and operate its own bank accounts; perform legal acts, or institute or defend any legal action in its own name;

[81] Section 50(1) of Act 40 of 2007.
[82] Ibid.
[83] Section 56 of Act 40 of 2007.

and do anything that is incidental to the performance or exercise of any of its functions or powers”.[84]

The Act also contains provisions for the appointment of board members[85], and also specifies their term of office[86] and the grounds for disqualification or vacation from office[87]. Member’s duties[88] are also outlined in the Act, which states that the board of the Agency is the accounting authority of the Agency within the meaning of the Public Finance Management Act[89] and must, in addition to the duties and responsibilities provided for in the Public Finance Management Act, provide effective, transparent, accountable and coherent corporate governance and conduct effective oversight of the affairs of the Agency; comply with all applicable legislation and agreements.[90]

The Act also further stipulates that the Minister is the executive authority for the Agency, and the agency is accountable to the Minister. The Minister has a duty to ensure that the Agency complies with this Act, the Public Finance Management Act and any other applicable legislation; ensure that the Agency is managed responsibly and transparently and meets its contractual and other obligations; establish and maintain clear channels of communication between him or her and the Agency; and monitor and annually review the performance of the Agency.[91]

2.3.2 Section 86 Regulations

The Co-operative Banks Act provides that the Minister may by notice in the Gazette make regulations regarding anything which must or may be prescribed in terms of this Act.[92]

Regulation Gazette No. 32357

This regulation[93] was passed by the Minister of Finance, to give clarity and guidance to certain provisions of the Co-operative Banks Act. Part 4 of the Regulation deals

[84] Ibid.
[85] Section 58 of Act 40 of 2007.
[86] Section 59 of Act 40 of 2007.
[87] Section 60 of Act 40 of 2007.
[88] Section 64 of Act 40 of 2007.
[89] Act 1 of 1999.
[90] See footnote 36 *opcit.*
[91] Section 71 of Act 40 of 2007.
[92] Section 86(1) of Act 40 of 2007.

with the prudential requirements of a co-operative bank as stated in Section 20 of the Act. They are the important requirements a co-operative bank must comply with in order to register.

The regulation states that the minimum capital adequacy ratio[94] for a co-operative bank must be 6% of the assets held by the co-operative bank. Sub-regulation (c) deals with liquidity of the co-operative bank. It states that a maximum of 5% of total assets may be held in fixed and non-earning assets. A minimum of 10% of total deposits must be held in investments, subject to no penalties and convertible into cash at any time. Furthermore, a minimum of 2.5% of total deposits must be deposited with the Agency or a higher tier co-operative bank.

2.4 Public Finance Management Act

The Public Finance Management Act[95] is the main legislation that governs and regulates financial management in the national government and provincial governments; to ensure that all revenue, expenditure, assets and liabilities of those governments are managed efficiently and effectively; to provide for the responsibilities of persons entrusted with financial management in those governments.

Therefore, the Act also applies to co-operative banks since they are under the purview of the Minister, and must account for all revenue and expenditure used. The Co-operative Banks Development Agency also receives funds from the National Treasury for its operations; this also means that it falls under the Act. The Directors of the Agency are supposed to prepare annual financial statements as per the provisions of the Act, to show how they spent the budget for a financial year.

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[93] Regulation Gazette Volume 529, July 2009, Pretoria.

[94] For purposes of calculating the capital adequacy the following qualify as capital:

a. Membership shares issued by the co-operative bank
b. Indivisible reserves as required in terms of Section 3(1)(e) of the Co-operatives Act
c. Non distributable reserves created or increased by appropriations of surpluses
d. Any other non-distributable funds of a permanent nature held by a co-operative bank not subject to a legal claim, and confirmed by the supervisor in writing.

[95] Act 1 of 1999.

The Co-operative Banks Act states that the board of the Agency is the accounting authority of the Agency within the meaning of the Public Finance Management Act.[96] Furthermore, Section 69 states that the annual budget and strategic plan of the Agency must be submitted to the Minister in terms of the Public Finance Management Act, Section 70 goes on to point out that the financial management and the preparation and submission of financial statements and annual reports must be in accordance with the Public Finance Management Act.[97]

2.5 Conclusion

Therefore, this sums up the main legislations and policy frameworks that regulate the institution of co-operative banking in South Africa. They deal with processes like the registration, supervision and de-registration of such banks. The Co-operative Banks Act also led to the establishment of the Co-operative Banks Development Agency, which is a juristic person primarily responsible for the growth and expansion of co-operative banks, through continuous research, education and training for the improvement of co-operative banks. The Agency is the main body, representing the Minister and has to comply with the provisions of the Public Finance Management Act.

[96] Section 64 of Act 40 of 2007.
[97] Act 40 of 2007.

CHAPTER THREE: ISSUES AND CHALLENGES

3.1 Introduction

This chapter will focus on the issues and challenges that have been encountered with regard to the registration of co-operative banks in South Africa. At present, there are only two co-operative banks which have managed to satisfy and meet the requirements for registration, the rest are still operating as Co-operative Financial Institutions (CFI's) under an exemption notice.[98] Therefore this chapter will analyse the major reasons resulting in the failure of more co-operative banks to register, and the effects the situation has on potential co-operative banks. This chapter will also investigate and expose some of the challenges leading to the ultimate failure to register co-operative banks in South Africa and will also assess the contribution made by co-operative banks to socio-economic development and poverty alleviation.

3.2 Status of Co-operative Banking

The co-operative banking sector has only recorded a total of two successfully registered co-operative banks since the promulgation of the Co-operative Banks Act, and the establishment of the Co-operative Development Agency. The Co-operative Banks Act was promulgated in 2007, and as part of the provisions of the Act, the Supervisors are supposed to prepare an annual report on the status of co-operatives.[99] An analysis of the reports they provided would be analysed to check some of the challenges encountered by CFI's.

3.2.1 Annual Report (2010/11)

The Combined Annual Report of the Supervisors of the Co-operative Banks Development Agency and the South African Reserve Bank (2010/11), stated that applicant Co-operative Financial Institutions (CFIs) are expected to satisfy certain requirements as contained in the Act to be considered for registration. In the same vein, an all-inclusive registration framework is applied by the supervisors that only

[98] Banks Act Exemption Notice No. 404, published in Government Gazette No. 35368 dated 22 May 2012.
[99] The report is in terms of section 52 of the Co-operative Banks Act (40 of 2007).

accommodate sustainable CFIs that adhere to the co-operative principles to register as co-operative banks.

The Supervisors of Co-operative Banks therefore take into account the following factors to register co-operative banks taking due regard of the nature, size and developmental potential of each potential CFI, the Supervisor concerned will register an applicant as a co-operative bank if, *inter alia*, it has:

- "the characteristics of a co-operative, adhering to the co-operative principles;
- sufficient human, financial and operational capacity;
- fit and proper directors, and a competent management team, including proper governance;
- adhered to minimum prudential requirements;
- adequate policies and procedures in place, including risk management systems; and
- adequate internal control systems"

Therefore taking into account the above mentioned requirements, the Supervisors received applications from eligible CFI's for registration after the coming into operation of the Act.

The Supervisors of the CBDA received numerous applications from potential CFI's, a total of 17 CFI's were met the minimum requirements as at that date. More applications were received from 2 additional CFI's who also met the requirements, however, sadly one CFI became disqualified because the value of deposits fell below R1 million. Therefore on 31 March 2011, there were 18 eligible CFIs with a total of 28 034 members and approximately R161 million in deposits.[100] During the same year, only 11 applications were completed satisfactorily and that enabled the Supervisors to conduct pre-registration assessments.[101]

[100] Combined Annual Report of the Supervisors of the Co-operative Banks Development Agency and the South African Reserve Bank (2010/11).
[101] Ibid.

Ditsobotla[102] became the first successfully registered co-operative bank in South Africa on the 17th of February 2011. The Supervisors also approved one more co-opertive bank which met the requirements which was Orania Savings and Credit Co-operative Limited. However, its registration was incomplete because it awaited the successful reservation of its name by the Companies and Intellectual Property Commission (CIPC) and the publication of the required notice of registration in the Government Gazette in compliance with section 8 of the Act.[103]

The successful registration of the two co-operative banks was a mile stone, but however the remaining nine CFI's failed to satisfy the registration requirements. The Supervisors informed the applicants the reasons for the failure that resulted in the non-registration. The Supervisors also made it clear that once those shortcomings were addressed, the Supervisors will reconsider their applications for registration. The Supervisors requested progress reports to be submitted to the applicants' self-regulatory bodies and copies thereof to be submitted to the Supervisor concerned.[104]

Therefore the report clearly shows that only one co-operative bank managed to register during the 2010/11 period, and the rest of the CFI's failed to meet registration due to failure to meet the prudential requirements.

3.2.2 Annual Report (2011/12)

In the 2011/12 report[105] the Supervisors received more applications, with the addition of three more eligible CFI's, Orania finally satisfied all the requirements for registration as a co-operative bank and became the official second co-operative bank in the country. Therefore, there were a total of nineteen CFI's and two co-operative banks. The three additional CFI's had the opportunity to apply as a co-operative bank under Section 3 of the Act.

The Supervisors noted significant growth in the membership base for CFI's during this period, they noted an increase of 12.5% from 28 034 members to 31 481

[102] The institution was established in 2000 following the merger of three worker-based financial cooperatives in the North West Province i.e. Itireleng SACCO (formed by Lafarge Cement employees), Ikageng SACCO (formed by the Ditsobotla Local Municipality) and Aganang SACCO (formed by Holsim employees.
[103] Ibid.
[104] Ibid.
[105] Combined Annual Report of the Supervisors of the Co-operative Banks Development Agency and the South African Reserve Bank 2011/12.

members. This increase was prompted by growth in three CFI's which were Nehawu, Sibanye and Flash. This period also saw an increase in the number of eligible CFI's, and deposits of the two co-operative banks and nineteen CFI's increased by 17% to a staggering amount which was R187.9 million during this period of review, from R161 million in the preceding year. This was as a result of the bigger institutions showing strong deposit growth.[106]

The main challenge experienced during this period of review was the fact that none of the CFI's evaluated during the 2011/12 period managed to effect the recommendations of the Supervisors in order to meet the requirements for registration, so they failed again to get registered. Institutional assessments[107] were jointly conducted by the CBDA's Capacity Building and Supervisory units in respect of three eligible CFIs that had not applied for registration, but that met the minimum registration conditions. The CBDA Capacity Building Unit was in the process of providing these three CFIs with developmental support to assist them in qualifying for registration as co-operative banks.

