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Ownership and Governance of Portuguese Credit Co-operatives: The Legal Framework

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Abstract

Today, financial system enterprises operate in an environment full of global opportunities and threats; and in the sequence of corporate scandals and world financial crisis, the banking activity is constrained by ethical self-restraining as well as innovative regulations enforced by domestic and global governance institutions. The dual nature of credit cooperative is reflected by their formal and institutional solutions. They need to meet both banking and cooperative regulations, especially for those dedicated to relations between the two areas; hence, they result from considering their singularity and consistency. The main aim of this paper is to provide an insight of the Portuguese legal framework of cooperative credit.

Keywords: credit cooperative, ownership, governance banking regulation

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1. Introduction

During the last three decades, unprecedented changes in communications and information technologies have created conditions to an even-more-global economy. Relatively to financial system, undoubtedly, in the second decade of the 21st century, the firm environment is full of global opportunities and threats; and in the sequence of corporate scandals and world financial crisis, the banking activity is constrained by ethical self-restraining as well as innovative regulations enforced by domestic and global governance institutions.

Over the past decade, dull but safe, cooperative banks have steadily increased their share of retail banking in Europe's credit banking market.... A 2009 study by the Bundesbank, Germany's central bank, into the connection between financial stability and bank ownership also found that co-operative banks were much less likely to fail than those owned by private shareholders....Part of the reason may lie on ownership and governance structures (The Economist, January 23d 2010: 66).

In Portugal, in respect to credit cooperatives, the law only considers the existence of agricultural credit cooperatives, the CCAM (Caixas de Crédito Agrícola Mútuo). While, origin of CCAM goes back to the XVI century, its legal birth occurred in 1911. Following the democratization of the country in 1974 and the entrance to the European Union in 1986, the CCAM witnessed a spectacular growth in their activity. This period, characterized by initial euphoria and disorganization, ends with the creation, in 1992, of a financial group, the Credito Agrícola Group. Presently, the Credito Agrícola is one of the main financial national groups. In terms of Net Assets (7th), Deposits (6th), and Dimension of the Retail Franchise (3rd). Table 1 bellow presents the four biggest Portuguese commercial banks and Crédito Agrícola market share of Portuguese banking system.

Table 1 - The Biggest Portuguese Banks, by December 2008

(Figures in EUR million and activity for Portugal only)

	CGD		BCP		BES		BPI		CA	
	Values	Market Share	Values	Market Share	Values	Market Share	Values	Market Share	Values	Market Share
Employment (n.º)	9.747	17.00%	10.687	18.64%	7.942	13.75%	n.a.	—	3.858	6.73%
Branches (n.º)	832	13.29%	918	14.66%	743	11.87%	n.a.	—	673	10.75%
Net Assets	111,060	23.29%	94,424	19.80%	75,187	15.77%	39,963	8.38%	11,447	2.40%
Equity	5484	20.83%	8559	32.52%	4653	17.68%	1315	5.00%	979	3.72%
Net Profit	459	13.34%	201	5.84%	403	11.71%	360	10.46%	121	3.52%
Net Loans	77,432	24.09%	72,372	22.51%	45,901	14.28%	27,941	8.69%	7,188	2.24%
Total Deposits	60,128	27.60%	66,264	30.41%	26,387	12.11%	19,002	8.72%	9,158	4.20%

Note: n. a. – not available; Market share in percentage.

Source: Authors' calculation based on company annual reports; Bank of Portugal and Portuguese Banking Association websites.

The table above shows that Crédito Agrícola has a significant position in the Portuguese banking system, namely, regarding employment, branches network and total deposits. A structural analysis shows that Crédito Agrícola has a high dependency of costumers' deposits and presents one of the sector best levels of capitalization.

Additionally, comparing the Group performance with other relevant national banks, the Crédito Agrícola presents an excellent position regarding efficiency, solvency, liquidity, and customers claims. Table 2 bellow shows some performance indicators of Crédito Agrícola (SICAM) and its position regarding the banking sector performance.

Table 2 – Crédito Agrícola Position, by December 2009

Performance Indicators	Values	Ranking
Transformation Ratio*	87.0%	1st
Efficiency Ratio**	49.8%	2nd
Return on Assets (ROA)***	1.0%	2nd
Return on Equity (ROE)****	12.2%	4th
Solvency Tier 1 Ratio*****	12.0%	1st
Costumer claims:		
Deposits: claims <i>per</i> 1000 accounts	0.06	1st
Housing credit: claims <i>per</i> 1000 contracts	0.89	2nd
Checks: claims <i>per</i> 10,000 checks processed	0.06	1st

Source: Crédito Agrícola (2010); Banco de Portugal (2010)

* Net Loans / Deposits; ** Structural Costs / Net Worth [Structural costs include amortisation + general administrative expenses + staff costs; Net Worth include financial margin + net commissions + other income (including results from financial operations)] *** Net Profit/ Average Net Assets; **** Net Profit / Equity; ***** Basic Own Funds / Weighted Risks (assets + off-balance-sheet items)

Crédito Agrícola presents the lowest transformation ratio. Historically, it never presented a value higher than 90%, a percentage much inferior to all the generality of the other financial institutions that exceed 100%. This fact has a positive influence in terms of CCAM liquidity. Efficiency ratio reflects CCAM efficiency-cost efforts and its ability to explore economies of scale. Indeed, in the last years CCAM were able to control the increase of structural costs bellow net worth, although the year saw some institutions with efficiency ratios down, given the harsher operating conditions. Return on operations overall was therefore good, with ROA coming in at 1%, better than most of the other banks. ROE came in at around 12.2%, an indication of the high level of financial autonomy in SICAM. Given the Crédito Agrícola cooperative nature, profits are mostly directed to the reinforcement of equity. This continuous reinforcement reflects in the solvency ratio of 12%, the best of Portuguese banking sector and much higher than the 8% imposed by Bank of Portugal. Finally, the quality of the services provided by Crédito Agrícola (valuated by the costumer claims indicator) is one of the best. Except for banking operations, the CCAM are ruled by following the traditional cooperative principles, namely, open membership, democratic control and restricted residual claims. The

dual nature of credit cooperative is reflected by their formal and institutional solutions. In recent years CCAM felt the need for some adjustments in their legislative framework and after a long process of negotiations between Bank of Portugal and the CCAM representatives, new changes were introduced in 2009, adopting a regime closest to the one ruling investor owned firms (IOF).

