11

Networking, Governance, and Stakeholder Engagement of Financial Cooperatives: Some National Case Studies

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11.1 Introduction

This chapter will study the network organization of financial cooperatives (FCs) and illustrate the most prominent experiences in terms of network structure, governance, and stakeholder engagement. Based on existing literature, it considers the case of Rabobank in The Netherlands, Desjardins Group in Canada, and Cassa Centrale and ICCREA in Italy.

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The need to investigate the network organization of FCs stems from the coordination patterns observable since their origins in the late nineteenth and early twentieth centuries. FCs were conceived as local or community banks, which could often operate only in their home municipalities. Moreover, they were usually anchored in different territories, so the overlap between their operations was limited. The local character of FCs and their embeddedness in the community differentiated them from commercial banks.

Competition among FCs was avoided in most cases, as it was considered incompatible with the nature, values, and purpose of this type of institution. Instead of competition, a process of spontaneous cooperation and networking among the different local FCs has been observed since their inception. Cooperative networks, in most cases, became more structured and formalized over time, leading to the formation of one or a small number of networks at the national level, which enabled FCs to coordinate with each other, increase their market share, and respond in unison to external challenges. Coordinated development was also accompanied by the creation of a group of FCs that had a common point of reference in a central institution, such as a central cooperative bank having a pivotal role in the group. In other cases, a more decentralized and less formalized network was preferred, in which FCs still interacted cooperatively, but without the creation of a central institution to serve as controller and lender of last resort, and without stringent constraints on mutual aid and control. In any case, spontaneous inter-organizational cooperation seems to be inscribed in the behavioral predispositions of FCs, although the regulation of intra-network relations proved to be a complex undertaking that did not develop without difficulty. This places FCs in sharp contrast to the expansion and marketing policies of commercial banks, which are instead driven by competition, profit, and market share maximization.

Networks of cooperative banks were studied as examples of progressive degrees of integration among atomized organizations pursuing common goals and seeking coordination both to pool resources and to achieve economies of scale. From this perspective, networks were instrumental in reducing the risk of internal contrasts and competition in the same credit and deposit market. Desrochers and Fischer (2005) classify different types of cooperative bank networks according to the degree of integration. Three categories are identified: (i) atomized systems (no or very low integration) in which FCs act completely autonomously and networks are based on spot contractual relationships; (ii) consensual networks (medium level of integration), in which network arrangements are usually formalized in terms of alliances that reduce supply costs but can generate collective agency costs and contractual failures in terms of decision-makers' (managers') spending preferences and appropriation risks. This group includes consensual networks where participation is voluntary and where collective choices require horizontal coordination among partner organizations since a monitor and central decision-maker are usually absent or lack executive decision-making power; (iii) partner cooperatives merge and become members of a single organization. Contractual relationships are internalized and become part of the governance structure. This standardizes procedures, reduces coordination costs, achieves economies of scale in service production, and reduces procurement costs, but can generate significant organizational costs due to appropriation risks and spending preferences. Included in this group are strategic networks, such as Cassa Centrale and ICCREA in Italy, or the Desjardins Group in Canada, in which a central organization functions as a hub that ensures the standing and solvency of all member organizations conducting production activities and, at the same time, is charged with making strategic decisions. Also included are mergers in the narrow sense, in which all member organizations merge into one larger organization, such as Rabobank in The Netherlands (Desrochers & Fischer, 2005; Hennart, 1993; Novkovic & Holm, 2012).

The most crucial dimensions in the process of integrating networks from atomized systems to consensual and strategic networks to mergers are the pooling of resources and the separation of strategic and operational management and control. The former phenomenon shows the potential of integration in terms of coordination, standardization, and reduced procurement costs; but, at the same time, it increases organizational costs in terms of the cost of suboptimal and opportunistic choices.

The formalization and centralization of a network also imply the separation of strategic and operational choices, as the former is increasingly assumed by a central decision-maker, while the latter continues to be decentralized and left to member organizations (Desrochers & Fischer, 2005).

Other authors focus instead on cooperative values and the history of mutual benefit among cooperative banks as a guiding principle that can inform the creation of public value generated for communities by cooperative banks (Novkovic & Holm, 2012; Ramboarisata, 2009; Sacchetti & Tortia, 2016). Sacchetti and Sugden (2003), in particular, discriminate between networks in which coordination is based on authority and command-and-control principles, and networks based on mutual dependence, in which instead participants have access to strategic planning and are self-managing. These are two extremes on a continuum where FCs' networks can be positioned according to the level of inclusion of participating banks in strategic planning. Low inclusion means that there is little cooperation and that the authority of a single participant prevails in setting the coordination of resources and the direction of the network. High inclusion, on the other hand, means that coordination is cooperative and participants share common values and goals and give each other rules that allow joint and mutual access to strategic decision-making.