3.2.3 Annual Report (2012/13)

In this report[108], the challenge experienced on the previous financial years continued to this period as well, the Supervisors alleged that the applicant CFI's that had been evaluated during the 2011/12 year had managed to reform their affairs by addressing the weaknesses pointed out before, hence they were subsequently not registered again.[109]

The Supervisors also identified that three CFI's had become insolvent following the investigations that were carried out by SAMAF and the CBDA supervisor. This followed a recommendation from the CBDA supervisor stating that the CFI's had to be liquidated. However, the Provincial Departments of Economic Development elected to rehabilitate these CFI's. As a result, the CBDA Supervisor was only going

[106] Ibid.

[107] Institutional assessments are conducted at CFIs to determine, inter alia, the reasons for non-compliance with section 3 of the Act, that is, the submission of an application to the Supervisor for registration as a cooperative bank. Pre-registration assessments are conducted on CFIs that have submitted all documents required for registration.

[108] Combined Annual Report of the Supervisors of the Co-operative Banks Development Agency and the South African Reserve Bank 2012/13.

[109] Ibid.

to liquidate CFI's should the proposed interventions not be provided in a timely manner. This was going to be done to protect the depositors and maintain confidence in the CFI sector.

The challenges preventing potential applicant CFIs from registering as co-operative banks was highlighted in the Supervisors' 2010/11 Combined Annual Report. As was the case during the previous financial year, the primary challenges faced by applicant CFIs were insufficient capital, lack of proper governance and poor management of information systems.

3.2.4 Annual Report (2013/14)

In this financial year[110] the CBDA completed its first full supervisory cycle of the CFIs sector. These entailed ongoing assessments of new CFIs, conducting pre-registration on-site assessments of applicants, reviewing quarterly off-site assessments of returns, and conducting on-site assessments and inspections of registered CFIs within one year after registration.

On the 31st of March 2014, the CBDA recorded a total of 57 CFI's which had applied for registration in terms of the Exemption Notice[111]. The number calmed to a total of 24 CFIs which were subsequently registered after meeting the requirements for registration, bringing the total number of registered CFIs under the CBDA Supervisor to 25, this included *Ditsobotla* Co-operative Bank.

The Supervisors of the CBDA referred two applicants to the SARB since had exceeded the maximum deposit threshold of R30 million as specified in the Exemption Notice. During this period, the majority of applicants not registered with the CBDA were declined because they failed to meet the minimum registration requirements of holding R100 000 in deposits and having a minimum of 200 members. The remaining applicants were declined because they failed to meet one or more of the requirements.

The Supervisors also declined seven applicants since they were deemed to be insolvent. The CBDA also recognised the fact that most applicants had been

[110] Combined Annual Report of the Supervisors of the Co-operative Banks Development Agency and the South African Reserve Bank 2013/14.
[111] Exemption Notice, No. 404, published in Government Gazette No. 35368 dated 25 May 2012.

operating for more than five years; hence they discussed with each of these CFIs their present state of affairs with a view to determine a basis for registration. Subsequent to the meetings held with the respective CFIs, three of these institutions were registered during the course of the year under review after either providing the Supervisor with written guarantees of support from host companies and unions, or subsequently complying with the minimum solvency requirements.

During this period, no new co-operative banks were registered due to the fact that they also failed to satisfy the minimum requirements. According to the report, the supervisory team reviewed two applications held in abeyance from the previous reporting period due to outstanding audited financial statements. During the course of their registration assessments, concerns were raised about the self-sustainability of the institutions and their applications were subsequently declined.

3.3 Challenges deterring registration

The reports by the Supervisors of the CBDA clearly review that certain challenges are apparent and they preventing CFI's from becoming potential co-operative banks. Therefore, CFI's were given an opportunity to apply for registration, but however, every year they exhibit the same weaknesses which prevent them from registering as co-operative banks. In the report, the supervisors also mentioned that they offer support to the CFI's in order to allow them to meet the prudential requirements for registration, but the situation has remained the same, applications for registration have been denied on one or more grounds. The reasons for failing to register would be discussed below.

3.3.1 Insufficient capital levels

The Supervisors of the CBDA noted that the majority of CFI's lack capital to sustain their business, and pose risks to the restoration of confidence in member-based banking. The regulation passed by the Minister of Finance[112] stipulated that the minimum capital adequacy ratio must be 6% of the total assets held by the co-operative bank. However, most of the applicants fail to meet this requirement.

[112] Regulation Gazette No. 9110 , 1 July No. 32357 Vol. 529 Pretoria, 2009.

For purposes of calculating the minimum capital-adequacy ratio referred to in regulation 4(2), only the following qualify as capital:[113]

> "(i) Membership shares issued by the co-operative bank
>
> (ii) Indivisible reserve requirement in terms of the Act
>
> (iii) Non-distributable reserves created or increased by appropriations of surpluses (retained earnings)
>
> (iv) Any other non-distributable funds of a permanent nature not subject to a legal claim by any person held by a co-operative bank approved by the Supervisor in writing."

The reports submitted by the Supervisors clearly show that the sector is inadequately capitalised, this is indicated by the consolidated capital-adequacy ratio averaging 2% over the four-year period. The weak capital position is attributable to the low member capital base and losses, which resulted in negative institutional capital[114]. This means that CFI's still need to grow their capital base by increasing the number of members, and finding ways to recover loses in order to meet the minimum capital adequacy ratio.

The other main challenge has been the fact that, most applicants regard the capital adequacy ratio as too high, and are failing to meet the requirement. The Supervisors stated that, "some applicants regard the capital-adequacy requirements as relatively high at this early stage, since some are in a rapid growth phase and the self-regulatory bodies are not imposing similar prudential requirements". They further alleged that, "there is concern about the weak capital position in general, compared to international standards, WOCCU, for instance, recommends that the minimum capital-to-asset ratio for credit unions should be 10% of total assets".

3.3.2 Insufficient credit risk management

Since, CFI's are still growing, and showing substantial growth over the years, risk is one of the aspects that need to be considered considering the nature of business

[113] Ibid section 4(2).
[114] See DTI at 3

carried by these institutions. According to the Supervisors of the CBDA, credit risk is undoubtedly one of the main risks affecting CFIs.[115]

The Supervisors further state that, special training is a pre-requisite as far as the monitoring and management of delinquent loans is concerned. In some of the pre-registration assessments that were carried out, it was clear that the management of the CFI's would react too late, especially in instances where no provisions for bad and doubtful debts had been made. In addition, it was evident that the management accounts that were scrutinised, some bad debts were often not appropriately written off to reflect the true financial position of some of the applicant CFIs.[116]

The 2010/11 report further observed that, while credit committees were generally found to be active, there were often instances wherein credit committee members had approved some loans that clearly exceeded their authorised limits in terms of the applicable loan policies that were utilised at the time of the assessments. This in simple terms means that granting loans in excess of the amount prescribed would pose a great risk to the CFI in the event that the loan is not repaid. This is one of the major challenges facing CFI's, and as pointed out earlier, the supervisors require training to be conducted.[117]

3.3.3 Lack of governance structures

The Supervisors of the CBDA also identified weak governance as one of the challenges affecting CFI's. Clearly, corporate governance in the co-operative banks sector is very weak. The Supervisors also pointed out that, "members of the supervisory and audit committees do not meet regularly to discuss prominent matters affecting the institutions. Committees that do meet on a regular basis often fail to provide effective oversight. Furthermore, members' active participation through annual general meetings (AGMs) is generally not enough, with some of the CFIs not holding Annual General Meetings at all. Members are in need of training, especially in respect of committee and board responsibilities. Training should not be limited to

[115] ibid
[116] Ibid.
[117] Ibid.

existing board members, but should be extended to all interested members in order to increase the pool of suitable members who could be appointed to the board".[118]

Therefore, the CBDA should conduct training exercises to these developing CFI's to ensure that there is corporate governance, and also apply the principles of corporate governance as outlined in the King III report[119]. These principles would assist towards proper governance of CFI's.

3.3.4 Weak operational capacity

The Supervisors also stated that, another challenge facing CFI's was weak operational capacity. Despite the fact that credit and savings policies are obtainable, they are often outdated or not implemented. The evidence suggests that CFIs merely adopt policy templates provided by the self-regulatory bodies, without the necessary expertise or knowledge to implement the applicable policy proposals successfully. A significant proportion of institutions that were assessed did not have liquidity or cash flow policies to guide them in managing their liquidity positions.[120]

3.3.5 Lack of accounting experience

In addition, the other challenge noted has been the fact that there are scarcely any members with the required experience and qualifications, especially in the rural areas, where the need for access to finance and economic development is the greatest. Financial statements and management accounts are often found to be unbalanced and in total disarray. Therefore, the supervisors suggest that the provision of basic training in accounting skills and accounting software to such CFI's

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[118] Ibid.

[119] King Report on Corporate Governance III of 2009, the principles include:

- Ethical leadership and corporate citizenship,
- Boards and directors,
- Audit committees,
- The governance of risk,
- The use of information technology,
- Compliance with the laws, codes, rules and standards,
- Internal audit,
- Governing stakeholders relationships, and
- Integrated reporting and disclosure.

