

# **THE PORTUGUESE SOCIAL SOLIDARITY COOPERATIVE *VERSUS* THE PECOL GENERAL INTEREST COOPERATIVE**

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## **ABSTRACT**

The Principles of European Co-operative Law ('PECOL') considers the Portuguese social solidarity cooperative as an example of a co-operative model that approaches the general interest cooperative. The general interest cooperative and the Portuguese social solidarity cooperative are both structured to pursue economic activity mainly in the general interest of the community. They also base their entire activity on the notion of solidarity. For these reasons, the legal frameworks for both types of cooperative have certain peculiarities regarding their categories of members, financial structure, governance and audit regimes. This paper analyses the main similarities and differences between the general interest cooperative and the Portuguese social solidarity cooperative.

**KEY WORDS:** PECOL, general interest cooperatives, social solidarity cooperatives, mutuality, altruism, solidarity, community.

**SUMMARY:** 1. Introduction. 2. The concept of cooperative in Portuguese legislation and in PECOL principles. 3. The composition of the membership group. 4. Financial structure. 5. Governance. 6. Cooperative audit. 7. Conclusions. 8. Bibliographical references.

## **1. INTRODUCTION**

The modern cooperative faces several challenges: to retain the cooperative identity, to achieve sustainability, to compete with profitable economic agents in an open economy, and to respond to new purposes.

In order to respond to these challenges, the cooperative model has to reinvent itself. This reinvention brings some changes to the configuration of the scope of cooperatives. This scope does not have to be "exclusively mutualistic". It may be "predominantly mutualistic." It does not have to only be pursued directly. It may, in certain conditions, be pursued indirectly. It does not have to respond only to the interests of the co-operators. It may respond mainly to the interests of the community.

It is in the context of this reinvention of the cooperative model that Italy, in 1990, introduced a law on social cooperatives (Law No. 381/1991). According to this law, social cooperatives pursue “the general interest of the community in promoting personal growth, and in integrating people into society by providing social, welfare and educational services and carrying out different activities for the purposes of providing employment for disadvantaged people”.<sup>1</sup>

Similar cooperative models emerged across Europe, albeit with changes and adaptations. The following examples are closest to the general interest cooperative discussed in this paper.

In 1998, Portugal published Decree-Law No. 78/98 to regulate “social solidarity cooperatives”. These are cooperatives whose activities are concentrated in the area of social services, and whose primary objective is to assist in situations of social and economic vulnerability. Social solidarity cooperatives provide assistance to families, children, young people, seniors, disabled, unemployed and other vulnerable groups. They operate in areas including professional integration, education, training, occupational and residential care.

In 1999, Spain published Law No. 27/1999, recognising “social initiative cooperatives”, whose goals are either: the provision of welfare services through health, education, cultural or other activities of a social nature; or the conduct of any economic activity with the purpose of integrating those who suffer any kind of social exclusion into the labour market; or meeting social needs that are not being attended to by the market (Article 106(1)).<sup>2</sup>

In 2001, by Law No. 2001/624, of 17 July, 2001, as amended by Law No. 201/856 of July 31, 2014, France introduced a new type of co-operative society, the Co-operative Society for Collective Interest (*société coopérative d'intérêt collectif*), whose purpose, according to its legal definition, is “the production or the supply of collective interest goods and services, with a social utility character.”<sup>3</sup>

One of the main reasons given for the emergence of special laws for cooperatives with a purpose focused on the pursuit of the general interest, was the inadequacy of mainstream cooperative laws to accommodate entrepreneurial and innovative phenomena characterized by an objective of collective interest, the absence of scope for profits, and a mode of organization based on democratic and participatory principles.<sup>4</sup> The emergence of these new laws raises the following questions: Is it permissible for a cooperative to have, as its predominant or exclusive purpose, the satisfaction of the interests of the community rather than its members? Can the interests of members be translated into the

<sup>1</sup> - See THOMAS, A., “The Rise of Social Cooperatives in Italy”, *Voluntas: International Journal of Voluntary and Nonprofit Organizations*, 15(3), 2004, pp 243-263. <http://dx.doi.org/10.1023/B:VOLU.0000046280.06580.d8>

<sup>2</sup> - See RODRÍGUEZ, A. & ORTEGA, A., “Algunas consideraciones sobre las cooperativas de iniciativa social en el marco del fomento de empleo y la inserción laboral. una perspectiva jurídico-económica”, *CIRIEC. Revista Jurídica de Economía Social y Cooperativa*, 19, 2008, pp. 57-78.

<sup>3</sup> - See MARGADO, A., “SCIC, Société coopérative d'intérêt collectif”, *RECMA- Revue Internationale de l'économie sociale*, 284, 2002, pp. 19-30.