Sacchetti and Tortia (2016) apply this network approach to networks created by cooperative enterprises and identify different types of participants. In particular, a cooperative participating in a network can take on different roles. First, we consider the role of "inter-actor", when commitment is based on reciprocity, mutuality, and shared control of strategic direction and resource allocation. This role is consistent with cooperative values. Second, a cooperative can be part of a network as a "recipient", when decisions are not participatory and the cooperative conforms to strategic and/or operational decisions made by the network center. Third, we consider an additional role: that of "director", when the main cooperative or the second-level coordinating level of the network assumes control without introducing cooperative governance mechanisms, but rather adopts command and control over other network members or recipients. This type of solution is based on the exclusive use of strategic decision-making power and is clearly at odds with cooperative values (Sacchetti, 2015).

In this chapter we illustrate network characteristics using formal networks orchestrated through a central bank with the aim of pooling resources, realizing economies of scale, introducing new centralized services, and improving the economic, environmental, and social sustainability of cooperative members' activities. On the other hand, centralization is not a necessary solution, and different countries have followed different paths. For example, centralization and formalization have been achieved in both The Netherlands (Rabobank) and Italy (Cassa Centrale Banca Group and ICCREA), but at very different speeds. While Rabobank was already a centralized network with one central bank in the 1970s and this centralization and unification process was completed in 2015, in Italy, the same process only started in 2015 and was completed in 2020 (Groeneveld, 2015). Illustrating the examples, we consider the degree of inclusion in strategic planning to assess whether networks are coordinated in cooperation rather than by authority.

11.2 The Network of Cooperative Banks in The Netherlands and Rabobank

Rabobank in The Netherlands represents a nationally integrated cooperative bank model. It was created in 1972 as a result of the unification of two separate networks of local financial cooperatives (LFCs). The new unified network was significantly centralized, as Rabobank assumed all central monitoring functions, developed information technology, and marketing networks, and acted as a lender of last resort for member cooperatives. The main function of the network is mutual support among member banks. All banks in the network provide financial support to member banks in financial difficulties. Mutual support is usually sufficient to solve the financial problems of member banks. However, in the most difficult cases, there is direct intervention from the parent bank, Rabobank (Cotugno, 2010).

11.2.1 Network Governance

The governance of the cooperative network evolved in tandem with the goals of member banks and the increasing formalization of network relationships, which eventually led to the complete unification of the network in 2015 under a unified corporate identity. Since its establishment in 1972, Rabobank has been characterized by a dual governance structure in which local banks represent the first tier and Rabobank Netherlands (RN) represents the central banking unit (Groeneveld, 2015). During RN's development period, the 1980s and 1990s, governance became increasingly formalized and centralized because of the need to issue financial instruments such as bonds to finance the group, as neither customer deposits nor internal funding was sufficient to achieve adequate capitalization and reserves. In an internal debate on Rabobank's cooperative identity in the mid-1990s, demutualization and transformation into a commercial bank was also considered, because the unification and centralization of the 1970s had wiped out cooperative values from the RN. In the end, the cooperative identity was retained to diversify the Dutch banking system and preserve the participatory and local character of the bank.

The issuance of financial instruments by RNs, particularly saleable member certificates, which still counted as core Tier 1 capital without voting rights, was again accused of diluting participation rights and democratic governance. This danger was perceived but overcome when the group was able to collectively coordinate and agree on the need to achieve financial sustainability through the growth of financial markets. The result of the process of building integrated governance was a high degree of risk sharing, internal supervision, and regulation. Internal interrelationships and linkages have helped to create a fluid environment in which capital stocks can be accumulated and cash flows circulated seamlessly. The local character of the bank has been preserved, however, as LFCs still operate primarily within their home communities (Groeneveld, 2016). The last step toward centralization and formalization of the LFC network took place in 2015. Following the replacement of the Dutch Central Bank's external oversight with that of the European

Central Bank in November 2014, further systematization and rationalization of internal regulation, administrative procedures, and financial flows were proposed to counter the increasing costs of reviewing and complying with European regulation and stricter capital and liquidity requirements. The LFC network, which historically had the RN as a central service provider or delegated supervisor, was to be replaced by a single bank controlled by the RN.

The new governance structure required reformulation of the statutes and regulations of member LFCs, which no longer operate as independent legal entities, although they keep their own accounts. The RN's delegated supervision of LFCs and internal clearing rules have been replaced by a simplified advisory structure that does not hybridize different structures at the grassroots and central governance levels. Rabobank continues to operate as a decentralized organization of LFCs based on cooperative principles. LFCs act in local communities and are directly represented in Rabobank's central governance bodies. The main goal of the new governance structure was to better meet financial markets requirements, European Central Bank (ECB) supervisory regulations (especially bail-in requirements), and to improve Rabobank's cost efficiency by reducing regulatory and compliance costs (Groeneveld, 2015). The reform was approved by member LFCs in December 2015 and came into effect in January 2016.