The main aim of this paper is to provide an insight of the Portuguese legislative framework of credit cooperative keeping in mind the specificities related with ownership property rights and governance. To achieve the goal, besides this introduction the paper is organized as follows: section 2 describes the evolution of the agricultural credit cooperative; section 3 includes the legal framework of the Portuguese agricultural credit cooperative making some comparisons with the non-cooperative banks; section 4 describes the model of governance used by the credit cooperative system; finally, the paper concludes with some final remarks in section 5.

2. Evolution of the agricultural credit cooperatives

The Cooperative Banking System in Portugal comprises only agricultural credit cooperatives. Although Portuguese Cooperative Code stipulates credit as one of the cooperative branches, there is no legal regime for credit cooperatives in Portugal but a legal regime for agricultural credit cooperatives. Consequent of Portuguese legislation only agricultural credit cooperatives can be founded in the domestic territory. This is a serious gap in the Portuguese law, since it limits the cooperative movement growth in the credit system, and is contrary to Constitutional Law and European legislation. Indeed, according to the Directive 2000/12/CE, a cooperative bank with headquarters in any other EU Member, and, therefore, authorized by their national central bank to perform banking activities there, can operate in Portugal, without the restrictions imposed by Portuguese law to domestic cooperative institutions (Fróis, 2009).

The genesis of Portuguese agricultural cooperative credit goes back to the XVI century, to an institution called Common Barns, allowing farmers to keep stocks and seek financing. The early CCAM were of small size, membership consisted of small farmers with low incomes. Management activity was exercised by voluntary individuals with no business or finance skills. This initial period was of absolute failure: the capital provided by the state was insufficient to accomplish the objectives; and the cooperatives used to pursuit managers' personal goals, being common to find management mistakes and even frauds when audited (Cabo, 2003). Despite these setbacks the number of CCAM grew significantly until the 1929 financial crisis. Consequently, CCAM cooperatives were placed under the umbrella of Caixa Geral de Depósitos, a state owned and simultaneously the biggest Portuguese bank institution.

During the dictatorial regime “Estado Novo” (1931-1974) CCAM were used to restrict the expansion of the communist ideology and to control the rural population. It was a lifeless period for CCAM. Thus, until 1976, the CCAM played a minor role in Portuguese banking system, with a share of only 1% of total deposits and credit.

Following the 1974 political changes, all private financial institutions were nationalized, except for CCAM and non-Portuguese financial institutions. CCAM started a lobby movement for autonomy, expanding implantation and broad its activity.

In 1978, occurs the creation of the National Federation of Agricultural Cooperative Credit Institutions (FENACAM), to support and represent the interests of their associates, both national and internationally.

In 1982, the sixty years old Agricultural Cooperative Credit law suffers profound alterations by the publication of a specific Legal Regime for Agricultural Cooperative Credit (RJCAM). Subsequently, CCAM run off Caixa Geral de Depósitos guardianship and, in 1984, Caixa Central was founded, whose mission was to regulate the credit activity of their associates.

In 1986, Portugal joins the European Union (EU), with the following ten years being a period of deep transformations in Portuguese economy. The CCAM were considered an important player in the framework of a financing strategy for the development of the agricultural sector. So, during the eighties of last century the CCAM activity experienced a spectacular growth in their activity.

In 1991, it was created the Integrated System of Agricultural Cooperative Credit (SICAM) formed by Caixa Central and associated CCAM. Caixa Central was empowered with the mission of supervision, intervention, guidance and representation of SICAM. SICAM establishes a regime of co-responsibility between Caixa Central and the associates, therefore solvency and liquidity supervision is accountable on consolidated basis. A more demanding framework for the creation and functioning of the CCAM, along with the reinforcement of CCAM own funds, put term to the joint liability of CCAM members. The “*agency agreement*” allowed CCAM to intermediate operations that are forbidden to them in its normal scope of activity, by acting as Caixa Central representative.

Four years later, in 1995, the RJCAM was modified, widening the scope of CCAM operations to other activities connected to rural world as hunting, fishing, agro-tourism, handcraft, and allowing CCAM to give out excesses to members (limited to 30% of net profits and once complying with legal and prudential equity requirements) and convert reserves into capital