[120] See Notice 620 at 21 opcit.

would be essential for the development of member-based banking, especially in the remote rural areas.[121]

3.3.6 Poor management of information systems

Upcoming CFI's have a critical shortage when it comes to information technology, therefore the supervisors identified it as a problem as well by pointing out that urban-based CFI's use basic computerised accounting and management information systems (MIS's). These are, however, in most instances considered inadequate for basic banking operations. For instance, loan portfolio performance is not monitored in most instances. Rural CFIs are using manual systems to open accounts and record transactions. Such institutions will not be able to submit their prudential returns on time to the Supervisors to conduct effective off-site supervision. It is evident that they are in need of technical support to provide accurate and effective management information in a timely manner.[122]

3.4 Overcoming challenges: lessons learnt from Ditsobotla

The challenges discussed *supra* clearly indicate that more needs to be done to address the situation preventing CFI's from meeting the requirements for registration. It is also crystal clear that the CBDA Capacity Building Unit[123] is not doing enough to ensure that these institutions receive the necessary guidance to meet registration. Therefore, in this section lessons would be drawn from Ditsobotla Co-operative Bank[124], which was the first co-operative bank to register and how it overcame some of the challenges it succumbed prior to registration.

According to Padi, who is the Managing Director of Ditsobotla Co-operative Bank[125], the major challenge facing CFI's is the fact that there is poor growth in terms of

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[121] Ibid.

[122] Ibid.

[123] The CBDA's Capacity Building Unit is responsible for supporting, promoting and developing CFIs and promoting the establishment of representative bodies and support organisations. In fulfilling this responsibility, the Capacity Building Unit determines the training needs for the cooperative banking sector and develops appropriate capacity enhancement programmes in conjunction with relevant stakeholders such as representative bodies, BANKSETA, other national and provincial development agencies, and institutions of higher learning.

[124] See Van Niekerk at 5 *opcit*.

[125] Padi, S. Challenges and lessons in registering as a co-operative bank in SA http://www.treasury.gov.za/coopbank/Conferences/CFI%20Indaba%2019%20-%2021%20October%202011/Challenges%20and%20Lessons%20in%20Registering%20as%20a%20Cooperative%20Bank%20in%20SA.pdf. Assessed on July 1, 2016.

membership. This means that a lot of people are unaware of the services provided by these institutions. As a result, a low membership base would mean that the CFI would not be able to meet the capital adequacy ratio; hence it would eventually fail to register. He further pointed out that to address the challenge, there is need to address any challenges that affect the co-operative bank in order to sustain continuity, safe and sound banking.[126]

The Managing Director (MD) of Ditsobotla also adds on and states that marketing is needed so that the CFI reaches out to a large number of members. This will increase the capital base and build on capital adequacy which is a requirement for registration.

Adherence to co-operative principles is also an important aspect which will eventually persuade the Supervisors to grant the application for registration. They state that such adherence is a precondition for registration. The Supervisors of the CBDA add that, "it is imperative that a co-operative bank adheres to the co-operative principles.[127] In addition, it should foster ethical values of honesty, openness and social responsibility. The adoption and maintenance of co-operative principles and values contribute to the stability and growth of CFIs, and improve the co-operative image and reputation that should restore confidence in the sector".[128]

According to the MD of Ditsobotla, he also supports that CFIs should be guided by the seven cooperative principles[129], he believes that such compliance would ensure registration, since Ditsobotla also had to comply with those principles before registration was granted by the Supervisors of the CBDA. Therefore, other CFI's are supposed to follow similar footsteps to ensure they meet the requirements for registration.

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[126] Ibid.

[127] The seven co-operative principles are:

(i) voluntary and open membership
(ii) democratic member control
(iii) member economic participation
(iv) autonomy and independence
(v) education, training and information
(vi) cooperation among co-operatives and
(vii) concern for community

[128] See Van Niekerk at 21 *opcit.*

[129] Ibid.

The DTI purports that, "the ability to establish and maintain adequate and effective processes of corporate governance that are consistent with the size, nature, complexity and inherent risks of the activities and the business of the institution is crucial. This includes the proper evaluation of the processes that have been established to achieve the institution's strategic and business objectives efficiently, effectively, ethically and equitably. Co-operative banks must have proper governance structures in place, including the implementation of a supervisory committee, governance committee and audit committee".[130] This conforms to the King III Code, under the corporate governance principles.[131]

In the case of Ditsobotla, the MD stated that there is need for proper governance, which places greater responsibility on the Board and the management. The board of a co-operative bank must craft a strategic plan with vision, mission and objectives and should organise an AGM. The board should make sure financial statements are prepared and the co-operative bank is audited.[132] Furthermore, he added that the management and board should develop policies and also revise the policies. The policies include savings policy, loan policy, liquidity management, membership recruitment, investment, training, performance appraisal, procurement, IT, and security. This all conforms to the corporate governance principles.

Co-operative banks are required by the Act[133] to meet and maintain minimum prudential requirements. The capital-adequacy requirement is set at 6% of the total assets. Additional capital, calculated as 2% of all loans, is also required for co-operative banks that provide loans to their members. Sufficient provisioning for delinquent loans and sufficient liquidity are crucial for the proper functioning of the CFI. Minimum liquidity requirements prescribe that at least 10% of total deposits must be held in liquid investments and loans may not exceed 80% of the total assets. The potential of applicants to reach these levels within a reasonable period is taken into account for registration purposes by the supervisors.[134]

In the case of Ditsobotla, the MD also stated that there is a need to comply with all the prudential regulations, the cooperative banks act and the cooperative act. This

[130] See DTI at 3 *opcit.*
[131] See King Code III at 119 *opcit.*
[132] See King Code III at 119 *opcit.*
[133] Act 14 of 2007.
[134] See DTI at 3 *opcit.*

however has been a huge impediment to CFI's because they state that the prudential requirements are difficult to comply with since the percentages are too high, and it is almost impossible to meet them. This has been the major reason why most applications have been denied.

Furthermore, matters relating to human resources, such as capacity building and staff training, are critical for the effectiveness and sustainability of co-operative banks. In terms of Ditsobotla, they also list education and training as one of the key factors affecting the growth and sustainability of co-operative banks. Succession planning is also important, especially at senior management and board levels. It is a requirement that every co-operative bank must have the adequate human capacity to operate proficiently and expertly. Every co-operative bank has to appoint suitably qualified and experienced members as directors and executive officers. Once again, the nature and size of the co-operative bank are taken into consideration when determining whether directors are considered to be "fit and proper".[135]

The Supervisors also noted in the 2010/11 report that, Co-operative banks should be fully committed to sound risk management standards and practices commensurate with their nature and size. A co-operative bank must, *inter alia*, ensure that:

- "policies and procedures that are in place are consistent with its vision and business strategies;
- realistic benchmarks and limits have been set to guide its risk appetite;
- appropriate systems are in place for reporting, monitoring and controlling risks; and
- Independent checks and balances are in place to monitor compliance with prudential requirements."[136]

Finally, co-operative banks must have appropriate means to interact effectively with their members, suppliers, regulators and counterparties. Furthermore, an appropriate MIS must be in place to support their business operations. More advanced technologies are required by larger co-operatives, especially those operating closer to cities and towns, to cater for the needs of their members. This would also enhance their competitiveness ability and result in improved access to finance for members.

[135] Ibid.
[136] Ibid.

The MD of Ditsobotla also stated that, "We need to keep pace with information technology", this means that IT is also vital for the sustenance of a co-operative bank.

Ditsobotla Co-operative Bank also noted that some of the challenges experienced in the industry are the ways in which co-operative banks are regulated. They went further to also outline that amendments in co-operative legislation will go a long way in ensuring the survival of co-operative banks, since the current regulations make it difficult for upcoming CFI's to thrive in this seemingly restrictive economy. Competition from major banks in the country is also one of the major reasons preventing the growth of more co-operative banks in South Africa. These are some of the lessons learnt from Ditsobotla Co-operative Bank, the first success story in terms of registration as a co-operative bank.

3.5 The nexus between co-operative banking, economic development and poverty alleviation

The introduction of the Co-operative Banks Act[137] has made tremendous strides towards uplifting socio-economic development in South Africa. Despite all the challenges being experienced in the industry, the Act has managed to provide a platform wherein Financial Co-operatives may develop and thrive. The Act targets people in communities, by giving them access to member based banking and affordable loans through their own co-operatives. This in turn ensures that people in communities may emancipate themselves through projects that improve their standard of living. The Act, through the Co-operative Banks Development Agency continues to give guidance and training to current and newly emerging Financial Co-operatives.

The Government[138] recognizes the importance of co-operatives in South Africa and that the main purpose of co-operatives is to render services to their members. Co-operatives contribute significantly to the development of the nation, economy and communities through the improvement of the socio-economic status of its members.[139] It further acknowledges the specific potential of co-operatives, as

[137] Act 40 of 2007.
[138] The Government of the Republic of South Africa.
[139] The Department of Trade and Industry. *A Co-operative Development Policy for South Africa.* 2004.

enterprises and organizations inspired by solidarity, to respond to members' needs and to ensure greater black participation in the mainstream economy, especially persons in rural areas, women, persons with disabilities and the youth. The Government also stated that it shall continuously engage with stakeholders in the youth and women sectors to design appropriate support programmes for co-operatives.[140]

The CBDA records show that there are currently two registered co-operative banks regulated by the South African Reserve Bank. These contribute toward 40% of the sector's total assets. Eleven institutions are eligible for registration as co-operative banks since they met the Act's regulatory threshold of more than 200 members and R1million in deposits. However, they have not met other prudential requirements, regulated by the CBDA. They make up 53% of the assets of the sector. The CBDA also supervises and regulates thirteen 'other' CFI's, making 6% of the sector.[141]

The industry has a total of 24 722 members, and a combined total of R236 533 481 in assets.[142] This clearly shows the economic potential of financial co-operatives and how they contribute to socio- economic growth in the country. The main obstacle has been the failure to meet the requirements for registration which the CBDA must address. This industry is also dominated by women and the youth which makes it the perfect tool to emancipate and develop communities.