11.2.2 Stakeholder Engagement

Rabobank's main stakeholders are its member LFCs and their members, employees, customers, and the local community. Given the strongly rooted nature of the bank and its ties to local communities in The Netherlands, it is important to seek a better understanding of stakeholder engagement processes. Given the agricultural origins of the bank, the inclusion of smallholders is critical and involves strong interdependencies and uncertainties, perhaps even conflicting stakeholder interests. Smallholders and customers must be included in food value chains, and Rabobank has a central role in meeting their expectations and responding to their social and economic goals (Blok et al., 2013). Achieving sustainability and economic independence for smallholder farmers is hindered by several problems, including low productivity and product volumes, variable quality, high transaction costs, and limited access to upstream and downstream markets. Overcoming these problems requires the implementation of a complex combination of different financial and organizational instruments, and may require the involvement of multiple stakeholders. Rabobank, both in The Netherlands and in other countries, including developing countries, has activated partnerships with farms, NGOs, and government organizations. Rabobank's Corporate Social Responsibility (CSR) Department and Ethics Committee are responsible for social and environmental sustainability, e.g., in terms of reputation with stakeholders and especially in dealing with employee requests regarding internal and external policies (Jagersma, 2009; Spitzeck & Hansen, 2010). Local stakeholders participate in the development of internal guidelines for sustainable lending, asset management, and customer engagements. In the case of strategic ethical issues, an ethics committee, chaired by Rabobank's CEO, provides advice. In addition to ordinary administrative procedures, RN can intervene in sustainable development projects through the Rabobank Foundation, established in 1974, an independent nonprofit organization that provides financial and technical support to external stakeholders to achieve social inclusion. These projects aim to improve the financial and economic position of members and partners, especially in terms of capitalization, creditworthiness, access to finance, governance, and organizational structure. Specialized curriculum training programs are also implemented (Groeneveld, 2016).

RN supports its stakeholders' projects, but also oversees important social issues in its member organizations: for example, working conditions, corruption issues, and environmental impact. Consequently, CSR in RN implies that stakeholders and member organizations are treated by RN in full compliance with national and international legislation, without exploiting the bank's bargaining power in any way to reduce stakeholder welfare. Responding to stakeholder needs requires promoting sustainability and economic independence by overseeing the proper functioning of member and customer supply chains and business operations. In addition, communication plays a central role in meeting stakeholder expectations. The efforts of Rabobank Foundation and Rabobank's CSR and development departments are complementary in connecting producer members and integrating them into value chains (Blok et al., 2013; Bulsink, 2017).

11.3 The Desjardins Movement in Canada

The Canadian Desjardins movement of credit unions (or *caisses populaires*) was created in 1900 by Gabriel-Alphonse Desjardins, who followed the European model of *volksbanken*, introduced in Germany in 1850 by Hermann Schulze-Delitzsch. Because Desjardins remained in close contact with many of the founders of the European cooperative movement throughout his life, he was also influenced by the models of the Raiffeisen credit union in Germany and the Luzzatti people's bank in Italy. The first *caisses*, later renamed *Caisses populaires Desjardins*, had about 130 founding members, whose number increased to about 720 after only one year (Sanchez Bajo & Roelants, 2011). Desjardins credit unions developed from the beginning as a network of FCs, whose number in Québec grew from zero to 187 in 1920, with 30,000 members and total assets of more than C$6 million. Another 24 were created in Ontario and nine in the United States.

In the early decades of the twentieth century, a network of *caisses* on a regional basis was foreshadowed. In 1920, the first second-tier cooperatives were created as "regional unions", with supervisory and control functions (Bajo & Roelants, 2011). In the following decades, Desjardins reached maturity and growth, especially in the 1960s and 1970s. By 1960, the network included 1227 *caisses* and had 1.2 million members, with assets of C$1 billion. The phase of greatest expansion occurred in the 1970s. Assets rose to C$11.5 billion in 1979, and the range of services offered was greatly expanded. During the same period, regional unions strengthened their capacity to provide services to local *caisses*, especially in the areas of administration, education and training, and financial services.

The group's central administration strengthened its powers and responsibilities in coordinating training and accounting. In 1981, the

Caisse Centrale Desjardins (CCD) was created. It responded to the liquidity needs of individual *caisses* and other organizations affiliated with the group. The CCD created an extensive international network of relationships with other similar groups in different countries (Bajo & Roelants, 2011). In addition, a first wave of mergers and consolidations was observed in the 1980s. In the 1990s, inter-company services and alliances among *caisses* were strengthened to improve penetration in industrial credit markets and led to the creation of Corporate Financial Services (CFE). The clustering of business centers enabled improved skills and support for entrepreneurs through professional training and partnerships.