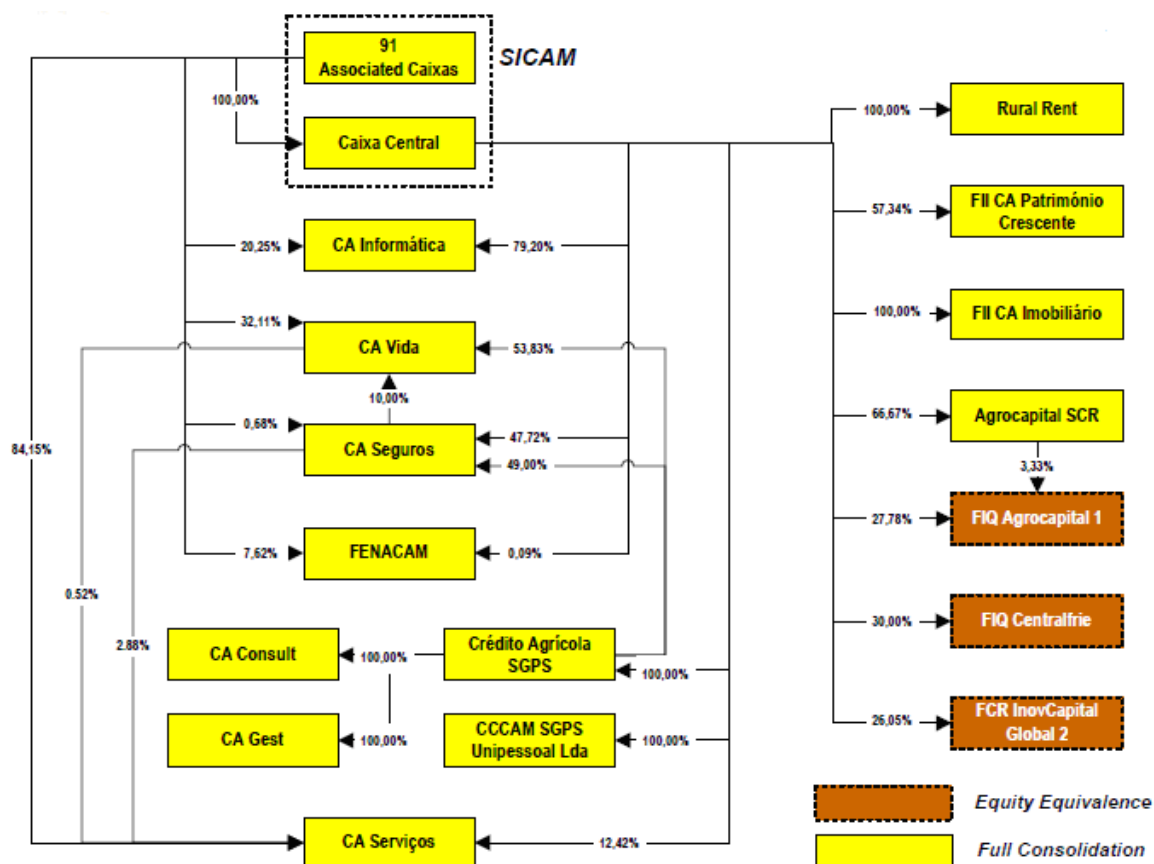
shares transferable to members. This modifications were crucial to boost CCAM ability to attract new (and deeper investing) members, improving CCAM capitalization. Additionally, the new diploma expanded Caixa Central's activities converting it into a truly universal bank.

In 2009, new changes were introduced in RJCAM adopting a governance model closest to the ruling of private enterprises and brightening up CCAM activity and membership restrictions, widening the members' scope as well as the possibility of the CCAM to carry out credit operations with no members or purposes not agriculturally related. Additionally, once CCAM comply with the prudential requirements applied to banks, they are authorized to perform the majority of the commercial activities carried out by the remaining financial institutions.

During the last two decades, along with organic growth of the CCAM a regional merging process occurred, and consequently, the number of CAAM fall from the prior 220 in the 1990s to 91 in 2009. Simultaneously the CA has direct and indirect holdings in affiliated and associated firms¹, resulting in the Group represented in Figure 1.

¹ Affiliated companies are those where the holding is more than 50% of equity. Associated companies are those where the holding is between 20% and 50% or where SICAM has a significant influence, directly or indirectly, on management and financial policy.

Figure 1 - Crédito Agrícola Group² Structure



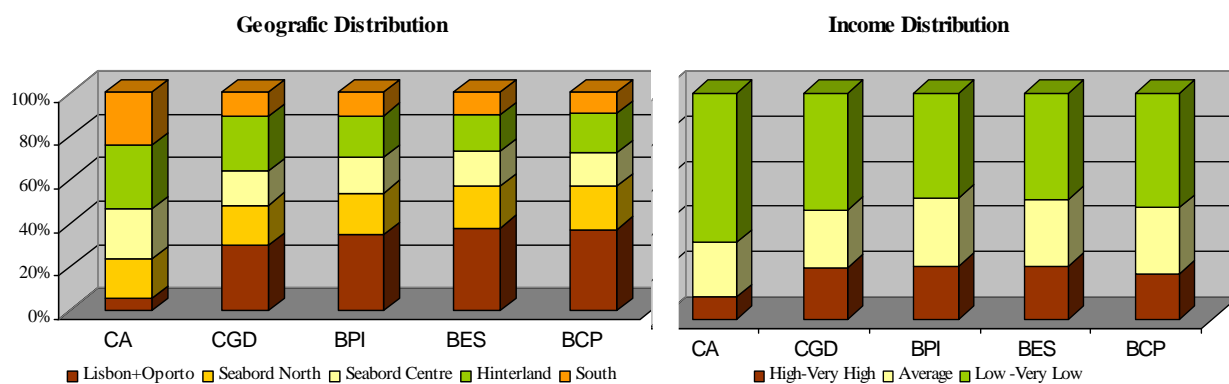
Source: Crédito Agrícola (2009)

Essentially, the agricultural credit cooperative system in Portugal is made up of an integrated system (SICAM) of two types of cooperatives: the central and the singles (associated), i.e., SICAM = Central CCAM + Associated CCAM, including 91 CCAM. Altogether, they have 681 domestic branches in mainland Portugal and the Azores Islands, plus 2 offshore branches. There is no doubt that the Crédito Agrícola robustness increases the CCAM capacity to act as financial leverage in the socio-economic development of its regions, fulfilling Crédito Agrícola corporate mission “... contributing to the development of Local Communities.” (Crédito Agrícola, 2010). The CCAM assume fully its inclusion function, being spread across all domestic territory, with exception of the Island of Madeira. SICAM network market share, at national level, except for Lisbon and Oporto Conurbations, is considerable, in some districts, more than 30% of the district banking network is owned by CCAM, and this percentage is even higher in some towns. In fact, in 250 villages, the only financial institution