The Department of Trade and Industry also noted that, "the government shall also contemplate on introducing support measures for the activities of co-operatives that meet specific social and public policy outcomes, such as employment creation and the development of activities benefiting disadvantaged groups or geographical areas".[143]

The promotion of co-operative enterprises is a crucial programme of the Government's Broad-Based Black Economic Empowerment (BEE) strategy that aims to address the imbalances of the past and to make an equitable transfer of the ownership and control of economic resources to the majority of South African citizens. The BEE strategy will, among other things, encourage and support efforts

[140] Ibid.
[141] The Co-operative Banks Development Agency Annual Report, 2014/15.
[142] Ibid.
[143] See DTI at 139 *opcit.*

by co-operatives and other forms of enterprises that support Broad-Based Economic Empowerment (Broad-based empowerment models-ESOPs, community trusts/groups, worker co-operatives, stokvels, burial societies, etc.) to assert ownership and control of economic activities in new and existing enterprises and break into new sectors of economic activity. The Government stated that it is therefore committed to work with the co-operative movement to ensure that an increasing portion of the ownership and control of the economic activities is vested amongst co-operative enterprises.[144]

3.5.1 Co-operative Banking as a tool for alleviating poverty in South Africa

Statistics review that almost half of the world's six billion people are living on less than two dollars a day, therefore alleviation of poverty has become the biggest challenge to the human society. In response, the global campaign against poverty has gained momentum, with various development actors proposing the use of different instruments to alleviate poverty. However, there is an emerging consensus among many players, including the United Nations (UN), the International Labour Organization (ILO), the International Cooperative Alliance (ICA) and the European Union (EU), that the co-operative initiative is one of the few forms of organizations that meets all dimensions of poverty.[145]

The massive role played by co-operatives in the modern history of South Africa cannot go unnoticed, especially towards the development of its economic foundations. The period of apartheid was characterised by huge conglomerates which dominated the racialized and exploitative mainstream economy, however, co-operatives mainly in the financial services and agricultural sectors were also a crucial feature of the apartheid economy. According to Satgar, he clearly contends that:-

> "…..In other words, Afrikaner empowerment in the 20th century did not just happen through the logic of capital accumulation but had to also coexist with a logic that met human needs through co-operative forms of organising

[144] Ibid.

[145] Wanyama, F., Develtere, P., Pollet, I. 2008. Encountering the Evidence: Co-operatives and Poverty Reduction in Africa. Working Papers on Social and Co-operative Entrepreneurship WP-SCE 08-02.

production and consumption; albeit underpinned by perverse and racialised relations of productions".[146]

Co-operatives are catalysts for economic growth and sustainable development for the disadvantaged, vulnerable and marginalised communities as well as those with limited resource capabilities.[147] The sustainability of these enterprises contributes significantly towards poverty alleviation, giving poor people the opportunity to uplift themselves out of poverty and its associated forms of deprivation.[148]

There is a distinct lack of infrastructure and resources in rural communities, particularly amongst the previously disadvantaged and marginalized poor. The co-operative concept introduces an opportunity for people to pool their labour and other resources such as capital or credit loans in order to survive, sustain and produce a surplus that could translate into a viable co-operative enterprise. The co-operative provides a vehicle for workers to participate in a communal relationship that encourages self-management in a democratic organisational structure. This type of control restores ownership, dignity and self-worth in people who are the key to constructive change and development in the rural sector.[149]

The Co-operative Act recognizes the important role that co-operatives play in social responsibility, self-help, democracy and social re-engineering. The Act also recognizes the important role that a national co-operative movement can make in advancing social and economic development. The recognition of the important role of co-operatives in the content of the Act should stimulate the need for similar and further research into the activities and advancement of co-operatives towards the alleviation of poverty and unemployment in the rural sector.[150]

Addressing the issues of poverty and unemployment in rural development within a developing country like South Africa is a crucial part of the country's economic

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[146] Satgar, V. 2007. The State of the South African Cooperative Sector. Executive Director of the Cooperative and Policy Alternative Centre (COPAC).
[147] Zulu, L. 2014. Minister of Small Business Development, Pretoria. http://www.sanews.gov.za/south-africa/cooperatives-contribute-poverty-alleviation.
[148] Ibid.
[149] Abrahams, C. 2009. Research Dissertation: Cooperative Enterprises As A Solution To Rural Poverty And Unemployment Case Studies Of The Heiveld Cooperative At Nieuwoudtville In The Northern Cape And Die Berg Vrugteverwerking At Piketberg In The Western Cape Province. Faculty of Economic and Management Sciences , University of the Western Cape.
[150] Ibid.

development and the social development of its people. This standpoint is made within the context of the democratization, post-1994, and the aim, vision and mission of the state, business and civil society to uphold the new constitution. It is also noted that within the context of the South African socio-economic scenario it is important for all stakeholders to play a part in contributing to moving the country and its people forward with regard to development and prosperity. More importantly, there is a need for stakeholders to work together on reaching short, medium and long-term goals.[151]

The foundation for post-apartheid co-operative development is based in the Broad – Based Black Economic Empowerment Act[152], the Act serves as a basis for the Co-operatives Development Policy and the new Co-operatives Act. While the former Act provided unequivocally for co-operatives to be part of socio-economic strategies to empower black people, it threw up several contradictions that restrict cooperative development in post-apartheid South Africa.[153] To begin with, the deracialising of companies, procurement policy and the numerous BEE charters in various sectors has not benefited co-operatives in any direct way. Hence, the BEE discourse, particularly the broad based version, has not worked for co-operatives and has purely been about class formation at the upper ends of society.

The BEE has also been subject to criticism based on the fact that it generally does not assist with institutionalising co-operatives in a sustainable way on the ground. The BEE promised so much hope to the ordinary South Africans, but to date little help has been extended to upcoming co-operatives; hence the expectations are so high because of the populist nature of BEE. The corruption that flows from this has made it extremely difficult to build trust amongst groups in co-operative development processes.[154] Another point is that the racially exclusive nature of BEE in general stands in direct contradiction to the international principles enshrined and espoused in the new Co-operatives Development Policy and Act.[155]

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[151] Ibid.
[152] Act 53 of 2003.
[153] See section 1 and 1 (b) dealing with definitions and section 2 (b) regarding objectives of the Broad-based Black Economic Act, 2003, which defines the role for cooperatives.
[154] See COPAC Research Reports. 2005. Co-operatives in Gauteng (A Quantitative Study): Broad Based BEE or Push Back Into Poverty and Cooperative Support Institutions in the Gauteng Cooperative Sector (Case Studies): Enabling Support or Dependent Development?".
[155] See DTI at 119, opcit.

Furthermore, to clearly shed light on the BEE strategy, taking a look at the first principle of the International Co-operative Alliance Statement of Identity on Co-operatives it refers to, 'voluntary and open membership' and in that regard a positive qualification is made such that membership cannot be restricted based on gender, social, racial, political or religious discrimination. Hence, the BEE approach in general is inconsistent with the essence of what a genuine co-operative is all about. The implication of a racially exclusive approach to co-operative development maintains a racialised duality in the South African co-operative sector which, in economic terms, is dominated by mainly white farming co-operatives.[156]

Put differently, a BEE approach does not foster solidarity and cooperation links between historically white co-operatives and the developing black co-operatives. It also does not give motivation towards breaking the divide brought about by apartheid especially towards deracialising historically white co-operatives but however it replicates the racial divide. On a more positive light, non-racial practices are taking centre stage based on a comprehension of the co-operative principles, and this needs to be encouraged. In summary, the basis of the argument being pursued is that the BEE policy needs to be revisited, such that BEE in general does not undermine co-operative development in post-apartheid South Africa. More sternly, a time has come for serious consideration to be given towards uncoupling co-operatives from a BEE approach to a more development oriented approach. Instead a co-operative based approach and model of empowerment needs to prevail in the co-operative sector; taking into account the fact that by definition and inherently co-operatives are empowerment based institutions.

As has been mentioned the Cooperative Development Policy for South Africa and the Co-operatives Act are important policy pillars for the development of a strong co-operative sector.[157] Both the policy and legislative framework are crucial to ensure co-operatives in the post-apartheid context are not just ameliorative but are capable

[156] Ibid.

[157] The Cooperative Development Policy provides a framework for the Cooperatives Act. It sets out a vision, makes a case for the role of cooperatives in development, affirms the international identity of cooperatives, defines the policy approach of government and most importantly defines roles and responsibilities of government to realise the objectives of the policy. Complementing the policy is the Cooperatives Act 14 of 2005 which contains 13 chapters and 2 schedules. The Act deals with definitions.

of leading structural change and transformation. The content of the cooperatives policy and Act ensures certain crucial assumptions are institutionalised.[158]

3.6.1.1 Overcoming Poverty through Co-operatives

a. Employment Creation

Co-operatives are main drivers for employment creation and this may be demonstrated in three different ways. Firstly, co-operatives offer direct wage employment towards people who work in primary and secondary co-operatives as well as in governmental co-operative support institutions for instance in ministries, departments, and co-operative colleges. Secondly, co-operatives offer self-employment to members, who participate in the economic activities of the co-operative so that they make a possible decent income.[159] Thirdly, co-operatives also indirectly employ through their spill over effects, their activities on non-members whose income-generating activities are only viable through the transactions they have with, as well as opportunities created by, co-operative ventures.[160]

By employment creation, generating income and facilitating financial flow for the members and non-members, co-operatives also make available to the member financial resources that are used to participate in activities through which a living is earned. Co-operatives, therefore, significantly contribute to both members' and non-members' access to financial capital in Africa and across the world.

b. Investing in Human Capital

Poverty is manifested by certain signs which include ignorance, illiteracy and poor health; however these signs are also causes of the poverty[161]. Therefore, efforts towards improving on the delivery of educational and health services are vital for poverty reduction. Co-operatives have made a contribution towards this cause in three different ways. First, members of co-operative societies use the income that

[158] Ibid.
[159] See DTI at 119 opcit.
[160] Ibid.
[161] Ibid.

these societies make possible to educate their children, with a view to reducing poverty in future following children's employment.[162]

Moreover, secondly co-operatives also operate as educational centres for their members. Many members emancipate themselves by optimising economic opportunities through co-operative educational programmes. A clear example is that of Rooibos Tea Co-operative Society in South Africa. Rooibos is a tea plant that grows naturally in a dry, mountainous region north of Cape Town.