<sup>4</sup> - See FICI, A., La funzione sociale delle cooperative: note di diritto comparato”, *Verso un Diritto Dell' Economia Sociale. Teoria. Tendenze e Prospettive Italiane ed Europee*, Napoli: Editoriale Scientifica, 2016, pp. 241- 263; HIEZ, D., “The general interest cooperatives: a challenge for cooperative law”, *IJCL - International Journal of Cooperative Law*, I, 2018, pp. 93-109.

interests of the community, based on the values of altruism and solidarity? Are these entities true cooperatives or do they approach associations? Is there a new type of cooperative?

All of these issues were canvassed in the Principles of European Cooperative Law (PECOL) project. The PECOL are a set of norms that are presented as “ideals” in the regulation of European cooperatives and reflect their key characteristic features. These standards were developed by a small team of legal scholars (Study Group on European Cooperative Law -SGECOL), following a comparative investigation of cooperative law and best practice in seven European legal systems (Germany, Spain, Finland, France, Italy, Portugal and the United Kingdom).<sup>5</sup> The PECOL project did not have the specific objective of promoting the harmonization of national legislation on cooperatives. Rather, these principles can be recognized and assumed by cooperative organizations and can be a reference for legislators when regulating cooperatives.<sup>6</sup>

In view of the fact that general interest cooperatives are a reality in several legal systems, the PECOL principles admit that “Cooperatives may also be established to carry on an economic activity mainly in the general interest of the community (“general interest cooperatives”)” (Section 1.1 (3)). According to PECOL (Chapter 1 – Section 1.1.(4)), general interest cooperatives are a special type of cooperatives, whose purpose is to satisfy not the interests of the members (through transactions with them as consumers, providers or workers of the cooperative enterprise) but the general interest of the community. PECOL considers the Portuguese social solidarity cooperative, regulated by Decree-Law No. 78/98, January 15th, as an example that approaches the general interest cooperative.

Both general interest cooperatives and social solidarity cooperatives are structured to pursue an economic activity that is mainly in the general interest of the community. Social solidarity cooperatives are cooperatives whose activities are concentrated in the area of social services. They have a clear mission to assist those in situations of social and economic vulnerability, supported by a paradigm of social intervention. These cooperatives base their entire activity on the notion of solidarity, and for this reason they fall under a legal framework with certain peculiarities, both as regards the categories of members, their governance, their financial structure and audit regime.

In this context, this paper aims to answer two questions:

- (i) Can Portuguese social solidarity cooperatives be considered general interest cooperatives, in PECOL terms?
- (ii) What are the specificities of the legal regime that characterize general interest cooperatives and social solidarity cooperatives?

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<sup>5</sup> - The Study Group on European Cooperative Law (SGECOL) aims to conduct comparative research on cooperative law in Europe. **Principles of European Cooperative Law (PECOL)** was its first project. See FAJARDO, G., FICI, A., HENRÿ, H., HIEZ, D., MÜNKNER, H., HIEZ, D., “El nuevo grupo de estudio en derecho cooperativo europeo y el proyecto “Los principios de derecho cooperativo europeo”, *CIRIEC. Revista Jurídica de Economía Social y Cooperativa*, 24, 2013, pp. 331-350.

<sup>6</sup> - See HIEZ, D., “Introduction”, In G. Fajardo, A. Fici, H. Henrÿ, D. Hiez, D. Meira, H. Münkner, and I. Snaith, (eds), *Principles of European Cooperative Law. Principles, Commentaries and National Reports*, Cambridge, Intersentia, 2017, pp. 1, ff.

In answering these questions, the ordinary cooperative as regulated by the *Portuguese Cooperative Code (PCC)*,<sup>7</sup> will serve as *secundum comparationis* for these two other types.

## 2. The concept of cooperative in the Portuguese legislation and in the PECOL Principles

In Portugal, the cooperative is defined as an “autonomous association of persons, freely associated, of variable composition and capital, which, through cooperation and mutual assistance of its members, and in obedience to cooperative principles, aims not at profit but at satisfying economic, social or cultural needs and aspirations of the said members.” (Article 2 of the *PCC*).

This definition is based on four distinctive features of this type of legal entity. The first two have a formal character — the variability of the social capital and variability of the shareholding structure. The other two are of a substantive nature — the *social object* of the cooperative (the satisfaction of the economic, social or cultural needs of members, though remaining a non-profit entity) and the management style of the cooperative enterprise (obedience to cooperative principles, and cooperation and mutual assistance of members).

It is worth noting that this definition of a cooperative makes compliance with the cooperative principles a mandatory requirement. These principles are embodied in Article 3 *PCC*: voluntary and open membership; democratic control by the members; member economic participation; autonomy and independence; education, training and information; co-operation among co-operatives; and concern for the community. This article reproduces verbatim the cooperative principles as enshrined in the International Cooperative Alliance (ICA) Statement on the Cooperative Identity,<sup>8</sup> with the latest interpretation given to them by the 2015 ICA Guidance Notes to the principles.<sup>9</sup>

In the Portuguese legal system, the cooperative principles are mandatory and are even enshrined in the Portuguese Constitution (*CRP*). No. 2 of Article 61 of the *CRP*, states that “Everyone is accorded the right to freely form cooperatives, subject to compliance with cooperative principles.” In turn, No. 4, a) of Article 82 of the *CRP* states that the cooperative subsector covers “the means of production that cooperatives possess and manage in accordance with cooperative principles.” Consequently, a disrespect for the cooperative principles in the business operation is a cause for dissolution [Article 77, No.1, h), *PCC*]. This definition refers to ordinary cooperatives who have a mutualistic purpose or scope. It must aim to satisfy the needs of its members as consumers, suppliers or workers of the cooperative. It is this mutualistic purpose that distinguishes them from other entities.