² Credito Agrícola SGPS - Holding Company; CCCAM SGPS - Holding Company; CA Seguros - Non-Life Insurance Company; Rural Rent- Long Term Car Rental Company; CA Serviços - Shared Purchasing and Services Company Systems; CA Gest - Funds and Assets & Liabilities Management; CA Vida - Life Insurance Company; CA Consult - Mergers & Acquisitions, Consulting; CA Informática - Data Processing.

is the CCAM local office and, in more than about 400 other small villages the only link to the banking system is the ATM machine provided by the local CCAM. In terms of geographic distribution (Figure 2) CCAM are very different from the other banks, given that over half of its costumers (53.3%) live in the country's inland regions. The Crédito Agrícola has a special responsibility in these circumstances. Its distribution across regions means it is present in many places where the economic strength has been sapped. Thus, a very high proportion of the costumers (more than 90%) have low and moderate incomes (Credito Agricola, 2009)

Figure 2– The Biggest Portuguese Banks Costumers Profile



Source: Adapted from Crédito Agrícola (2009)

In organizational terms, the CCAM have freedom of association with the Central CCAM and they can operate outside SICAM, although the rules for this are more stringent and approximate more to those that prevail in other credit institutions. Currently, only five CCAM remain outside SICAM. The Central CCAM (holding in 100% by the CCAM) role has no parallel in the remaining financial institutions. Central CCAM is a financial institution under the cooperative form, offering a full service bank, competing in equal terms with the largest banks operating in Portugal³. Central CCAM acts as central bank for the group, creating and developing a joint banking strategy⁴.

Although Bank of Portugal are the responsible for the banking sector supervision, regarding SICAM associates the law delegates great part of these functions in the Central CCAM which, in turn, is under the Bank of Portugal supervision. The Bank of Portugal defines the relations and prudential limits applicable to the SICAM, and supervises the system accounts on consolidated basis. Central CCAM assures the fulfilment of SICAM and associated

³ The Central CCAM aims the concession of credit and the practice of remain acts inherent to the banking activity, in the same terms as commercial banks. However, it should not compete with the associates. For example, Central CCAM is authorized to open branches, in the same terms of banks, but previously it must consult the local associated CCAM.

⁴ For instance, individual excess of liquidity is transferred to Central CCAM, which can lend to non primary economic sectors or transact in the money, foreign exchange or capital markets.

CCAM solvency and liquidity rules and controls and guides them. The accounts consolidation of associated CCAM is of Central CCAM responsibility in compliance with the terms defined by the Bank of Portugal. Specifically, Central CCAM orientation powers include the definition of general rules: (a) necessary to assure the fulfilment of the solvency and liquidity rules of the SICAM and associated CCAM; (b) of commercial and credit granting policies including the setting up of guarantees; (c) regarding admission, remuneration, formation and qualification of the staff; (d) regarding to the creation of new offices; (e) to define general rules of office' operation and security.

Additionally, without damaging Bank of Portugal competences, Central CCAM is empowered to control their associated CCAM administrative, technical and financing aspects and their organization⁵ and management. Moreover, Central CCAM can intervene in the associates, by the assignment of a representative to track CCAM management or the nomination of provisory directors. When it verifies a disequilibrium situation that can jeopardize the CCAM daily running, the solvency is at risk or serious irregularities occur. Plus, when the associated is in (risk of) financial disequilibrium and unfollow Central CCAM guidelines, Central CCAM can dismiss total or part of the associated management and supervision boards and assign provisory directors to them.

Finally, Central CCAM guarantees the associates without limitations and is also guaranteed by them. In fact, Central CCAM guarantees the obligations assumed by the associated CCAM, even if they are previous to the fellowship, in the same conditions a bailer guarantees the obligations of warranted, without enjoying the right of exclusion. SICAM is, by this way, subordinated to a double guardianship, in fact Central CCAM is the direct responsible not only for the organization, but also for the associates economic and financial management.

3. Legal framework

Even formed under the idea of economic freedom, is in most legal systems, the banking and financial activity is subject to severe regulations and monitoring of supervision authorities, due of its importance to the real economy and social confidence.

The credit intermediation is the core business of banking activity. It's through deposits and other forms of collecting of savings that financial institutions obtain the necessary funds to apply in loans and other forms of credit. Under the financial institution definition provided by

⁵ Exemplifying, a Central CCAM unfavourable appreciation regarding the registration of the associates' governance bodies implies the refusal of their registration by the Bank of Portugal.

the RG⁶ lays a mix of institutions. Homogeneous types of institutions like banks along institutions with specific characteristics, as the CCAM. There are institutions that can perform all operations allowed to the banks while others only can perform the operations endorsed by the legislation ruling their specific activity. Indeed, there are two types of credit institutions: the universal and the specialized ones. The first can perform unrestrictedly all banking operations, the second have unique characteristics and only can perform the operations allowed by their specific legislation. CCAM are credit institutions specialized because of various restrictions imposed by RJCAM, namely, territorial area and authorized operations.

According to the RJCAM⁷, the CCAM are credit institutions under the cooperative form, whose goal is to perform agricultural credit operations in favour of their associates, as well as the remaining banking acts inherent to the banking activity. Thus, CCAM are under a special regime, essentially because of their cooperative form and the link to the priority goal of performing agricultural credit operations in favour of their associates.