The success of the co-operative society demonstrates the power of investing in human capital. Wanyama states that, "In 2000, some small scale farmers, who had been familiarised with organic tea farming by a representative of an environmental NGO, decided to form the co-operative with a view of establishing a facility to process tea before it could be delivered to a rooibos marketing company. After a while, there was discontent with the price the company paid for the tea. The organizational dynamics of the co-operative soon enabled members to learn that they could get a much better price by marketing their tea through a local fair trade agent who was promoting the marketing of organic agricultural produce rather than the company".[163]

Wanyama adds on and stated that, "The better price that the farmers received on marketing their tea through the said agent served as an eye opener to the economic potential of rooibos tea farming that they decided to lease a centrally located facility to increase production. The venture was so successful that the co-operative started realizing a substantial surplus. The 100 South African rand (US$. 15.6) entrance fees contributed by the fourteen founding members in 2001 had raised an initial capital of only 1, 400 rand (US$. 222.2)". [164]

At the end of 2004, the co-operative had recorded so much success that Wanyama added that, "the co-operative membership had increased to 36 with a turnover of 1.25million rand (US$. 198,412.7) and assets valued at 896, 708 rand (US$. 142,334.6), including a truck to deliver the tea, a welding machine and a tractor used

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[162] Mrema, H. A. 2007, Uganda: Starting all over Again, in P. Develtere, I. Pollet & F. Wanyama (eds.), Cooperating out of Poverty: The Renaissance of the African Cooperative Movement, ILO/The World Bank Institute, Geneva/Washington D.C., forthcoming.
[163] See Wanyama at 145 opcit.
[164] Ibid.

in the production of tea. Of significance to the educational needs of the members is that the co-operative committed 30% of its annual profit to the training of those members who, in the opinion of the board, have been most disadvantaged for their race and/or gender to undertake sustainable economic activities. The training and development programmes in this regard have included various topics ranging from financial management to global climatic changes that affect tea production".[165]

c. Social Protection

In terms of co-operatives, it refers to the societal security mechanisms in anticipation to the unexpected socio-economic risks that people meet in their livelihoods. The Traditional African society relied on such a mutual aid to secure every individual from disasters that would happen anytime and beyond the individual's control. In its most basic form, mutual aid on a daily basis would find expression in interfamilial and neighbourly help ranging from bringing back strayed cattle; tending the crop of someone fallen ill; chasing away marauding wildlife; and helping family, kin and villager to ease the burden of death by meeting the expenses of a funeral, among others.[166]

Recently co-operatives have moved towards more complicated forms, which include provision of financial services. Financial co-operatives have formulated advanced banking services and cash salary advances that are popularly referred to as "instant loans". Under certain conditions, financial co-operative's approved and paid these advances in less than one day.[167] Unlike emergency loans, these advances are payable on a shorter period of time, usually not more than six months, and the ceiling on borrowing depends on the individual's ability to repay within the stated period of time. However, they can be accessed within a very short time to respond to unexpected emergencies. It is in this regard that instant loans are increasingly

[165] Theron, J. (2007), Cooperatives in South Africa: A Movement (re-)emerging, in P. Develtere, I. Pollet & F. Wanyama (eds.), Cooperating out of Poverty: The Renaissance of the African Cooperative Movement, ILO/The World Bank Institute, Geneva/Washington D.C., forthcoming.
[166] Bouman, F.J.A. 1995, ROSCA: On the Origin of the Species, Savings and Development, Vol. 19, No. 2, pp. 117-148.
[167] Evans A. C. 2002, The Unpaved Road Ahead: HIV/AIDS & Microfinance: An Exploration of Kenya Credit Unions (SACCOs), Research Monograph Series No. 21, World Council of Credit Unions, Madison, Wisconsin.

becoming more popular than emergency loans though their repayment terms are shorter and interest rates higher.[168]

3.6 Conclusion

This chapter has exposed the main challenges encountered by Co-operative Financial Institutions in South Africa, chief amongst these being the failure to register. Lessons have been drawn from the success story of Ditsobotla Co-operative Bank, which managed to meet the requirements and was the first co-operative bank in South Africa. Therefore, solutions were brought forward to assist other co-operative financial institutions to also meet the requirements.

It went further to assess and critique the potential contribution of co-operatives towards economic development. Co-operatives are a lucrative opportunity to achieve socio-economic development and to establish communities that are self-reliant. Co-operative Financial Institutions may contribute significantly if proper regulations are put in place, and the government render sufficient support towards co-operatives to allow them to grow and be self-sustaining. Poverty is also another main challenge in South Africa, co-operatives are a way to emancipate people to stand on their own and develop their own businesses. Cooperatives are drivers for economic growth and sustainable development especially for the disadvantaged, vulnerable and marginalised people in societies as well as those with limited resource capabilities; therefore co-operatives are essential to achieve socio-economic development.

Co-operative Financial Institutions have so much to offer, and the Co-operative Banks Development Agency must put in place mechanisms to assist the growth of this industry to allow more people to participate in order to eradicate unemployment, destitution and overall poverty.

[168] Ibid.

CHAPTER FOUR: COMPARATIVE STUDY

4.1 Introduction

This chapter will draw comparisons from Kenya and Canada on how they regulate the field of financial co-operatives in order to note areas where South African co-operatives need to improve. It further demonstrates how this sector is performing within a local and global context. A study by the Department of Trade and Industry confirmed that co-operatives were undeniably making a reasonable contribution in the economic and social development of many communities around the world and that this type of business venture could also be beneficial to South Africa.[169]

Therefore, to ensure a success story in the co-operative sector, lessons from other countries must be taken into account to inform a proper strategy that will improve the co-operative sector. In the year 2012, the United Nations declared the year as a year of co-operatives and urged all member states and various key players and stakeholders to promote them.[170]

The Sector of co-operative financial institutions in developing countries faces notable challenges. In many developed economies, Financial Cooperatives (FCs) and their networks are well-developed and have large shares of the financial services market.[171] The co-operatives contribute significantly to the Gross Domestic Product (GDP), and South Africa needs to follow the same path.

However, financial co-operatives in most developing countries are under-resourced and consequently have negligible market shares. Financial cooperatives in developing countries are limited by restrictive legal frameworks, low capacity, absence of an appropriate regulatory framework, and lack of sufficient supervision.[172] These are some of the challenges South Africa is succumbing to, therefore this chapter aims to draw some of the success stories and apply them to the South African context. The comparison is based on examples of both an underdeveloped country and a developed country in order to strike a balance and

[169] Department of Trade and Industry (2004). NEDLAC Study Tour, *Baseline Study of Co-operatives*.
[170] United Nations, (2010).
[171] Nair, A. Todd, R.K. 2007. Reaching Rural Areas with Financial Services: Lessons from Financial Cooperatives in Brazil, Burkina Faso, Kenya, and Sri Lanka. Agriculture and Rural Development Discussion Paper 35.
[172] Ibid.

draw a proper unbiased conclusion that will improve the co-operative sector in South Africa.

4.2 Financial co-operatives in Kenya

Co-operatives have a long standing history around the world and have recorded success stories. They have also proven to be remarkably adapted in meeting a wide variety of social and economic human needs.[173] Kenya adopted a model of co-operative development in which the government not only leads, but also makes concerted efforts to foster strong partnerships with the co-operatives movement.[174] Kenya as a developing country has made strides in the co-operative industry as a main drive for socio-economic development.

4.2.1 Background of Financial Co-operatives in Kenya

Kenya has one of the most fast growing co-operative industries, especially co-orporative financial institutions. Co-operatives have played a crucial role in sustaining the Kenyan economy since pre-independence days with its first co-operative society being registered in 1908.[175] The growth and development of co-operatives in Kenya may be attributed to two major factors which were intensive colonization which left the majority of Africans outside the mainstream economy until the late 1950's and the extensive participation of the government in the affairs of the co-operatives afterwards. While there were initially no legal and policy structures in place, co-operatives grew through white colonial farmers' agitation.[176]

Upon attaining its independence in 1963, the Government of Kenya's strengthened its policy of involving the participation of all Kenyans in the economic activities of the new nation; such policies guaranteed that co-operatives remained significant. A paper[177] on the topic of, "African Socialism and it's to Planning in Kenya" that was promulgated by the Government of Kenya promoted principles similar to those adopted by the Co-operative Movement. Co-operatives were considered as suitable vehicles with an appropriate framework for Kenyans' participation in economic

[173] See Department of Trade and Industry at 169 opcit.
[174] Ibid.
[175] Conference Paper. 2012. Co-Operatives As Potential Channel For Enhancing Financial Inclusion. Abuja Nigeria.
[176] Ibid.
[177] Sessional Paper No. 10 of 1965.

development. The main objective was to ensure that the public and co-operative sectors grew simultaneously together and to hold a large percentage of the economy.[178]

This also led to the emergency of financial co-operatives which are deposit taking institutions. Kenyan co-operative financial institutions are known as Savings and Credit Co-operative Societies (SACCO). The growth and expansion of the industry led to the enactment of a SACCO Societies' Act in 2008 to provide for the enforcement of prudential standards for SACCO's[179]. This led to the introduction of the SACCO Regulatory Authority (SASRA) which is a body tasked with the responsibility of regulating deposit-taking SACCOs.

The year 2011, financial co-operatives in Kenya accounted for 60% of the total number of registered co-operatives which are 14, 126 in total, this makes it the most active segment in Kenya's co-operatives. The end of the financial year only had half of the registered financial co-operatives active. An active co-operative legally means one which filed annual audited accounts with the Kenyan Ministry of Co-operatives. Kenyan co-operatives are structured based on employment, trade, small-scale industries, and transport. This affords the members a chance to accumulate savings thereby creating a pool from which members can access credit on favourable terms for personal growth and enterprise development purposes.