<sup>7</sup> - Law No. 119/2015, published in 31 August 2015 and entered into force on 30 September 2015.

<sup>8</sup> Text of the 1995 ICA Statement on the co-operative identity at: <http://ica.coop/en/whats-co-op/co-operative-identity-values-principles>.

<sup>9</sup> - See NAMORADO, R., “Artigo 3.º”, In D. Meira and M. E. Ramos (eds), *Código Cooperativo anotado*, Coimbra, Almedina, 2018, pp. 28-36. Although ICA is a non-governmental organization, it should be taken into account that these principles have been integrated in the 2002 International Labour organization Recommendation No. 193 concerning the promotion of cooperatives (ILO R. 193). ILO R.193 is the text of an international and transnational organization, which the Portuguese State voted for. On this subject see HENRÝ, H., “Public International Cooperative Law: The International Labour Organization Promotion of Cooperatives Recommendation, 2002”, In D. Cracogna, A. Fici and H. Henrý (eds), *International Handbook of Cooperative Law*, Heidelberg: Springer, 2013, pp. 65-88.

The *cooperative social object* articulates two dimensions: the economic and the social. The economic dimension is present in Article 2, No.1 *PCC* referring to the cooperative scope as “*meeting the needs and economic aspirations*” of its members. The cooperative is an enterprise dedicated to the production of goods and services, under the *aegis* of a rationality that implies the maximization of results and containment of costs. The term “*enterprise*” is understood in a broad sense to mean any form of organization of human, material or financial resources to pursue economic purposes, whether or not they are profitable. The cooperative is a business organization with economic aims, carried out in an economical way. For example, they may be designed to achieve a lower cost of goods for the benefit of their members than could be obtained by other means. Even cooperatives whose primary purpose is to pursue cultural aims for the benefit of members have an economic dimension. The meeting of its members’ needs involves a cost and therefore must have a price to be minimised.

In the *PCC*, the importance given by the legislator to the predominant economic purpose of the cooperative becomes apparent, as illustrated in Article 7: “*while complying with the law and the cooperative principles, cooperatives can freely carry on any economic activity.*” However, this is a business entity with the specificity of pursuing a mutualist scope. This means that the cooperative’s social activity is necessarily directed to its members, who are the main users of the economic and social activities that it carries out. This “dual capacity” is based on the carrying on of an economic activity in which members participate. This participation will lead to a mutual exchange of benefits between the cooperative and the members. Such benefits are specific to the cooperative’s social object. In fact, the coop member, unlike a stockholder in a commercial company, not only has the obligation to contribute to the cooperative share capital, but also an obligation to participate in the cooperative activity. In this sense, Article 22, No. 2, c) of the *PCC* states that members should “participate in the general activities of the cooperative and provide work or service which are assigned to them.”

The members’ obligation to participate in cooperative activity emerges as a basic mechanism for developing the cooperative’s social object and achieving mutual advantage. However, it must be noted that the teleological connection between the cooperative and its members should not be understood in absolute terms and the cooperative should not be considered as a closed organization, operating solely with its members. While the principle of mutuality is an underlying and distinctive feature of cooperatives and one that distinguishes them from other legal entities, it does not necessarily mean that the cooperative only conducts business with its members. It may carry on activity with non-members.

The possibility of entering into contracts with non-members means that the cooperative will be open to business with outside partners, offering its services to those who, although not members, share the same needs. Simultaneously, it must prioritise the satisfaction of the interests of its members. This new conception of mutuality enables cooperatives to operate in the market by competing with other businesses in the provision of goods and services to non-members. In line with this conception, the *PCC*, in its Article 2, No. 2, states that “cooperatives, in pursuit of their objects, are allowed to conduct business with non-members, subject to any restrictions laid down in the law applicable to each cooperative type.” Although the law does not define what is meant by non-members, there seems to be a consensus around the views of Rui Namorado, that “non-members, from the cooperative point of view, are those who hold a business relationship directly related to the carrying on of the cooperative’s primary object, as if they

were members, although, in fact, they are not.”<sup>10</sup> This means that any business the cooperative conducts with non-members should be the same kind of business that is conducted with its members.