The 1990s saw new organizational innovations. The establishment of regional unions and the central federation had already exerted a strong push toward network integration. New central governance issues emerged and became increasingly important due to increased competition in the sector. In the same years, a new network reform occurred that led to greater integration. The debate between centralization and decentralization was about maintaining a flexible, effective, and resilient system while preserving democratic decision-making and involvement of grassroots organizations. Voting systems were reviewed, seeking to maintain the representativeness of local co-op networks without overriding the democratic principles of the International Cooperative Alliance (ICA). Local networks are embedded in regional cooperative networks and in some cases are considerably different in size.

During the same period, there was a new wave of mergers and acquisitions (M&As), with the number of *caisses* reducing from 1,275 to 800. The pace of integration into a formalized, more centralized network has increased over the past 50 years, but it still consisted mainly of lateral partnerships, meaning that individual member institutions remained small, regardless of the size of the network (Desrochers & Fischer, 2005). In 2003, the Desjardins network in Québec had more than 1,000 member institutions with a total of more than 5 million shareholders/customers. In addition, a major new reform of the network and its governance was implemented in the early 2000s. The reform aimed at simplification, cost reduction, and better coordination within the network. The second-tier structure was eliminated and, after long and controversial debates and voting, a single federation with 16 regional offices was introduced. The new regional networks were allowed to consider new mergers, which took place according to democratic procedures and led over time to a drastic reduction in the total number of *caisses* (Bajo & Roelants, 2011).

The strength and resilience of the Desjardins Group are demonstrated by its financial condition immediately after the global financial crisis (Birchall, 2013). In 2009, Desjardins was the leading financial institution in the Canadian province of Québec and the sixth largest in Canada, with assets of just under C$200 billion. Its Tier 1 capital ratio for 2009 was 15.8%, of which 83.7% consisted of unremunerated capital reserves, and increased to 16.13% in 2010. In 2009, the Group ranked 26th among the 50 safest financial institutions in the world. In Québec, it held 44.2% of savings, 45.3% of agricultural loans, 39.6% of mortgage loans, 27.3% of commercial and industrial loans, and 23.4% of personal loans (Bajo & Roelants, 2011). It employed 39,000 workers in Québec and 42,000 across Canada, ranking among the top 20 largest employers in Canada (Bajo & Roelants, 2011).

In 2017, the Desjardins Group consisted of 293 local credit unions that operated 1,032 branches and had more than seven million members and customers in Québec and Ontario. More than twenty branches of the Group offered products and services related to property insurance, venture capital funds, and brokerage. The Group was also active as a development banking agency in more than 30 developing countries (Desrochers & Fischers, 2005). Desjardins International Development (DID) is an international development organization that strengthens the culture of the cooperative network, leverages available tools and resources for development projects and demonstrates the importance of cooperation in developing countries. It employs permanent consultants with the goal of responding to the demands of local financial cooperatives. Fundraising campaigns and mediation between local contributions and investment projects have significantly reduced transaction costs and failures in local credit markets (Cruz et al., 2015).

In recent years, the Desjardins Group has been configured as a continuously developing and integrated cooperative network to ensure sustainable financial services, owned, and administered by its members, as well as a network of complementary financial organizations that strive to achieve competitiveness in their business sectors and that are still controlled by their member cooperative organizations. Key financial figures for 2020 show that the Desjardins Group has assets of C$397 billion. It achieved surplus earnings before member dividends of C$2.9 million (+21.6%), net loans and acceptances outstanding of C$ 230.8 billion (+9.0%), assets under management of C$ 91.3 billion (+17.8%), a Tier 1A capital ratio of 21.1% of total risk-weighted assets, and member dividends of $ $387 million (+17.3%). The institution employs 53,783 employees and has about 7.5 million members. In terms of social and environmental sustainability, the Group records C$514 million redistributed to members and the community, C$250 million for 2016–2024 from its community development fund (GoodSpark), 127 projects for sustainable communities, and $1.21 billion invested in renewable energy infrastructure (Desjardins, 2021).

11.3.1 Network Governance

Throughout this process, which lasted several decades, the size of the individual *caisse populaire* remained remarkably small compared to, for example, credit unions in the rest of Canada and the United States. On the other hand, the total size of the Desjardins network in Québec is remarkably large, exceeding, for example, the size of all credit unions in Ontario, even though the total size of the Ontario province's economy is larger than that of Québec (Desrochers & Fischer, 2003). The network structure of the Desjardins movement, according to Desrochers and Fischer's (2005) taxonomy discussed earlier, can be placed between consensual and strategic. While regional-level networks preserve their horizontal and diffuse structure, they have built over time central agencies, and developers of products and services that serve the entire group and can assume strategic importance given their unique experience and vision within the group. Thus, while the grassroots FCs deal primarily with day-to-day operations and relationships with individual members and customers, the central agencies provide primarily strategic guidance.

Local FCs appear to have reached, but not significantly exceeded, the minimum size that allows them to be active operational partners in the alliance. Reaching minimum size is critical to increasing the range of products available to members.