The end of the 2011 financial year, the active SACCO's in Kenya had noted a significant growth in membership, which was about 4.5 million members and had accumulated deposits and share capital totalling 2.25 billion US dollars and extended loans to members to the amount of 2.25 billion US dollars. The total assets and deposits of the SACCO's which excludes the SACCO Unions stood at 2.95 billion US dollars and 2.1 billion US dollars by close of 2011 financial year.

Since the 1970's, SACCOs have shown rapid expansion, with the most growth being recorded in 1990, this was when commercial banks closed their operations in rural areas by merging their branches, centralizing services and automation which left small depositors, mainly in rural areas, without banking services. This led banks to

[178] Ibid.
[179] The Republic of Kenya, Ministry of Industrialisation and Enterprise Development, (2014). History And Organization Of Cooperative Development And Marketing Sub Sector In Kenya.

increase their minimum deposits for opening and maintaining bank accounts. This change in the banking sector led to the introduction and fast growth of quasi banking services by rural SACCO's through the Front Office Service Activities (FOSA). This provided with alternative banking services to thousands of farmers, teachers, civil servants and other low and middle income individuals since they could access salaries and crop proceeds paid through their SACCO.

4.2.2 Law regulating Financial Co-operatives in Kenya

Financial co-operatives play a significant role in Kenya's economic climate, and the Government of Kenya has taken notable strides to regularise the industry. Kenya's Co-operative movement is currently ranked first in Africa and seventh internationally.[180] Furthermore, the World Council of Credit Unions (WOCCU) also stated that SACCO's was the fastest growing sub-sector in the world.[181] This means that a lot can be learnt from Kenya's financial institutions, and be applied to South Africa.

In Kenya, there was no legislation, regulations or specific rules controlling SACCO's or financial co-operatives, until 2004. Since SACCO's are co-operatives, they were administered under a general co-operative legislative framework. The growth and development of quasi banking business or Front Office Service Activity (FOSA) demanded that appropriate regulatory framework be passed to address the exceptional aspects of quasi banking business and the risks associated with it.[182]

The regulatory reforms implemented in the SACCO sector in Kenya have been inspired by the need to position SACCOs as an integral part of the Kenyan financial sector and in turn makes it a reliable place to save money. This led to the enactment of the Sacco Societies Act of 2008, which is a risk based regulatory framework and also the creation of the Sacco Societies Regulatory Authority (SASRA) to license and regulate the Sacco societies. This legislation provides for the operational regulations and prudential standards which are the same as those required of banks

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[180] See footnote 179 opcit.
[181] Ibid.
[182] See footnote 171 opcit.

or deposit taking microfinance institutions to give effect to the primary objective of protecting member deposits.[183]

The new legislation provides that SACCO's are required to keep larger amounts of funds in reserves and to ensure strict compliance with prudential norms. The SACCO Act provides for:-

- "The registration and licensing of SACCOs;
- Prudential requirements;
- A standard chart of accounts;
- Governance requirements, amalgamations, divisions, and liquidations;
- A SACCO Regulatory Authority;
- A Savings Protection Insurance;
- A Central Liquidity Fund;
- Information sharing; and
- Transitional provisions".[184]

The regulatory frameworks, policies and provisions in Kenya have clearly allowed an environment wherein co-operatives may thrive and grow. The industry is also well monitored and compliance with the laws is strictly adhered to, therefore the SACCO Societies Act has gone a long way in ensuring that financial cooperatives contribute significantly to socio-economic growth in Kenya.

4.2.3 Analysis of Financial Co-operatives in Kenya and South Africa

Therefore drawing comparisons between South Africa and Kenya, similarities may be noted and on the same breathe some differences are also prominent, and Kenya has made progress on its financial co-operatives which South Africa may draw lessons from. An analysis of Kenyan SACCO's clearly reviews that co-operative financial institutions are one of the main drives for economic growth in the country since they contribute billions and offer employment opportunities. The Ministry of Co-operative Development in Kenya estimated that at the end of the 2011 financial year,

[183] Ibid.
[184] See Nair at 171 opcit.

financial co-operatives accounted for 60% of the 14,126 registered Co-operatives and form the most dynamic segment of the co-operative sector in Kenya.[185]

The Kenyan government came up with policies to redefine the co-operative industry in the country. Some of these reforms included the boosting of alternative financial service providers such as SACCOs and MFIs to complement the commercial banks especially among individual Kenyans and small businesses segments of the financial services market. Therefore, listed below are some of the policies that have informed the legal and regulatory framework for co-operatives which includes financial co-operatives so as to make them more effective in serving the needs of their members in Kenya.

a. Prudential regulation of SACCOs

The Kenyan Government emphasized the crucial need for a legislation that promotes transparency and accountability in the management of SACCOs. The Act would promote financial stability of SACCOs as financial service providers and also increase public confidence in the sector, which would attract more members who would make use of the services. Therefore, the government promulgated the Sacco Societies Act in 2008 and the establishment of the Sacco Societies Regulatory Authority (SASRA) to license and regulate the Sacco societies.

In comparison to South Africa, the Co-operative Banks Act was also enacted for this purpose. The Act provides that its main purpose is to promote and advance the social and economic welfare of all South Africans by enhancing access to banking services under sustainable conditions.[186] The Act provides for the establishment of a Development Agency for Co-operative Banks to develop and enhance the sustainability of co-operative banks.[187] The provision led to the establishment of the Co-operative Banks Development Agency (CBDA), which has the primary responsibility of overseeing all co-operative banks in the Republic to ensure compliance, and proper registration of such banks. The CBDA has the same purpose as SASRA in Kenya.

b. Refining Governance reforms in the Co-operative Sector

[185] Ministry of Co-operative Development and Enterprise, Kenya.
[186] Section 2(a) of Act 40 of 2007.
[187] Section 2(c)(ii) and (iii) of Act 40 of 2007.

In Kenya, the management and control of co-operatives has certain challenges especially if the leaders are democratically elected, this means that such candidates lack the requisite skills to manage. The Kenyan Government therefore ensured that the regulatory framework in place oversees the election of leaders who are accountable and dependable to members of the co-operative by inciting best management practices. This is supported by a code of conduct, rotational elections of directors, declaration of wealth, strategic plans, member education, annual audits and general meetings of members every year. This gives a guarantee that members evaluate and hold the directors to account.

The Co-operative Banks Act also promotes corporate governance through the King III Code. The CBDA ensures that there is corporate governance, and also application of the principles of corporate governance as outlined in the King III report.[188] These principles would assist towards proper governance of CFI's. However, CFI's in South Africa still need training as far as these aspects are concerned, hence they must take lessons from Kenya.

c. Evaluating the role of Governance in the Co-operative Sector

When government plays a more dominant and central role in the management of co-operatives, an atmosphere of dependency is created and that in turn disturbs production. The policy currently operating in Kenya is one which moderates the involvement of the government and allows co-operatives to conform to the co-operative principles while ensuring sound management of the co-operative. The regulatory framework by Government should therefore promote such practices and appropriate enforcement actions taken for non-compliance.

This is an important lesson which South Africa may also derive; CFI's must also be given an opportunity to develop their own systems with relatively low government

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[188] King Report on Corporate Governance III of 2009, the principles include:

- Ethical leadership and corporate citizenship,
- Boards and directors,
- Audit committees,
- The governance of risk,
- The use of information technology,
- Compliance with the laws, codes, rules and standards,
- Internal audit,
- Governing stakeholders relationships, and
- Integrated reporting and disclosure.

involvement. However, the government must ensure that regulatory frameworks are in place that safeguards the interests of the members.

d. Promotion of self-regulation in the Co-operative Sector

The Kenyan government realised that there was a need to strike a balance between regulation, facilitation and control. Considering the fact that financial co-operatives are private businesses, they should be controlled in such a way that the system rewards those that comply with the law and are properly managed, at the same time punish those that contravene the law. This ensures a system of checks and balances and hence promotes self-regulation within the Financial Cooperative System which will reduce extra Government involvement in the Co-operatives management.

Compliance with regulations is also one of the main problems facing the South African cooperative movement. The main challenge is that most CFI's fail to meet the requirements for registration because of non-compliance with the provisions of the Act which includes appointing a board of directors and submitting annual financial statements to the CBDA. Therefore if more severe penalties are imposed to those CFI's that do not comply with the regulations will go a long way in ensuring that other CFI's comply for fear of such stiff penalties

e. Boosting Co-operative Education and Training

Kenya, as a country with a well-developed co-operative industry has fairly developed national co-operative infrastructure that is well equipped towards provision of education and training to co-operatives. Therefore the primary concern is the quality and relevance of the trainings in order to develop management and leadership that are capable of directing and controlling co-operative enterprises for the benefit of members. This means that emphasis should be made on the duties and responsibilities of members and understanding of their triple role as members, customers and owners of the Co-operative enterprise. The Government should set standards to guide institutions that undertake Co-operative education and training including financial Cooperatives.

South Africa on the other hand lacks the essential training to Co-operatives to allow them to familiarise with the requirements of the Act which includes annual financial statements and regular audits. Most financial co-operatives in South Africa are owned by black people who are uneducated and incapable of meeting some prudential requirements of the act. Therefore the Kenyan model of allowing training for co-operative members allows for efficient management and leadership, as already pointed out Kenya has a fairly developed co-operative infrastructure.

4.3 Financial co-operatives in Canada

Canada as a developed country has also adopted policies that favour the development and sustainability of co-operatives. The United Nations has also evaluated and noted that co-operatives play a significant role in economic growth that on the 18th of December 2009, the General Assembly proclaimed the year 2012 to be the International Year of Co-operatives. Canada was also on the forefront of supporting this resolution since co-operatives contribute to economic development and social uplift. Therefore, the proclamation by the UN urged governments to create a conducive environment for the development of co-operatives and to inspire them to contribute more to economic growth in the countries in which they operate.[189]

4.3.1 Background of Financial Co-operatives in Canada

Co-operatives have played a crucial role in the Canadian economy, the most dominant co-operatives being in the agricultural and financial sectors.[190] In order to get a clear picture of the financial co-operatives in Canada, the most popular co-operative movement is known as the Desjardins; it is regarded as the biggest financial service provider in Quebec province and is the fifth largest in Canada.[191]

The Desjardins movement began in the year 1900. The financial co-operative movement also known as *Caisse Populaire* was established as a result of the high interest rates that were charged by money landers at that time. The development of these credit unions grew rapidly after there were laws put in place to regulate them; as a result 200 credit unions were formed before 1920. This was the same year that the founder of the movement, Alphonse Desjardins died at the age of sixty-five. After

[189] Richards, B. 2012. Status of Co-operatives in Canada: Report of the Special Committee on Co-operatives. Public Works and Government Services Canada.
[190] It is a credit union in Canada.
[191] Sriram, M.S. Financial Co-operatives in Quebec, Canada: A Study of the Desjardins Movement.