To preserve the mutualist scope of cooperatives, transactions with non-members may be subject to limitations in the sectorial legislation of different types of cooperative. Such limitations are expressly provided for in the following: Article 9, Decree-Law No. 523/99, December 10 (trade cooperatives), Article 7, Decree-Law No. 313/81, November 19 (cultural cooperatives), Article 14, Decree-Law No. 502/99, November 19 (housing and building cooperatives), Article 6, Decree-Law No. 309/81, November 16 (worker cooperatives), in Article 6, Decree-Law No. 323/81, December 4 (service cooperatives), and Article 24, nos. 2 and 3, Decree-Law No. 24/91, January 11 (agricultural credit cooperatives). This latter Decree places a limits on the agricultural credit cooperatives’ credit transactions with non-members (35% of the cooperative’s total net assets, which may be increased to 50%, subject to authorization by the Bank of Portugal).

It follows that, in Portuguese Law, cooperatives are characterized by “a predominantly, though not exclusively, mutualistic scope and may conduct business with non-members.”<sup>11</sup> Given the mutualist aim of cooperatives and obedience to the cooperative principle of voluntary and open membership, anyone interested — and who meets the admission requirements — should be able to join as a member of the cooperative and benefit from the services it offers. To do so, the prospective member must apply to the Board of Directors of the cooperative for admission to membership [Articles 19, No.1 and 47.d), PCC]. Rui Namarado argues that “*any restriction on the free entry of new members must derive from the very nature of the cooperative and not from an arbitrary judgment of rejection, potentially discriminatory, because it is based on individual preferences.*”<sup>12</sup> The Board’s decision to accept a candidate for membership must rest on their ability to use the services of the cooperative; to carry out the work required by the cooperative; and their willingness to accept cooperative culture and values.

The Portuguese cooperative legislator established that the statutes of each cooperative must contain the “*admission requirements*” of members [Article 16. No. 2, a) PCC]. If a candidate meets those conditions, the proposed admission must still be subject to approval by the Board of Directors [Article 47, d) PCC]. This resolution is mandatory for the acquisition of membership. Therefore, there is no subjective right to be admitted as a member. Various authors consider this to be an ordinary legal expectation i.e., an active position that, although legally significant, lacks the assurance mechanisms of subjective rights.<sup>13</sup> Under Portuguese Law, the General Meeting will act as an appeal body as to the admission or rejection of new members [Article 38, k) PCC].

The *cooperative social object* is not limited to meeting the needs of its members. It should equally attend to the interests of the community in which the cooperative carries on its activity. The principle of concern for community is set out in Article 3 PCC, where it is stated that: “cooperatives work for the sustainable

<sup>10</sup> - See NAMORADO, R., *Cooperatividade e Direito Cooperativo. Estudos e Pareceres*, Coimbra, Almedina, 2005, pp. 184-185.

<sup>11</sup> - See MEIRA, D. A., “As operações com terceiros no Direito Cooperativo Português (Comentário ao Acórdão do Supremo Tribunal de Justiça de 18 de Dezembro de 2007)”, *Revista de Ciências Empresariais e Jurídicas*, 17, 2010, pp. 93-111.

<sup>12</sup> - See NAMORADO, R., *Os Princípios Cooperativos*, Coimbra, Fora do Texto, 1995, p. 61.

<sup>13</sup> - In this sense, see for all NAMORADO, R., *Cooperatividade e Direito Cooperativo. Estudos e pareceres*, p. 21.



development of their communities through policies approved by their members.” Although primarily focused on the needs of their members, cooperatives work to achieve the sustainable development of their communities, under criteria approved by their members.

This principle is strongly connected with another cooperative principle: voluntary and open membership, which is the traditional *open door principle* formulated in Article 3 *PCC*: “*Cooperatives are voluntary organizations, open to all persons able to use their services and willing to accept the responsibility of membership, without gender, social, racial, political or religious discrimination.*” This principle can be considered under two perspectives. Firstly, joining should be voluntary, as it depends exclusively on the will of the member. Secondly, the cooperative must be open to all people, providing that its member candidates meet two requirements: the ability to benefit from and contribute to the cooperative’s transactions, and acceptance of the responsibilities of membership. The way that these two principles connect is evident. The traditional open-door policy adopted by the cooperative when accepting new members is justified by its willingness to service the community in which it is embedded. Openness to members who reside in the area where the cooperative carries out its activity is a constant characteristic of this type of organization. This practice means that the cooperative is a generator of stable jobs. It is an organization that is strongly rooted in the community. It carries on activities that typically do not allow relocation and this provides the fuel for a local entrepreneurial spirit. Consequently, cooperatives have a special responsibility to ensure that the development of their communities is economically, socially and culturally sustainable. Under these principles, cooperatives become involved in the social context. It is the members’ responsibility to decide upon the policies through which this involvement will materialize.

The principle of education, training and information is also relevant to the defence of the claim that the cooperative object is within the scope of the socially relevant activities. In Article 3 *PCC* the legislator says that “*cooperatives will provide education and training for their members, elected representatives, managers and employees, so they can contribute effectively to the development of their cooperatives. They will inform the general public, particularly the young and opinion leaders, about the nature and benefits of cooperation*”. This principle emphasizes the obligation of cooperatives to guarantee the education and training of their members, representatives of the elected bodies, directors or employees, in cooperative thought and action. This principle also includes the duty to inform the general public in order to raise awareness of the nature and benefits of cooperation and to encourage new membership, especially, informed membership.