RJCAM specifies that CCAM are created under the cooperative form, limited liability and seek, without lucrative proposes, the satisfaction of its members economic, social and cultural needs and aspirations. The CCAM present, in this way, structural and intrinsic differences to banks, since according to RG banks must adopt the public limited company (corporation) form and, therefore, aiming profit.

The RJCAM has several limitations resulting from their social object, territorial area and members' attributes. Plus, it's hard for CCAM to increase their issued share capital once they cannot publicly do it. These limitations have counterpart in minor issued share capital, organizational structure, technical and human resources available, solvency, control and accountability requirements (in individual but not in consolidate basis).

The 2009 RJCAM alterations basically aimed to adjust CCAM governance model to ones set for corporations in the Portuguese Commercial Companies Code (CCC), and, simultaneously, widen the CCAM members' base, approaching it to the other financial institutions, boosting issued share capital increase, in view of the recession felted in the agricultural sector.

The Table 3 summarizes the main features of cooperative credit and the main differences to (non cooperatives) banks, according to Portuguese legislation. The Central CCAM as mentioned above has unique features and, thus, is subjected to a separate analysis.

⁶ RG - General Regime of Credit and Financial Institutions, approved by the Decree Law n° 298/92.

⁷ Approved by Decree of Law n.° 24/91, with the following alterations, and republished in apex of the Decree of Law n.° 142/2009.

Table 3 – CCAM versus Non Cooperative Banks

	CCAM	Non Cooperative Banks	Central CCAM
Creation	Bank of Portugal approval, following the agreement of Central CCAM and FENACAM	Bank of Portugal approval	Similar to banks.
Legal form and nature	Credit Institution, Cooperative form RJCAM (and subsidiarily: RG for the banking activity, and Cooperative Code and other cooperative legislation) applies.	Credit Institution, Public limited company (corporation) form RG applies.	Credit Institution, Cooperative form RJCAM
Operations	Granting credit primarily to their members and for financing of primary sector activities. CCAM complying, in individual basis, with prudential rules settled in the RG, can perform operations with no members or financing activities outside primary sector until 35% of the net assets. Exceptionally, that limit can be raised to 50% by the Bank of Portugal for SICAM associates, by Caixa Central suggestion. Additionally, CCAM that have adequate structural conditions and sufficient funds could be authorized by the Bank of Portugal to perform mostly of the remaining activities allowed to banks, with few exceptions.	No specific restrictions applied. Operations stipulated in general to credit and financial institutions legislation and inherent to its credit intermediation function. Sufficiently ample scope: Reception of deposits or other reimbursed funds; credit operations; payment services and transactions on their costumers behalf or on its own; participation in issuing and placement of securities; operate in the interbank markets; management and consulting of assets; holding participation in the companies capital; other operations.	Similar to banks. Representation of SICAM and supervision, orientation and monitoring competences over the associated CCAM.
Membership	Singular or collective person, that carry out any activity linked to primary sector (production, transformation or services) in the CCAM territory (or adjacent). Membership outside primary sector activities is permitted but limited to 35% of the CCAM members. Exceptionally, that limit can be raised up to 50% by the Bank of Portugal. Minimum shareholding: €500 Minimum of 50 members.	There are no restrictions regarding the membership profile. Shareholdings up to 20%, 33%, or 50% of the capital social or voting rights must be communicated to the Bank of Portugal. Company bylaws.	CCAM Other entities linked to the agricultural cooperative credit, with Bank of Portugal approval.
Territorial scope	CCAM activity is restricted to their headquarter municipality. CCAM can expand to an adjacent region if there is no other CCAM operating there, or when that results from CCAM merger.	National scope	National scope
Opening of branches	The branch opening is subject the authorization of the Central CCAM for associated CCAM and of the Bank of Portugal, for independent CCAM.	No need of previous authorization	Similar to banks, requires previous checking of the local associated CCAM.

Shareholders Capital	<p>Capital is variable; it can be increased by new members' admission or higher shareholdings, or by the incorporation of reserves; or it can be reduced by members exit or lower shareholdings or by covering losses.</p> <p>Capital reduction is restrained by prudential rules. The maximum reimbursement value is defined by the accounting value net of compulsory reserves.</p> <p>Capital minimum fixed by the Ministry of Finance: 7.5 million Euros; SICAM associates: 1.496 million Euros (5 million Euros until 30th June of 2015⁸)</p>	<p>The general rules for public limited company applies, except regarding capital reduction that requires previous authorization of Bank of Portugal.</p> <p>Capital minimum fixed by Bank of Portugal: 10 million Euros.</p>	<p>Capital can be increased by new members' admission or higher shareholdings, or by the incorporation of reserves.</p> <p>Shareholding reimbursement is restrained by prudential rules and requires the General Meeting approval.</p> <p>Capital minimum fixed by the Ministry of Finance: 17.5 million Euros</p> <p>Minimum shareholding: €5000</p> <p>Maximum shareholding: 10% of capital, except in the case of extraordinary supplies.</p>
Resources	<p>Deposits and other reimbursed funds from their members and/or costumers. The access to other financing means, namely, interbank market, requires the Bank of Portugal (and Central CCAM for associated CCAM) approval.</p> <p>General financing means stipulated in Cooperative Code, namely, issuing of investment securities or debt.</p>	<p>Similar to CCAM: deposits or other reimbursed funds from the public. The access to other financing means, namely, interbank market, requires the Bank of Portugal approval.</p>	<p>Similar to banks.</p>
Financial applications	<p>Besides deposits, CCAM can make applications in public debt in conditions established by Bank of Portugal.</p> <p>CCAM can only hold participations: (a) in regional unions, Central CCAM and FENACAM; (b) in enterprises whose object is of regional interest (until 20% of own funds); (c) to assure the reimbursement of credits; (d) when especially authorized by Bank of Portugal⁹.</p>	<p>No restrictions.</p>	<p>Similar to banks.</p>
Governance Bodies	<p>The management and supervision bodies (composition and competences) stipulated for corporations apply, preserving the importance and competences of the General Meeting characteristic of the cooperative model.</p>	<p>The general governance models stipulated for public limited company apply.</p>	<p>Similar to CCAM.</p> <p>Existence of an advisory body, elected between the associated CCAM not represented in the other governance bodies.</p>
Tradability of shares	<p>No.</p>	<p>No restrictions.</p> <p>Company bylaws can impose "poison pills" or other anti hostile takeover measures.</p>	<p>No.</p>