Continuous consolidation processes have occurred among the smaller network members, although no large *caisses* have been created and the network has maintained its local roots. Mergers were designed to sustain local ties and increase coordination within networks (Desrochers & Fischer, 2005). The Desjardins group has evolved into a strategic network in which central nodes provide various managerial services and functions to the central banks of the group. Among these functions, leadership and monitoring are particularly important. Strategic alliances between cooperatives and central nodes pool resources and use them as hybrid forms of ownership to achieve common goals. This is done both at the individual level, with reserves accumulated by individual *caisses*, and at the network level, for example, with the lender of last resort function provided by the group's central bank. A sophisticated governance structure has been developed in which each individual cooperative in the network participates in a system of common resources and risk sharing.

11.4 Cooperative Banks in Italy: Cassa Centrale and ICCREA

The first Italian cooperative banks emerged in the northeast of the country, in the regions closest to the German-speaking countries (Veneto, Trentino, South Tyrol, and Friuli), in the last decades of the nineteenth century. They mainly associated producers in rural areas as a reaction to the agrarian crisis of 1882–1883 and the spread of usury. They closely followed the banking model of Friedrich W. Raiffeisen in the Rhineland. The first Rural Bank (RB) was founded by Leone Wollemborg near Padua (Loreggia) in 1883 and associated 32 members. The original RBs were very close to their communities, as they were based on ethical principles of solidarity and followed the doctrine and social action of the Catholic Church (see Pope Leo XIII's 1892 Encyclical "Rerum Novarum"). By 1888, the Federation of Rural Banks and Similar

Enterprises included 51 Rural Banks. The most urgent need in rural areas was to combat usury, which affected many producers whose access to credit was rationed by commercial banks. Second, Italian agriculture needed to increase its capital intensity in a substantial way and significant investment had to be devoted to this goal. The goal was to modernize agriculture and rural areas and support the growth of the country's nascent industrial sector (Catturani & Stefani, 2016).

By the end of the century, there were more than 900 RBs nationwide, of which 775 were Catholic-inspired. RBs also began to spread outside the northeastern regions. In 1909 the National Federation of Rural Banks was founded in Brescia, while the Italian Federation of Rural Banks was reconstituted in 1917 at the end of World War II with functions of group representation and protection, promotion and improvement of member banks, and technical and financial support structure. To be more effective, the Rural Banks were grouped into local federations. The National Federation can be seen as the predecessor of the Italian Federation. In 1919 an important split occurred: the Catholic cooperatives separated from the League of Cooperatives (Laga-Coop, socialist-inspired) to form the Italian Confederation of Italian Cooperatives (ConfCooperative, Catholic-inspired), which included the Italian Federation of Rural Banks.

After World War I, high inflation, unemployment, weakening liberal government, and problems of governance and internal politics challenged the very existence of the *Casse Rurali,* whose structure was still young and financial health still weak (Zamagni, 2006). After more than 20 years of decline and restrictions imposed by the fascist regime, in 1946 the democratic Catholic movement reconstituted the Confederation, and in 1950 the National Federation was recreated. In the following decades (between 1964 and 1975) local federations were recreated and strengthened. They had a role of regional and interregional representation, protection, and technical assistance (Cafaro, 2017). In 1963, ICCREA (*Istituto di Credito delle Casse Rurali e Artigiane*), the central banking institution of all RBs, was created. In addition, the Central Guarantee Fund was established as the main instrument of protection for Rural Banks (Catturani & Stefani, 2016).

The new banking law passed in 1993 (*Testo Unico Bancario*, Legislative Decree 385/93) was a keystone in the institutional evolution of RBs. It loosened previous limits on credit specialization and expanded the geographical area of activity, which remained, however, strongly delimited at the local level. The new name of Cooperative Credit Banks (BCCs, *Banche di Credito Cooperativo*) was introduced throughout the country, with the exception of the provinces of Trento and Bolzano, where they retained their traditional names (Rural Banks and Raiffeisen Banks, respectively). BCCs were authorized by the new law to offer all types of financial services and products to their members, who needed no longer be producers residing only in rural areas. The strong link to localities is demonstrated by the legal constraint requiring BCCs to allocate at least 95% of credit exposures to their geographic area and to assume at least 50% of credit exposures to cooperative members.

Since the reform, some BCCs have been liquidated, transformed into commercial banks, or merged and acquired. The first wave of M&As corresponded to a process of persistent growth in size and economic weight. From 1999 to 2014, the number of Italian BCCs fell from 531 to 376, while in the same period the number of members increased from 558,000 to 1.2 million and the value of assets increased from 77 to 240 billion euros (Catturani & Stefani, 2016). In 1997, the Cooperative Banks Deposit Guarantee Fund replaced the Central Guarantee Fund. The new banking law had the effect of weakening the previously marked differences between BCCs and commercial banks while maintaining localism. In addition to continuing to provide small loans to local farmers and artisans in rural areas, they began to compete with commercial banks and mutual banks (Popular Banks) in providing credit to households and small businesses in urban areas.