It should also be noted that the law provides for a compulsory reserve fund “for cooperative education and technical and cultural training of members, and employees of the cooperative as well as of the community” (Article 97 *PCC*). The establishment of reserves for education and training means that the cooperative is not only a business organization, but also an organization with social and educational concerns. This reserve fund aims to bear the costs of activities that are beyond the satisfaction of the purely individual interests of cooperative members. These activities are not strictly of an economic nature, but may result in direct or indirect, immediate or deferred economic benefits, both to the cooperative and to the community where the cooperative operates. This reserve is one of the most distinctive features of the cooperative enterprise when compared with other types of enterprise. It generates assets that are

allocated to social purposes, to the benefit of members, cooperative workers and to the social environment.<sup>14</sup>

Finally, further evidence of the social dimension of the cooperative object can be found in the principle of disinterested distribution of assets. This principle is enunciated in Article 114 *PCC*, which states that on a winding-up, residual assets cannot be distributed among the members. This principle emphasises the social role that the cooperative fulfils and it implies that in the end, assets are to be allocated to the promotion of cooperation. Article 114, No.1 of the *PCC* provides that on the winding-up of the cooperative, any legal reserves that are not allocated to covering losses of the financial year and which may not be used for any different application “*can move, with the same purpose, to a new cooperative entity to be formed following the merger or division of the cooperative in liquidation.*” Article 114 No. 3 states that “when no new cooperative succeeds the cooperative in liquidation, the application of the mandatory reserve balance will be allocation to another cooperative, preferably from the same city, to be determined by a federation or confederation that represents the main activity of the cooperative.” Article 114, No.4 goes further, stating that “to the reserves established under the provisions of Article 98 of this Code apply, in the event of liquidation and when statutes do not provide otherwise, the provisions of numbers 2 and 3 of this Article”, which means that free reserves may also be covered by the principle of disinterested distribution.

In the PECOL principles, the definition of a cooperative is focused on its objective and there is no express reference to obedience to the cooperative principles. According to PECOL principles, ordinary cooperatives are “legal persons governed by private law that carry on any economic activity without profit as the ultimate purpose and *mainly* in the interest of their members, as consumers, providers or workers of the cooperative enterprise” (Section 1.1.(1)). For PECOL, the mutual scope of cooperatives “does not prevent cooperatives from pursuing additional objectives that go beyond the interests of their members and may be qualified as ‘altruistic’.”<sup>15</sup> It is in this sense that the use of the word “mainly” in the PECOL definition of cooperatives should be understood. So, cooperatives may also be established “to carry on an economic activity mainly in the general interest of the community (‘general interest cooperatives’)” (Section 1.1. (4)).

In addition to the economic dimension of its object, an ordinary cooperative may also have a complementary social object fulfilling the 7th ICA principle “concern for the community”. However, in a general interest cooperative this complementary objective becomes the main or even exclusive objective. In this context, the legal regime of the general interest cooperatives deviates from the legal regime of ordinary cooperatives in the following ways: general interest cooperatives are not obligated to undertake cooperative transactions with their members as consumers, providers or workers; they face no limitation

<sup>14</sup> - On this principle, see MEIRA, D., *O regime económico das cooperativas no Direito Português: o capital social*, Porto, Editora Vida Económica, 2009, pp. 162-167.

<sup>15</sup> - See FICI, A., “Chapter 1- Definition and Objectives of Cooperatives. Commentary”, In In G. Fajardo, A. Fici, H. Henry, D. Hiez, D. Meira, H. Münkner, and I. Snaith, (eds), *Principles of European Cooperative Law. Principles, Commentaries and National Reports*, Cambridge, Intersentia, 2017, pp. 27, ff.



on transactions with non-cooperator members; and they may freely admit to membership non-cooperator members (PECOL Chapter 1)<sup>16</sup>.

These deviations are not provided for in Decree Law No. 7/1998 of 15 January 1998 governing Portuguese social solidarity cooperatives. This law imposes limits for transactions with non-cooperator members. In fact, Article 2(2) establishes “Beyond the enumeration contained in the foregoing subsection, social solidarity cooperatives can undertake other activities of similar nature and, within the limits defined by the Cooperative Code, offer services to third parties”. Social solidarity cooperatives cannot freely admit to membership non-cooperator members. Finally, as we shall see in the next section, social solidarity cooperatives are obligated to undertake cooperative transactions with their effective members.