⁸ By 30th June 2015, CCAM capital should reach at least €5 million; beginning with €2.5 million by 30th June 2011 followed by an annual increase of €0.5 million.

⁹ CCAM hold direct participations in the Crédito Agrícola specialized companies under this special authorization.

Voting rules	Principle of democracy, voting right independent of shareholding value: one member, one vote.	Principle of proportionality to the shareholding value. Company bylaws establish the conditions for voting rights acquisition and can limit voting rights exercise ¹⁰ .	Principle of democracy, excepting for some specific decisions (election of the Central CCAM board of directors, budget approval and profits allocation) in which the voting rights can differ according to the shareholding and CCAM average deposits and the solvency ratio.
Reserves	CCAM must allocate up to 50% of the net profits to the reserves: (a) at least 20% to the legal reserve until it reaches the value of issued share capital; (b) at least 20% to the special reserve for reinforcement of equity in the case of CCAM under financial restructuring process, until it reaches the value of amount to the benefits obtained with the process; (c) between 1% - 5% to the members' education; and (d) a max of 5% to the mutualism reserve. CCAM statutes can design other reserves.	Banks must allocate at least 10% of net profits to the legal reserve until it reaches the value of issued share capital. Bank of Portugal can stipulate the creation of an additional reserve to reinforce banks capital adequacy. Company bylaws can create other reserves.	Similar to banks.
Profit allocation	After covering eventual losses of previous exercises, profits not allocated to the reserves can be distributed among members. The remuneration of capital shares is limited to 30% of the results ¹¹ . Profits cannot be distributed if the CCAM do not comply with prudential rules, or if the member shareholding is inferior of the minimum required, in which case his portion of the profit will revert to it.	Profits not allocated to reserves can be distributed among members without restrictions.	Profits not allocated to reserves can be distributed among members. Associated CCAM can deliberate by majority of the entire membership voting rights profits allocation to reserves.
Supervision	Bank of Portugal. Central CCAM for SICAM associates.	Bank of Portugal, CMVM for listed banks.	Bank of Portugal
Tax Policy	Profits are subjected to a rate (IRC) of 20%; excepting the results of no members operations or activities outside cooperative purposes and the taxation on consolidated basis, in which the IRC general rules apply ¹² .	The IRC general rules apply.	The IRC general rules apply.
Deposits insurance	Insurance Fund of Agricultural Cooperative Credit. This fund besides secure the CCAM costumer deposits, performs an active role in the SICAM economic and financial restructuring process, as part of its task to promote SICAM solvency and liquidity.	Deposits Insurance Fund, limited to the simple guarantee of bank costumer deposits. The participation in restructuring operations is forbidden	Insurance Fund of Agricultural Cooperative Credit

¹⁰ Two of the biggest Portuguese commercial banks limit the voting rights for purposes of their exercise to 20%, by a statutory provision. See Table A in annex

¹¹ CCAM do not usually give out profit to members. Members' remuneration usually takes the form of capital shares allocation resulting from the incorporation of reserves.

¹² According to the Cooperative Tax Statute, Law n.º 85/98. Although, according to FENACAM (2009) cooperative credit system is, inside of the Portuguese Financial System, in percentile terms, the greater contributor. In many cases cooperative credit system taxation is triple of the other banking company.

4. The governance of the cooperative credit system

The management and supervising of CCAM is structured according to the model formats (composition and competences) stipulated by law for corporations (Commercial Code to Corporations). It's a deviation from the general cooperative organization structure of the Cooperative Code, in favour of the corporation model, but keeping the original cooperative matrix.

According to CCC, the company governance bodies include: shareholders general meeting and management and supervision bodies¹³. The management and supervision of the companies may take on a 3 model format: i) Board of Directors, Audit Board and Statutory Auditor; ii) Board of Directors, Audit Committee and a Statutory Auditor; iii) Executive Board of Directors, General and Supervisory Board and a Statutory Auditor. Table 4 in next page shows the standard organization charts.

In the first 2 model formats, the Board of Directors is responsible for managing the activities of the company, and should be subordinated to the resolutions of shareholders or to the intervention of the Supervisory Board or the Audit Committee only in those cases where the Law or the Company bylaws stipulate it. In the third model format, the Executive Board of Directors is responsible for managing the activities of the company, without prejudice to the company bylaws of the company establishing that the Executive Board of Directors is required to obtain prior consent from the General and Supervisory Board before practicing certain categories of acts. The Board of Directors may delegate management powers to an Executive Committee or to one or more Chief-Executive Officers. The Auditing activities are carried out by the Audit Board and the Statutory Auditor for the first model format, the Audit Committee and the Statutory Auditor for the second model format and the General and Supervisory Board and Statutory Auditor for the third model format. In any of the previous cases, the Statutory Auditor shall proceed with the examination and statutory audits. The General and Supervisory Board shall appoint a Financial Matters Committee that is solely responsible for carrying out a set of supervisory duties provided for by Law (CMVM, 2007).