Over time, the central banking institutions in the group developed small subsidiaries that aimed to provide advice and technical services to member banks, while second-tier networks at the regional level supported individual banks in increasing efficiency and becoming more competitive. The result of this process was the formation of national and regional networks of BCCs, but these remained significantly decentralized compared to Rabobank in The Netherlands or Desjardins in Quebec. Since the financial crisis of 2007–2008, BCCs in Italy have shown remarkable stability and have been able to maintain or even increase their previous lending levels due to their lower involvement in the subprime crisis and less intensive use of derivatives and other structured financial instruments. In addition, mutualism and cooperative goals meant that BCCs continued to provide credit and services to their members to avoid their bankruptcy and loss of valuable assets. This positive trend was interrupted by the sovereign debt crisis that hit Italy in 2011. Rising taxation and falling consumption affected the social groups most strongly linked to BCCs (middle-income groups). The decline in aggregate consumption in the economy between the end of 2011 and 2014 had particularly damaging effects, as it led to bankruptcy risks for many small and medium-sized enterprises and a sharp increase in nonperforming loans, which had the effect of reducing the actual amount of assets held by BCCs. During this period, the number of BCCs undergoing insolvency proceedings increased and there was a new wave of mergers and acquisitions. In 2015, the national government initiated a new legal reform.

Prior to the reform, BCCs were completely legally independent banks, but at the same time, they were strongly interconnected through a voluntary network composed of two interdependent but not hierarchically ordered structures: an associative network (the national and local federations) with economic, social and political representation functions; and a second-tier banking structure that provides financial products and services. On the associative side, BCCs have been organized into 15 local federations that provide non-financial services (internal audit, compliance, information systems, and anti-money laundering), all of which are in turn affiliated with a national federation (Federcasse). Some local federations may also provide advice on governance and strategy (Catturani & Stefani, 2016; Tarantola, 2011). Financial services are provided by two second-tier central banking institutions, ICCREA in Rome and Cassa Centrale Banca in Trento, which have clear economic and financial functions as they develop economies of scale and scope, product differentiation, and economic efficiency.

The need for greater integration, mutual protection against adverse events, and better access to financial markets (including stock markets) were considered crucial by the government and legislators to ensure the financial sustainability of BCCs in the long run. The reform aimed to structurally change the network of BCCs which, prior to the reform, was predominantly a non-integrated system created on a consensus basis with the goal of mutual support based on cross-guarantee schemes.

11.4.1 The Reform Process in 2016

The reform project was initiated in 2015 and came into effect in 2016 under the impetus of the negative effects of the sovereign debt crisis and a substantial increase in nonperforming loans, including as a result of EU Directive 36/2013 and Regulation 575/2013. The Italian government allowed BCCs to submit independent proposals on how to reform cooperative banks, and the government stepped in to oversee the reform process and propose changes to the Federcasse proposal. The final reform draft was passed by Parliament in April 2016.

Due to the focus on traditional retail banking, the sector had structural weaknesses related to capital requirements for bank efficiency. These weaknesses exposed BCCs to cyclical trends in the real economy, increasing the risks of losses and liquidity crises during downturns. The rigid cost structure, based on traditional banking conducted through branches spread throughout the territory and its local characterization, exposed BCCs to specific adverse events affecting individual or localized banking institutions. The lack of direct access to financial markets, particularly external equity markets, that can recapitalize struggling BCCs, has been increasingly felt as an insurmountable obstacle to BCC's survival and expansion. The need to streamline governance was also highlighted, as closer coordination among BCCs and mutual crisis relief mechanisms were not sufficiently integrated into the governance structure. This could have led to individual BCC defaults that could have been avoided and could have endangered an entire group of financially integrated BCCs. The reform proposal called for, on the one hand, increasing capital levels and a balanced redefinition of the capital structure of BCCs and, on the other hand, opening up to operational forms that could diversify activities and hedge risks—all while respecting their mutualistic nature (Pagani, 2016). The cross-guarantees were to become structural and led to a scheme to mutualize the debt of BCCs undergoing bankruptcy proceedings, while at the same time centralized power of control, intervention and restructuring was given to central banking institutions on an increasing risk basis.

The reform introduced an integrated Cooperative Banking Group (CBG), which would replace federations at the local level and may be established at the national level. Law 49/16 characterizes the CBG as an instrument of integration among banks that maintain their predominant mutuality. The first distinguishing feature is the presence of a parent company established in the form of a joint stock company, while the group members maintain the form of FCs. The majority of the parent company's capital, the minimum amount of which is 1 billion euros, is held by the BCCs belonging to the group. The subsidiary banks can express an opinion and evaluation of the parent company's performance and, at the end of the term of office given to the directors, they can revise the composition of the corporate bodies if the parent company has not achieved the strategic objectives that the CBG had set for itself. The parent company must issue a "cohesion contract" detailing all aspects of governance and finance not defined by law. The contract must be signed by all member BCCs. The contract governs the mutual duties and responsibilities, common rights, and protections arising from the group membership of the individual entities and the parent company, ensuring that business models are consistent with cooperative and land protection principles.