### 3. The composition of the membership group

Ordinary cooperatives pursue a mutual purpose and so they are comprised of mainly co-operator members. In the case of general interest cooperatives, the activity pursued aims to meet the needs of the community, so the main beneficiaries will be not the members of the cooperative but the community. Consequently, in general interest cooperatives, membership is not a necessary condition to obtain services and goods. Importantly, services and goods are not defined to meet the needs of the members, because their altruistic purpose is to satisfy the interest of the community and not their members. According to PECOL Principles, general interest cooperatives are not obligated to undertake cooperative transactions with their members as consumers, providers or workers (PECOL, Chapter 1, sec. 1.4(1)).<sup>17</sup>

In contrast, in Portuguese social solidarity cooperatives, membership is a necessary pre-condition to obtaining services and goods. In the light of the definition contained in the Portuguese Cooperative Code, cooperatives characterize themselves by uniting people who share needs or aspirations to meet them through an economic activity developed in common. Membership is a pre-condition for the satisfaction of their needs, which will determine the object pursued by the cooperative.

Another important criterion for distinguishing ordinary cooperatives from general interest cooperatives is the composition of membership groups. In general interest cooperatives we can find a number of different categories of members: non-using investing members; promoting members; voluntary members; enterprises working in the community or region; as well as private and public corporations. For example, in the Italian social cooperatives (Law 381/91) the ownership structure may simultaneously include: worker members, including practitioners and managers who are remunerated; user members who are the recipients of the services supplied by the cooperative or their family members; volunteer members, who work in the cooperative freely, without receiving any form of compensation; financing members, defined as suppliers of capital with limited rights to participate in the decision-making and governance of the organization; and legal entities.

In contrast, the Portuguese social solidarity cooperative recognises only two categories of members: effective members and honorary members. The effective members are the reference members of the cooperative. They comprise those who intend to use the services provided by the cooperative for their

<sup>16</sup> - See FICI, A., “Chapter 1- Definition and Objectives of Cooperatives. Commentary”, pp. 27, ff; HIEZ, D., “The general interest cooperatives: a challenge for cooperative law”, pp. 98-101.

<sup>17</sup> - See FICI, A., “Chapter 1- Definition and Objectives of Cooperatives. Commentary”. pp. 27, ff.

own benefit or that of their relatives, or who intend to develop their professional activity in the cooperative. According to Portuguese legislation, social solidarity cooperatives are obligated to undertake cooperative transactions with their effective members. Honorary members are those who contribute with goods or services, including social volunteering, to the development of the cooperative's object. The admission of honorary members is made by the members in General Meeting, on the basis of reasoned proposal by the board of directors, which must contain a report on the donations of goods or services that contribute noticeably to the development of cooperative object (Articles 4 and 5 of Decree-Law No. 78/98). This has the effect that, in the current state of the Portuguese cooperative legislation, a social solidarity cooperative whose purpose is only to satisfy the general interest of the community, is not allowed. In other words, a social solidarity cooperative is not allowed without a minimum mutualistic scope.

#### 4. Financial structure

In Portuguese social solidarity cooperatives, the distribution of surplus among co-operators is prohibited, which means that all surpluses will revert, mandatorily, to reserves (Article 7 Decree-Law No. 78/98, January 15th).

The same requirement is provided in the PECOL principles. General interest cooperatives may not distribute cooperative surpluses to their members (Section 3.6.(6)). The prohibition on the distribution of cooperative surpluses to members for both general interest cooperatives and social solidarity cooperative flows from the fact that they develop their activity mainly in the interest of the community, guided by the values of altruism and solidarity and not by the values of mutuality.

Cooperative surplus is a term used in doctrine and legislation to refer to the positive economic results that stem from the pursuit of a mutualistic scope by the cooperative. It corresponds to the difference between revenue and the costs of the cooperative transactions with its members. It is an amount that is temporarily paid as excess by the cooperators to the cooperative or underpaid by the cooperative to the cooperators, in exchange for their participation in the activity of the cooperative.<sup>18</sup>

In a general interest or social solidarity cooperative, it is possible that no surplus will be generated. As explained above, general interest cooperatives are not obligated to undertake cooperative transactions with their members as consumers, providers or workers. In the absence of cooperative transactions, there will be no cooperative surpluses.<sup>19</sup> If there is a cooperative surplus, it must be allocated to reserves and reinvested in the promotion of general interest. In addition, if a general interest cooperative or a social solidarity cooperative is wound up, its residual net assets must be transferred to another general interest cooperative or social solidarity cooperative. This is consistent with PECOL Principles (Chapter 3, Section 3.8. (2)), where residual net assets shall be allocated in accordance with the principle of disinterested distribution, e.g. distributed to the community or other associated cooperatives. It is also consistent with

<sup>18</sup> - See FAJARDO, G. & MEIRA, A., "Chapter 3- Cooperative Financial Structure. Commentary", In G. Fajardo, A. Fici, H. Henry, D. Hiez, D. Meira, H. Münkner, and I. Snaith, (eds), *Principles of European Cooperative Law. Principles, Commentaries and National Reports*, Cambridge, Intersentia, 2017, pp. 89, ff; and BANDEIRA, A. M., MEIRA, D. A. & ALVES, V. M., "Los diferentes tipos de resultados en las cooperativas portuguesas. Un estudio de caso multiple", *REVESCO - Revista de Estudios Cooperativos*, 123, 2017, pp. 37-63.