1920, the growth of the credit unions continued to rise and a federal body was established to promote, regroup and strengthen the activities of the credit unions.[192]

The growth of credit unions continued in Canada, that by the year 1932 several regional federations had been established. The regional federations all fell under a single provincial confederation and the duty to inspect the credit unions was assumed by the confederation. In 1930, the movement had grown remarkably to an extent that by 1944 the number of credit unions had reached nearly 900 with over 300 000 members, and assets totalling $92 million. During those years, more regional federations were also established.[193]

The movement had advanced that by the year 1979; it had become computerised and installed automated banking for its members. The Desjardins movement was one of the first institutions in Quebec to adopt technology at such an early stage. In 1979, a *Caisse Centrale Desjardins* was established with its primary responsibility being the movement's financial agent in the international markets. In 1981, the Desjardins acquired the VISA network franchise and also set up its own network of automated teller machines (ATMs).[194]

At present, the range of financial services that the movement offers varies from provision of loans, banking services which include checking accounts, term deposits, credit and charge cards, automatic teller machine counters to internet banking. Besides banking, the movement is involved in insurance, marketing of mutual funds, investment services for individuals and corporates, brokerage services and international services including export and import financing, currency accounts, travellers cheques and so forth.[195]

4.3.2 Benefits of Co-operatives in the Canadian Economy

a. Contribution to economic growth

Co-operatives contribute significantly in many sectors of Canada’s economy. The most popular co-operatives have been the agricultural and financial sectors (credit unions and *caisses populaires*), however co-operatives have extended to other fields

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[192] Ibid.
[193] Ibid.
[194] Ibid.
[195] Ibid.

and sectors such as retail, housing, child care, telecommunications, funeral services and, in the past few years, health, and arts and culture. More recently, they have entered new areas such as renewable energy and fair trade.[196]

Financial co-operatives also exercise a similar role in many Canadian communities and regions, for instance over 1,100 Canadian communities have no other financial services except those offered by credit unions.[197] Furthermore, co-operatives have exhibited so much success in areas where other forms of business failed, especially by reaching people in the most remote parts. This clearly shows that co-operatives are a formidable economic force and assist so many Canadian people.

Co-operatives have also facilitated economic development to many Aboriginal communities. The system of co-operatives was adopted by many Aboriginal communities because it is in line with their traditional way of life.[198] The co-operatives have also occupied an essential position in the marketing of Aboriginal crafts which has encouraged more economic participation and enabled them to anticipate economic ups and downs.

b. A reliable alternative for economic development

Co-operatives are carefully designed to procure goods and services and to meet the critical needs of communities especially in sectors where provisions offered by government and private stakeholders are lacking. This is usually noted in areas that are so remote that the government engages the services of private initiatives to supply such goods and services because conventional private businesses are not keen to invest in such areas since they are deemed not to be profitable.

In such cases, co-operatives are the best alternative to ensure that poverty is eradicated and to promote economic development. An example of such co-operatives is the one in Alberta, Canada that specialises in gas. At present the co-

[196] Canadian Co-operative Association. 2011. Co-operatives Helping Fuel a Green Economy: A report on Canada's renewable energy sector, Ottawa, Canadian Co-operative Association, New futures: Innovative uses of the co-op model, Ottawa.

[197] Guy, D. 2012. Executive Director, Canadian Co-operative Association, Evidence, Meeting No. 3, 1st Session, 41st Parliament, Ottawa.

[198] Morrisson, A. 2012. Chief Executive Officer, Arctic Co-operatives Limited, Evidence, Meeting No. 6, 1st Session, 41st Parliament, Ottawa.

operative manages over 100,000km of gas pipelines. This area was deemed not to be profitable, but the co-operative model thrived.

c. Co-operatives as tools for Market Efficiency, Competitiveness and Competition

Co-operatives attract individual resources; this is because they make it possible for the sharing of knowledge and an increase in market competitiveness. Since co-operatives pool in resources, they provide with a platform for challenging large organisations in the market resulting in more competitive prices and services. The increase in competition allows for the supply of more innovative goods and services.

Therefore, such goods and services can eventually become the standard in a given market and escalate the competitiveness amongst the key players in that market. In the Canadian health sector, the Heath Connex co-operative in Nova Scotia exhibits the potential of co-operatives to provide innovative solutions through co-operation. The success of this form of co-operative has the potential to strengthen the model, thus eventually benefitting the Canadian population as a whole.

In addition, co-operatives can boost the efficiency of markets through their effect on prices and markets for a given product. Certain conditions must be satisfied for a market to be considered efficient, the first one being the fact that the price must be determined by competitive forces and secondly, there must be sufficient market outlets at such a price for corporate producers to sell their products.

However, large companies in certain markets may at times manipulate prices and make them artificially high or low. Co-operatives therefore represent a countervailing power against such companies and help establish a competitive relationship. Such a relationship results in more competitive prices and services and an increase in the number of market outlets. The presence of co-operatives enhances the market’s efficiency, ultimately benefiting all the communities.

4.3.3 Financial Co-operatives in Canada

Financial co-operatives are referred to as credit unions in Canada, and are seen as very strong performers on the market. Despite the economic crisis that affected many economies, credit unions continue to function as world class financial institutions. The dominance of credit unions has resulted in them performing very well and prompted a rapid increase in membership. Credit unions continue to be consolidated and have actually become a trend. In addition, they have for decades responded to increased complexity, compliance costs and changing demographic through consolidation.[199]

In the past decade, credit unions have exhibited significant growth to an extent that their balance sheets have tripled. Despite the growth noted in the upcoming co-operatives, the largest co-operatives make up a notable share of the credit union system in certain provinces. In the province of Alberta, two of the largest credit unions constitute 73% of the credit union assets and also the largest institution accounts for 58% of assets. The figures stand at 51%, 40%, and 37% for British Columbia, Saskatchewan and Ontario respectively.[200]

In Canada, credit unions have for so many years sourced for ways to carry on business in multiple jurisdictions. They have also discovered ways to acquire long term strategic investment to assist in funding their growth. With the advent of the newly promulgated federal legislation, credit unions and *caisses populaires* will have new opportunities to achieve these objectives.[201]

The Canadian Government introduced Bill C-9 on March 29, 2010, an Act which was introduced as part of the governments promise in the 2010 federal budget which seeks to introduce a framework enabling provincial credit unions and *caisses populaires* to incorporate, or continue as federal credit unions which will be under the Banks Act.[202]

Credit unions and *caisses populaires* will have to take into account the following in deciding whether to incorporate, or continue as, a federal credit union:[203]

- “The ability to carry on business across Canada under the supervision of a single regulator, the Office of the Superintendent of Financial Institutions (Canada) (OSFI);

[199] SaskCentral. 2012.
[200]Wrobel, M. 2012. Vice-President, Policy and Operations, Canadian Bankers Association, Evidence, Meeting No. 3, 1st Session, 41st Parliament, Ottawa.
[201] Elliott, R.E, McDowell, R.W, Picotte, D., Christensen K., and Mikhail, M. 2010. Federal Credit Unions: Significant New Opportunities for Credit Unions and Caisses Populaires. Fasken Martineau DuMoulin LLP.
[202] Ibid.
[203] Ibid.

- The ability to amalgamate with other credit unions in different jurisdictions (assuming they have continued as federal credit unions);
- The flexibility to issue non-membership shares, providing opportunities for strategic investments, which may include the right to elect a limited number of directors;
- Federal credit unions would be subject to the same rules as other banks in relation to permitted investments, related party transactions, business and powers (including commercial lending powers) and corporate governance;
- Federal credit unions would be subject to the same restrictions as other banks with respect to insurance distribution and automobile leasing; and
- federal credit unions would be subject to the same deposit insurance regime that applies to other banks"

4.3.4 Analysis of Financial Co-operatives in Canada and South Africa

The credit unions in Canada have been a success story all over the world and as such, South Africa can learn a lot from such a country with a well-developed economy. The Canadian co-operative sector has undergone numerous developments which include effective regulation and support from the government of Canada which has seen the development of credit unions to meet the requirements of being a federal credit union under the Canadian Banks Act.

a. Federal credit unions

The representatives of numerous credit unions applauded the Canadian Government's initiative to legislate the formation of federal credit unions. The benefit for incorporating credit unions under federal law is mainly that they may be active in several provinces outside their own province.[204] This assists credit unions to realise their business goals and improve services to their members.[205] However, these witnesses urged federal authorities to tailor the regulations accompanying the new legislation to the structure and size of co-operatives:

> "Our hope is that the federal government will continue to honour the governance structure of these credit unions, and ensure that the rules respect

[204] Lahey, J. 2012. Alternative Savings. 41st Parliament. Ottawa, Canada.
[205] Malli, R. 2012. Vancity Credit Union. 41st Parliament. Ottawa, Canada.

> the co-operative principles that laid the groundwork for the creation of these credit unions. If credit unions are simply considered and treated as “banks”, then the stability and resilience of the credit union structure may be lost, along with the co-operative values and social responsibility they represent”.[206]

The initiative may also be applied to South Africa, to allow co-operative banks to expand and establish themselves in other provinces in South Africa, by providing with sufficient Government support and regulations that allow for their expansion. The reality currently is that the few co-operative banks that have opened so far are not in position to expand because of obstacles like low membership and inadequate capital levels. Therefore the government may assist co-operative banks to expand to other provinces and increase their membership base.