The number of groups to be established was left unspecified and based on the self-organization of BCCs in the national territory. The reform had three main pillars: (i) each CBG would be centered on a central banking institution or group parent company established as an investor-owned (commercial) bank. The BCCs in each group would have been members of the parent company. The parent company would have had access to financial markets like all other banks, with the only constraint being that its control (at least 51% of its shares) would be retained by the member BCCs. Each parent company would have had a minimum capital of €1 billion and at least 500 members; (ii) protection against financial distress of individual BCCs was addressed in an integrated manner on the basis of a mutual assistance rule based on an increasing risk criterion. The CBG provides protection against insolvency risk to all members. It must intervene with its own funds deposited with the parent company to rescue any affiliate in financial distress. Upon intervention, the central bank must assume the liabilities of the subsidiary, if necessary, and is authorized to restructure its assets and liabilities to make it financial sustainability. When this proves impossible, the central bank may decide on the liquidation or forced takeover of the troubled subsidiary by other subsidiaries in better condition. It may also decide on the merger of two BCCs. Intervention should be strictly limited to cases of distressed affiliates, while in all other cases individual BCCs retain their full autonomy; (iii) governance can be restructured and integrated to enable BCCs in difficult conditions to regain organizational efficiency and effective decision-making. While prosperous BCCs retain their full autonomy, the increasing risk rule implies that, in the event of financial difficulties, the governance and especially the board of BCCs can be commissioned and changed by the parent company. In more general terms, all affiliated BCCs are free to select suitable candidates to be democratically elected as members of the board of directors and other corporate bodies, but the list of candidates must be approved by the central institution. The parent institution is also in charge of coordinating the BCCs in the group (Felicetti, 2020; La Torre, 2020; Poli, 2019).

11.4.2 The Creation of Two Strategic Networks: Cassa Centrale Banca and ICCREA Banca

The exact number of nationwide groups was the subject of intense debate for several months after the law was passed in 2016. While ICCREA, which was already the central banking institution for all Italian BCCs, proposed the creation of a single national cooperative group that would own a significant share of the credit market (BCCs as a whole account for about 10% of the credit market in Italy), Cassa Centrale, which traditionally was the second-largest financial institution and was also responsible for providing most non-financial services (ICT and back office, leasing, consumer credit, real estate, insurance, asset management), preferred to remain true to its cultural and regional identity in the northeast of the country, where BCCs had spread in the first stance in late nineteenth century. Other hypotheses of additional CBGs were aired, but they did not make it through the process of gathering enough member BCCs or a billion euros in capitalization. In the end, two groups were created and issued their respective cohesion contracts, to be signed by all member BCCs, in 2019.

The Cassa Centrale Group has 71 member banks: Cooperative Credit Banks, Rural Banks, and Raiffeisen Banks, with a total of 1,484 branches throughout Italy, 11,450 employees, and about 450,000 members. The parent company's branches throughout the country are located in Trento, where the headquarters are also located, Udine, Padua, Brescia, Cuneo, Bologna, Rome, and Bari. Capital strength, low risk, and an efficient organizational model are the key characteristics of this group, which has a CET (Common Equity Tier) 1 Ratio of 20.9%, a coverage ratio (coverage of impaired loans) of 66%, and a net profit of 307 million euros in 2021. Cassa Centrale Banca's stated goals are to sustainably promote the welfare of members in the areas in which it operates, growth and innovation, and a strong relationship with the local community. Autonomy and capital strength are the characteristics considered most conducive to efficiency, adaptability, and resilience (Birchall, 2013; Cassa Centrale, 2022).

The governance model adopted by Cassa Centrale is a traditional one, based on the distinction between the board of directors, with strategic and supervisory functions, and the board of statutory auditors, in charge of monitoring and supervising compliance with the law and the bylaws, compliance with the principles of proper administration, and the adequacy of the organizational, administrative, and accounting structure. The statutory audit is entrusted to an external and independent auditor, in accordance with the relevant statutory provisions.

The ICCREA Cooperative Banking Group has 130 affiliated BCCs (including 39 in the North, 47 in the Center and 44 in the South), with a total of 2,529 branches throughout the country, 824,610 cooperative members and more than 3 million customers. It manages and coordinates group companies and centralizes services related to key governance and control functions; it also supervises and manages banking, financial, and service activities for affiliated BCCs (ICCREA, 2021).