<sup>19</sup> - See HIEZ, D., "The general interest cooperatives: a challenge for cooperative law", pp. 106-108.

Article 8 Decree-Law No. 78/98, January 15<sup>th</sup>, which established that “where the cooperative in liquidation is not succeeded by a cooperative of the same branch, the application of the balance of the mandatory reserves will be allocated to another social solidarity cooperative, preferably from the same city, to be selected by a federation or confederation that represents the main activity of the cooperative.”

## 5. Governance

In general interest cooperatives and social solidarity cooperatives, there are specificities in terms of governance. General interest cooperatives and social solidarity cooperatives often have a multi-stakeholder membership, including in their governance all the different categories of members: workers, volunteers, customers, private or public organizations.<sup>20</sup>

The involvement of multiple stakeholders in the ownership and governance of cooperatives is not straightforward. Two questions are raised: How can the interests of the different categories of members be reconciled? How can participatory and democratic governance be ensured?

In an ordinary cooperative, members give the cooperative a clear mandate to promote the economic interests of their members. The membership group is relatively homogeneous and all members, or at least the majority, are simultaneously owners and users of their cooperative enterprise. This allows the organisation to work under clear and relatively simple rules (e. g. one member, one vote).<sup>21</sup>

In cooperatives with different categories of members, heterogeneous membership groups are generated, requiring complex rules to avoid one category of members dominating the others, either in relation to the exercise of voting rights or participation in governance of the cooperative. Possible solutions include: ensuring that board composition reflects the composition of the membership; special rules to secure fair representation of each group of members in the governing and controlling bodies; different voting rights for different groups of members such as employees and users of services to ensure equitable representation of different member interests on the board.<sup>22</sup>

All of these solutions are embraced by the PECOL principles. According to Section 2.4.(8) “When necessary for the better functioning of a cooperative, cooperative statutes may confer plural votes not related to capital contribution, and reflecting, for example, (a) participation in cooperative transactions; (b) the number of members in particular subdivisions; or (c) the balanced representation of different member groups. Section 2.4(9) establishes that “When cooperative statutes exercise the option in paragraph (8), they must in any case ensure that investor members or a minority of co-operator members do not control the cooperative.” Section 2.4(10) provides that “Total plural votes held by any co-operator member can never exceed a certain percentage of all members ‘votes cast at any members’ meeting at which they vote, as defined by the law. However, investor members may have plural votes according to

<sup>20</sup> - See HIEZ, D., “The general interest cooperatives: a challenge for cooperative law”, pp. 105-106.

<sup>21</sup> - See MÜNKNER, H., “How co-operative are social co-operatives?”, *CES - Cooperativismo e Economia Social*, 38, 2016, p. 54.

<sup>22</sup> - See MÜNKNER, H., “How co-operative are social co-operatives?”, p. 54; SNAITH, I., “Chapter 2- Cooperative Governance. Commentary”, In G. Fajardo, A. Fici, H. Henry, D. Hiez, D. Meira, H. Münkner, and I. Snaith, (eds), *Principles of European Cooperative Law. Principles, Commentaries and National Reports*, Cambridge, Intersentia, 2017, pp. 60, ff.

capital limited to a total of a certain percentage of votes.” Section 2.4(12) says that “Decisions are made by simple majority of the votes cast but special majorities are required for the fundamental decisions defined in paragraph (5),<sup>23</sup> which are always made on the basis of one member one vote.” Finally, Section 2.5(5) establishes that “Board composition, especially in general interest cooperatives, shall take into account the composition of the cooperative membership, including, for example, by geographical constituency or category of member.”

Some of these solutions are not possible in the context of the Portuguese social solidarity cooperatives. In fact, in the Portuguese legal system, the plural vote will only be permitted in cooperatives with more than twenty (20) cooperators and if those cooperatives are not worker, handicraft, fish, consumer or social solidarity cooperatives (art. 41, No.1 of the *PCC*). Another governance issue for Portuguese social solidarity cooperatives concerns the rights of honorary members to vote and to be elected to the organs of the cooperative. As already pointed out, in this type of cooperative, we have two categories of members: the effective members who are simultaneously owners and users of their cooperative, and honorary members who are limited to contributing goods or services to the development of the objects of the cooperative. Article 5.3 of Decree-Law No. 78/98 establishes that honorary members enjoy the right to information in the same terms as the effective members, but they cannot elect or be elected to the corporate bodies, even though they may attend general meetings without the right to vote. Participation in governance with the right to vote at general meetings, is the exclusive right of effective members.

These restrictions on honorary members are a derogation from the second ICA principle of democratic member control. Compliance with cooperative principles is mandatory for the Portuguese legislator. So, this derogation should be removed in any future reform of cooperative legislation.

## 6. Cooperative audit

In general interest cooperatives and social solidarity cooperatives, there are specific issues relating to the terms of the cooperative audit. How do we measure the satisfaction of community interests? Or stakeholder involvement?