The General Meeting is the supreme governing body of cooperatives, is composed by all the cooperative members enjoying full rights. Decision making process is democratic (one member, one vote) and its decisions are mandatory for the other social bodies and to all cooperative members.

¹³ Other governance bodies: i) Company Secretary- by Law, quoted companies must appoint a Company Secretary. The Company Secretary, in addition to the administrative functions of keeping the records of meeting minutes of board and general meetings and keeping and certifying documents related to them, is also responsible for answering questions made by shareholders under their right to information and to certify company actions; ii) Remunerations Committee- the Remuneration Committee's function is to fix the remuneration of the governance bodies members, and to formulate the remuneration policy and the retirement regime to apply.

Table 4 – Corporations Standard Governance Model Formats

Corporations Governance Bodies	Standard social organization charts
<p>Model 1 - General Meeting, Board of Directors , Audit Board and Statutory Auditor*</p> <p>*The existence of a Statutory Auditor, independent of the Audit Board is mandatory</p>	<pre> graph TD GM[General Meeting] --- SA[Statutory Auditor (ROC)] GM --- BD[Board of Directors] GM --- AB[Audit Board] </pre>
<p>Model 2 - General Meeting, Board of Directors, Audit Committee** and Statutory Auditor</p> <p>** Audit Committee members are non executive Directors</p>	<pre> graph TD GM[General Meeting] --- BD[Board of Directors] GM --- SA[Statutory Auditor (ROC)] BD --- AC[Audit Committee] </pre>
<p>Model 3 - General Meeting, Executive Board of Directors, General and Supervisory Board, Financial Matters Committee*** and Statutory Auditor</p> <p>***The existence of a committee for financial matters in the general and supervisory board is mandatory.</p>	<pre> graph TD GM[General Meeting] --- EBD[Executive Board of Directors] GM --- GSB[General and Supervisory Board] GM --- SA[Statutory Auditor (ROC)] GSB --- FMC[Financial Matters Committee] </pre>

Matters of the General Meeting exclusive competence, according to the Cooperative Code: i) electing and dismissing cooperative bodies members; ii) deliberating on the annual report and accounts, as well as the audit board report; and on the next year's budget and plan of activities; iii) appreciating certificate audit reports; iv) setting the interest rates payed to members and remuneration of the cooperative social bodies members, when the bylaws allow it; v) approving profit distribution; vi) amending bylaws and internal regulations; vi) approving cooperative merge, split or dissolution and its affiliation in unions, federations and confederations; vii) deliberating on members exclusion and social bodies' loss of mandate, and acting as appeal court, for the admission or refuse of new members, or for the sanctions applied by the management body; viii) deciding of the right of civil or criminal action against cooperative management and supervision members; ix) appreciating the matters included in the Cooperative Code, complementary specific arm legislation or in the bylaws.

The majority of SICAM associated CCAM have adopted the model 1 format and central CCAM opted for the model 3 format, with an Advisory Board as mandatory by RJCAM *"...comprising of a maximum of 15 members, of which 9 correspond to CCAM elected among the associates not represented in the other social bodies, and the 6 remain to non elected members, being the corresponding places filled up for inherence of functions or by personalities of recognized merit, external to the SICAM"*.

These 6 (not CCAM) advisory members are an innovation of 2009 RJCAM and an effort to bring some independence and outside SICAM expertise to Crédito Agrícola management. Additionally, contrary to former RJCAM (that specified the advisory board competences), this RJCAM amend left open the advisory board competences to be defined by Central CCAM bylaws.

Although Crédito Agrícola performance compares favourably with that of other credit institutions, individual CCAM occasionally do enter in distress as illustrated by history. The increasingly large size of the CCAM raises concerns regarding the resolution of potential distress situations given some of the cooperative governance rules.

In particular, the restrictions on control rights and residual claims linked to the cooperative governance framework limits the range of options for resolving systemically important CCAM as it makes raising capital more difficult for these organizations. Vaguely defined ownership rights combined with restricted voting rights might prevent raising capital from existing and new members, particularly at time of distress when large investors are more likely to provide capital injections. In the past, resolution of CCAM typically involved the merge or incorporation of the weak CCAM by another CCAM (Cabo and Rebelo, 2005a).

However, this resolution mechanism is more difficult to apply to a large systemic CCAM. Also, CCAM regional orientation can be a strong constraint to find another CCAM able to absorb it, without losing their territorial identity.

Plus, the cooperative governance structure limits shareholders control over management. Democratic decision making and weak ownership property rights result in minimal contributions. The resulting diffusion of ownership property rights exacerbates, according to agency cost theory, owner-manager conflicts, given that members typically do not have the incentive to exert effective control over management. Moreover, some effective mechanisms of management control such as the threat of takeover are virtually nonexistent due to the voting rule. Within SICAM management control are often exercised by Central CCAM that operates the orientation and supervision function and therefore, is the first to learn about managerial failures. In cases of gross management failure or fraud, the management can be formally dismissed by the Central CCAM, under its supervision and intervention powers. Cabo and Rebelo (2005b) show the importance of this mechanism in disciplining bad management in the presence of decision-related incentive problems of cooperatives, which create a potentially weak internal system of corporate governance. However, this solution is not free of costs and not only financial costs. The social costs of these interventions are far more dangerous. Civil actions and protesting movements against Central CCAM interventions questioning their legitimacy are usual. The most recent polemic involves the dismissal of the management and supervision bodies of a CCAM even before they are in office. On the other hand, endless interventions are not unusual, as illustrated by the more than ten years intervention¹⁴ on two of the major associated CCAM. In this case is difficult to defend the cooperative status of a CCAM, once it is no longer a user-owned and user-controlled business.