4.4 Conclusion

This chapter provided with an analysis of financial co-operatives in Kenya and Canada to pave way for the development of co-operative banking in South Africa. Lessons where drawn from these jurisdictions on how they regularise and control the sector to ensure proper performance. Therefore, South Africa may also adopt some of these lessons to ensure the growth and development of co-operatives to curb poverty in the country. Financial co-operatives have, in countries like Canada brought a about a new dimension of banking and have grown to even compete with other Banks. With proper regulations and monitoring, South African co-operative banking can also reach such a state and contribute to socio-economic development.

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[206] Excerpt from the brief submitted to the Committee, dated by Concentra Financial Services Association, Evidence, July 27, 2012.

CHAPTER FIVE: CONCLUSION AND RECOMMENDATIONS

5.1 Conclusion

This chapter will provide with a conclusion and recommendations to the whole study. It would revisit the aims and objectives of the study to assess and evaluate the efficiency and efficacy of the law regulating co-operative banking in South Africa and its contribution to poverty alleviation and economic growth. The study has delved into the sphere of co-operative banking and the legal frameworks regulating it, it has further exposed some of the challenges pertinent in this field and how it’s failing to assist the disadvantaged black South Africans to enter into the commercial business sector owing to the stringent requirements to meet registration. The study further provided with a comparative analysis of Kenya and Canada on how they have managed to boost their co-operative sector.

The field of co-operative banking in South Africa faces significant challenges; the participation of the majority of black South Africans is relatively low despite the efforts being made by the CBDA to spread awareness about the benefits of financial co-operatives. The law regulating the field is fundamental in the sense that it recognises the legitimacy of financial co-operatives in South Africa; however the registration requirements make it difficult for more CFI’s and Co-operative Banks to register. To date, only a total of two (2) Co-operative Banks have been registered and are able to maintain the regulations and requirements of the Act, these are Orania and Ditsobotla.

Co-operative banking in South Africa still needs to evolve in order to allow more people to participate. Currently, the Supervisors of the CBDA have compiled a long list of reasons why CFI’s are failing to register; these include insufficient capital, lack in terms of credit risk management, sub-standard governance structures, unsatisfactory operational capacity, lack of accounting expertise, and poor management of information systems. These are some of the main challenges preventing the successful registration of financial co-operatives in South Africa. A critique of some of these challenges will clearly review that most black South Africans occupied a position of inferiority perpetuated by apartheid and as result they clearly lack the relevant expertise to run such enterprises. This is therefore the major reason for their failure to register.

The main aim for this study was to analyse the state and nature of Cooperative Banks in South Africa and challenges in the application of the Co-operative Banks Act[207] as a tool to drive socio-economic development and growth in South Africa. The study has therefore discovered that the provisions of the Act make it very difficult for upcoming financial co-operatives to register. An example of such a provision is the regulation passed by the Minister of Finance[208] which stipulated that the minimum capital adequacy ratio must be 6% of the total assets held by the co-operative bank, most of the applicants fail to meet this requirement, and subsequently do not register.

Furthermore, the Act demands that applicants must meet the minimum registration requirements of holding R100 000 in deposits and having a minimum of 200 members. These numbers are simply unrealistic considering the fact that the majority of people applying are poor and they came from some of South Africa's poorest areas. Co-operatives are mainly driven by women and the youth, therefore some of these figures demanded by the Act make it very hard for registration to be possible.

The study also assesses the contribution of co-operative banking towards economic growth and poverty alleviation. The field of co-operative banking has made significant strides towards the goal of economic growth. The industry has a total of 24 722 members, and a combined total of R236 533 481 in assets[209]. This clearly shows the economic potential of financial co-operatives and how they contribute to socio-economic growth in the country. The statistics review that co-operative banking reduces the unemployment rate and in turn eventually reduces poverty.

The main challenge with registration has therefore reduced the economic potential of co-operatives and the government is clearly not taking advantage of the economic potential that financial co-operatives may bring to the country's GDP. In Kenya, towards the end of the year 2011, the numbers stood at 4.5 million in membership

[207] Act 40 of 2007
[208] Regulation Gazette No. 9110 , 1 July No. 32357 Vol. 529 Pretoria, 2009
[209] The Co-operative Banks Development Agency Annual Report, 2014/15 pp 25

for active SACCO's, and they had gathered deposits and capital amounting to 2.25 billion US dollars. In terms of total assets and deposits of the SACCO's which excluded the SACCO Unions stood at 2.95 billion US dollars and 2.1 billion US dollars by the end of 2011. This just shows the economic potential of financial co-operatives, and with the appropriate legislative frameworks and regulations, South Africa would also reach these targets.

Considering the political history of South Africa, a lot of black people suffered as a result of apartheid. The system ensured economic exclusion for black people, and they had no access to even attend proper schools that would teach them on how to conduct or manage a business. The study therefore aims to reach out to those black people and alert them about the benefits of financial co-operatives, and how they may give them access to cheap loans and member based banking. The Black Economic Empowerment (BEE) has emancipation of the ordinary black South African at its core, and financial co-operatives are one way of doing it.

5.2 Recommendations

The study also puts forward some recommendations that may be implemented to ensure that the field of co-operative banking in South Africa meets the standard of other countries for instance Kenya. The law regulating co-operative banking is too rigid and lacks flexibility to allow co-operative financial institutions to register; there is need for legislative frameworks that allow co-operatives to thrive considering the tough economic climate. In Kenya, the SACCO Societies Act of 2008 facilitates operational regulations and prudential standards which are almost the same as those required by ordinary banks or deposit taking microfinance institutions to fulfil the primary policy objective of securing and protecting member deposits. Such an Act is also needed in South Africa to allow more co-operative banks to be established.

The Co-operative Banks Act also states that to meet registration, a CFI must at least have R100 000 in member deposits and membership of 200 people. This is unsustainable considering the fact that the CFI's fail to register. The solution to the problem could be that the Supervisors of the CBDA could appeal to the Minister to pass a regulation that states that the amount available in deposits must be able to satisfy the capital adequacy ratio, and clearly show that the CFI is solvent. A stipulated amount dismisses even eligible CFI's from becoming co-operative banks hence a CFI that satisfies the capital adequacy ratio should be allowed to register and the amount of R100 000 done away with. The membership of 200 must also be significantly reduced because the CFI's are still developing, therefore the Supervisors must grant a grace period to CFI's to allow them to build their membership base.

The CBDA must conduct more workshops, seminars and conferences on co-operative banking. This would allow more people to know that such ventures exist and allow them to organise themselves to form co-operatives. The challenge has been mainly lack of awareness, even on the requirements that are demanded by the Act. Clearly, the people who are most affected by such lack of information are the poor people who are illiterate. Therefore there must be outreach programmes even to the most remote parts of the country.

Most CFI's are failing after only a short period in business. Such failure may be attributed to the fact that they succumb to insolvency. This leads the Supervisors with no choice but to deregister such CFI's. Therefore a solution to such a problem would be to appeal to the government through the Minister of Trade and Industry to source for funds in order to subsidise such CFI's. The people who run such co-operatives are ordinary poor people so assistance from the government would go a long way in ensuring that they do not live in destitution

The world is becoming more technologized every day, as a result for co-operative banking to occupy a strong position on the economy there is need for more Information Technology in the industry. The business of banking requires advanced technology which sadly is not available. The government, private stakeholders and even the current commercial banks could donate computers and important software to upcoming CFI's.

The market is dominated with competition, and co-operatives banks are not exempted. South Africa has some of the biggest commercial banks in Africa, and such banks are monopolies in the industry. Such a situation has led to the growth of co-operative banks to dwindle. Therefore the study recommends that the government must establish co-operative banks as an alternative to commercial banks, this may be done by making sure that co-operative banks have lower interest rates as compared to commercial banks, and on the long run this would attract more people to utilise the services of co-operative banks.

The study further highlights and recommends that the BEE strategy needs to re-visited, and there is need to remove the racial biasness that it has that keeps building the gap between white owned and black owned co-operatives. Its mandate is clear of trying to address the injustices of the past and promoting historically disadvantaged groups, but however as far as co-operatives are concerned that bridge must be closed to allow participation of all sectors, and to allow it to conform to the principles laid by the International Co-operative Alliance.

Lessons learnt from Kenya, have suggested quite a number of areas in which South Africa may also improve in order to allow a sustainable co-operative industry. These include the following:-

a. Refining Governance in the Co-operative Sector

This goal may be also achieved in South Africa by making sure that the regulatory framework provides a platform for the election of accountable leaders who pursue clear and transparent management practises and are answerable to their members. This may be done through a well drafted code of conduct, rotational election of directors, declaration of wealth, member education, strategic plans, general meetings and annual audits.

b. Minimising the role of Government in Co-operative Affairs

In Kenya, it was discovered that heavy involvement of government in the management of co-operatives is counterproductive and creates a dependency syndrome. Therefore, in South Africa the co-operative movement must be given room to develop its own policies and objectives and must stay in line with co-operative principles. Therefore the regulatory framework must promote good governance and professional management of co-operatives and ensure compliance.

c. Promoting Self-Regulation

The South African Government must also strike a balance between facilitation, regulation and control. Since co-operatives are private businesses, they should be allowed to facilitate their own network and ensure that the system rewards the best managed financial co-operatives while punishing those that are not well governed. This promotes a system of checks and balances, and encourages self-regulation.

d. Boosting Co-operative training and education

The CBDA must also ensure that policy emphasis is made on the duties and responsibilities of members, so that they may understand their triple role of being members, customers and owners of the co-operative business. The Government should therefore provide training and education and set up institutions to provide such vital services.

Last but not least, the government must also ensure that CFI’s adhere to the corporative principles to ensure success. The reality is that it is possible for CFI’s to become co-operative banks as demonstrated by Orania and Ditsobotla, but the law must be amended to ensure that more CFI’s register because currently the policies that are in place are unsustainable.

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