In mutual cooperatives, special instruments are required to measure success in terms of member-oriented effectiveness (promotion plan, promotion report) and special forms of audit are needed to measure aspects of internal and external control (financial and management audit).<sup>24</sup>

In the case of general interest cooperatives or social solidarity cooperatives, it is necessary to resort to additional instruments for measuring success, e.g. “social report.”<sup>25</sup> In the context of these cooperative models, regulatory authorities may also play an important role in terms of audit.

<sup>23</sup> - Fundamental decisions are decisions about restructuring or dissolving the cooperative, amending its statutes, participating in legal entities or groups, or establishing subsidiaries (Section 2.4(5)).

<sup>24</sup> - See MÜNKNER, H., “Chapter 4 - Cooperative Audit. Commentary”, In G. Fajardo, A. Fici, H. Henry, D. Hiez, D. Meira, H. Münkner, and I. Snaith, (eds), *Principles of European Cooperative Law. Principles, Commentaries and National Reports*, Cambridge, Intersentia, 2017, pp. 106, ff.

<sup>25</sup> - See TOMÉ, B., MEIRA, D. A. & BANDEIRA, A., “The Integrated Reporting and Corporate Social Responsibility in the context of Social Economy (Mutual Association situated on the Health and Welfare Sector)”. *CIRIEC-España, Revista de economía pública, social y cooperativa*, 85, 2015, pp. 109-142; and MÜNKNER, H., “How co-operative are social co-operatives?”, p. 63, ff.

Under Portuguese law, there are no regulatory authorities for the cooperative sector or the social economy sector in general. Although it cannot be classified as a regulatory authority, António Sérgio Cooperative for Social Economy (CASES) exercises some regulatory powers, because its duties are to monitor and supervise the cooperative sector and its mode of operation. CASES was created by Decree-Law No. 282/2009 of 7 October 2009. It is a public interest cooperative that is responsible for overseeing the use of the cooperative format in compliance with the principles and rules concerning its incorporation and operation. Pursuant to Article 117, No.1 of the PCC, it is the responsibility of CASES to issue an annual credential attesting to the legal incorporation and proper functioning of the cooperative. In the case of social solidarity cooperatives, Article 9, No.1 of Decree-Law No. 78/98 states that this annual credential shall also confirm the purposes of social solidarity.

According to PECOL, in general interest cooperatives, the cooperative audit includes the manner in which the general interest has been pursued and stakeholder involvement in the cooperative (Section 4.2(1)).<sup>26</sup> In addition, as in ordinary cooperatives, the audit includes but is not limited to the volume of cooperative transactions with members and with non-members; the use and results of subsidiaries; member participation in cooperative governance; member democratic control of the cooperative; the composition of assets; the origin and allocation of the economic results; the amount of the indivisible and divisible reserves; the economic sustainability of the enterprise; the existence of practices of cooperation among cooperatives and cooperative social responsibility; and the level of engagement in cooperative education and training (Section 4.2(1)).

## 7. Conclusions

General interest cooperatives and Portuguese social solidarity cooperatives were both conceived as cooperative models whose driving force is not mutuality but altruism and solidarity. Rather than primarily addressing the needs of members, they are oriented towards the needs of the entire community.

In general interest cooperatives, membership is not a pre-condition to obtaining services and goods. In Portuguese social solidarity, cooperative membership is a pre-condition to obtain those services and goods. According to PECOL Principles, general interest cooperatives are not obligated to undertake cooperative transactions with their members as consumers, providers or workers. According to the Portuguese legislation, social solidarity cooperatives are obligated to undertake cooperative transactions with their effective members. So, in its current state, Portuguese cooperative law requires that social solidarity cooperatives must have a minimum mutualistic scope.

In general interest cooperatives and social solidarity cooperatives, the distribution of surplus among co-operators is prohibited, and all surpluses must revert to the cooperative reserves. In both cooperatives, residual net assets are allocated in accordance with the principle of disinterested distribution. General interest cooperatives and social solidarity cooperatives often have a multi-stakeholder membership, requiring specific rules relating to governance, so that the composition of the board reflects the composition of the membership and allowing different groups of members to have different voting rights. These rules are clearly expressed in the PECOL Principles, ensuring truly participatory and democratic

<sup>26</sup> - See MEIRA, D., "Portugal", In G. Fajardo, A. Fici, H. Henry, D. Hiez, D. Meira, H. Münkner, and I. Snaith, (eds), *Principles of European Cooperative Law. Principles, Commentaries and National Reports*, Cambridge, Intersentia, 2017, pp. 501-502.

governance. However, for Portuguese social solidarity cooperatives it is not possible to adopt plural voting and honorary members are deprived of the right to vote and the right to be elected to the organs of the cooperative. Finally, the cooperative audit in general interest cooperatives and social solidarity cooperatives must consider the manner in which the general interest is pursued and stakeholder involvement in the cooperative.

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