Most of the governance reform proposals within the cooperative credit involve some level of cooperative principles sacrifice. But surprisingly, the solution for the CCAM governance problems might lay in the Cooperative Code. Indeed, implementing proxy voting or promoting the issuance of nonvoting shares and hybrid capital instruments granting investors the right to appoint a delegate to assist at the supervision body meetings, as referred in Cooperative Code, can enhance shareholders participation and provide additional capital in distress times.

¹⁴ Interventions have up to one year of lifetime, after that it can be renewed.

5. Final remarks

The Portuguese credit cooperative system is a typical example of how public entities can influence the development of the credit cooperative institutions. Until 1990's of last century CCAM have no control over its own life. Been developed in a top-down process, the CCAM depend on public funds to carry out its mission and were often used to accomplish political goals. Indeed, CCAM were used to put on the field the public vision to the rural economy and rural population.

Like cooperatives in other sectors, the CCAM increasingly face survival challenges related to financial issues linked with equity capital. Being not-for-profit enterprises CCAM do not have access to publicly raised capital. Thus, CCAM capital base growth is supported by their retained profits. During 1990s the solution adopted by them to overcome this constraint was based in the creation of an economic group and an intense process of mergers. This strategy allowed the CCAM to benefit of scale and scope economies and improve their financial structure. Additionally, legislative changes delegating to Central CCAM part of Bank of Portugal supervision competences proved to be beneficial to control the CCAM management. Presently, CCAM system enjoys of a healthy financial situation, however its pursuit of economic and financial success are driving the CCAM away from the cooperative identity and diluting their cooperative advantages. CCAM face the challenge of matching the application of the traditional cooperative rules (along with the resulting set of vaguely defined property rights) with being successful in an ever more strong and competitive banking sector. Worldwide cooperatives have adopted varied strategies to beat difficulties inherent to the cooperative form. Most of the solutions presented are based in some degree of deviation from the traditional cooperative principles. CCAM implemented a very different strategy. They opted to focus their efforts on the cooperative activity and performance rather than on the cooperative rules it selves. Still, facing an increasingly competitive banking sector, the 2009 RJCAM changes ameliorate CCAM activity (product and territory) restrictions and near their governance model to the corporations' model. It's an alteration that distances RJCAM from the Cooperative Code. Nevertheless, is in the Cooperative Code that CCAM can find the solutions for some of their governance problems without losing their identity.

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Table A - The Biggest Portuguese Banks Governance Models*

Governance Bodies		Voting rights
<i>CGD</i> Model 1	<ul style="list-style-type: none"> • Board of General Meeting: 3 members (Chairman, Vice-Chairman, Secretary) • Board of Directors: 7 members (Chairman, Vice-Chairman, 5 Directors); • Audit Board: 3 members (Chairman, Vice-Chairman, 1 Director) • External Auditor • Company Secretary 	The Portuguese State is the only shareholder, being represented in the general meeting by a person assigned by the Minister of Finance.
<i>BCP</i> Model 3	<ul style="list-style-type: none"> • Board of General Meeting: 3 members (Chairman, Vice-Chairman, Secretary) • Executive Board of Directors: 9 members (Chairman, 3 Vice-Chairman, 5 Directors); • General and Supervisory Board: 13 members (Chairman, 2 Vice-Chairman, 10 Directors); • Statutory Auditor • Remunerations and Welfare Board: 3 members (Chairman, 2 Directors); • Company Secretary 	<p>1000 shares - one vote</p> <p>Shareholders not entitled to vote may form a group with other shareholders to make up the number of shares required to grant the right to vote.</p> <p>According to a statutory provision, the voting rights for purposes of their exercise are limited to 10%.</p>
<i>BES</i> Model 2	<ul style="list-style-type: none"> • Board of General Meeting: 3 members (Chairman, Vice-Chairman, Secretary) • Board of Directors: 26 members (Chairman, 2 Vice-Chairman, 23 Directors): <ul style="list-style-type: none"> • Executive Committee: 11 members • Audit Committee: 3 members • Statutory Auditor • Company Secretary 	<p>100 shares – one vote</p> <p>Shareholders not entitled to vote may form a group with other shareholders to make up the number of shares required to grant the right to vote.</p>
<i>BPI</i> Model 1	<ul style="list-style-type: none"> • Board of General Meeting: 4 members (Chairman, Vice-Chairman, 2 Secretary) • Board of Directors: 25 members (Chairman, 3 Vice-Chairman, 21 Directors); <ul style="list-style-type: none"> • Executive Committee: 7 members; • Audit Board: 3 members (Chairman, 2 Directors); • Statutory Auditor • Remuneration Committee: 3 members • Company Secretary 	<p>500 shares – one vote</p> <p>Shareholders not entitled to vote may form a group with other shareholders to make up the number of shares required to grant the right to vote.</p> <p>According to a statutory provision, the voting rights for purposes of their exercise are limited to 20%.</p>
<i>CA</i> Model 3	<ul style="list-style-type: none"> • Board of General Meeting: 3 members (Chairman, Vice-Chairman, Secretary) • General and Supervisory Board: 9 members (Chairman, 8 Directors); • Executive Board of Directors: 5 members (Chairman, 4 Directors); • Advisory Board: 9 members • Statutory Auditor 	<p>One member – one vote</p> <p>Excepting for some specific decisions (election of the Central CCAM board of directors, budget approval and profits allocation) in which the voting rights can differ according to the shareholding and CCAM average deposits and the solvency ratio.</p>

* The governance bodies' composition and competences are the referred in the CCC and complementary legislation. The information was collected from the company bylaws and other documents (structure of governance and organization charts) published by the banks.