Maintaining strong ties with the respective territories of member cooperatives is one of ICCREA main stated objectives. To this end, the financial resources raised by member BCCs are almost entirely deployed in the same places where they were created, with the aim of supporting long-term economic and social development. The effort to achieve a strong capital base has resulted in capital reserve ratios above the required minimum. The CET 1 Ratio is 16.4%, while from December 2017 to June 2021, the stock of impaired (or nonperforming) loans (NPLs) was halved from about 17.5 billion to about 8.3 billion. The reported net income is 400 million in the first half of 2021, up from 122 million in the first six months of 2020. Net commissions grew by 50 million in 2021, generating revenues of 650 million euros. The financial and social sustainability model pursued by the group meant that 84% of its loans in 2021 went to support families and small and medium-sized enterprises, while 41 million euros were disbursed to support 15,837 territorial initiatives. More than 99% of its suppliers are Italian. In terms of environmental sustainability, the group has reduced climate-changing gas emissions into the atmosphere by 17.43% in 2021 compared to 2019, and the use of electricity from renewable sources accounts for more than 72% (it was 64% in 2019). In terms of indirect impacts, the group has contributed to the EMTN (Euro Medium Term Notes) program through the issuance of Green and Social Bonds. Financial support to local businesses, the adoption of circular economy principles, and promotion of the well-being of the group's employees through welfare, inclusion, and diversity policies are among the main objectives in pursuing sustainability goals (ICCREA, 2021).

11.5 Discussion and Conclusion

Analysis of three cases of financial cooperative networks in three different countries (The Netherlands, Canada, and Italy) revealed some important elements that seem to be common and create similar evolutionary patterns among different nations, and historical and institutional contexts. These common elements appear especially important. The first concerns local embeddedness, cooperation, and relational intensity: (i) a strong degree of local rootedness, in that their action is always locally anchored and aims at the improvement of socio-economic conditions in their close range of action, involving actors (small businesses, households, communities, and local governments) who, as a rule, act in networks of interpersonal relationships in the territory in which they are located. In this sense, FCs can be said to be an integral part of local development processes driven by endogenous factors (Borzaga & Tortia, 2009; Capello, 2015); (ii) horizontal personal and organizational coordination prevails over vertical relationships, as FCs not only create networks among themselves, but are embedded in broader networks of local actors that most often do not have central or stronger nodes, but are instead complex, multilateral, and decentralized. The personal dimension, which is often quite marginal in traditional banking systems, gains in importance following the paradigm of relational banking. Tacit knowledge and trust may be dominant, according to the relational paradigm (Aoki & Dinç, 1997;Cornée et al., 2018); (iii) FCs follow development patterns informed by cooperation rather than competition. Although competition among FCs is observed sporadically, dominant evidence shows that FCs seek horizontal coordination through cooperation with other institutions that have similar goals even in the context of market exchanges. Cooperation is based on common values, but also on instrumental and substantive rationality, as it can lead to mutually beneficial outcomes, while the small size and local nature of FCs prevent them from achieving significant economies of scale and large market shares. Cooperative pacts, both formal and informal, are used to pursue common network goals and also to acquire needed services, either from common providers or by producing within the network.

The second important element emerging from the case studies is a clear evolutionary trend of cooperative networks becoming more formalized and integrated over time. This process took place first in The Netherlands (Rabobank), but has also been observed in Canada (Desjardins) and Italy (ICCREA and Cassa Centrale). The trend toward integration can be explained in neo-institutionalist terms. The need to make network-specific investments in new financial services, tools, and digital technologies, for example, is a powerful incentive for FCs to seek forms of greater integration in governance and production. In addition, integration and formalization help reduce contract failures, risks and costs, as simple contracts or informal relationships are replaced by increasing elements of centralized administration (Hennart, 1993; Williamson, 1975). Integration does not only have positive effects. Administrative structures can be costly and burdensome, and their governance can encounter difficulties and breakdowns due to inability to make collective decisions effectively (Hansmann, 1996). However, the observed tendency to seek integration seems to show that the benefits outweigh the costs and that CFs have found this evolutionary pattern almost inevitable. On the other hand, it should also be added that banking regulatory frameworks at the national and international levels have strongly favored integration to support the financial sustainability of FCs and reduce the risks borne by their customers, especially depositors.

A third important observation concerns the presence of a central banking institution in all the networks analyzed, which plays a pivotal role in serving the member banks with the production of financial services, acts as a lender of last resort, but also carries out monitoring and control activities, in some cases including sanctions and restructuring of the members' governance. It can intervene to safeguard customers from financial risks taken by member banks. The functions of the central institution prove vital to the survival and expansion of the entire network, and a relentless process of strengthening both financial and control functions is observed in all networks.

As a final comment, we emphasize that the FC networks studied in this chapter all involve a transition from a consensual network to a strategically oriented and integrated network, as hypothesized by Desrochers and Fischer (2005). In all cases, the initial creation of FCs in the late nineteenth and early twentieth centuries largely represented spontaneous choices and behavioral patterns, in which membership and cooperation are voluntary but deliberately sought, leading to an important degree of internal coordination and agreement among affiliates. Spontaneous coordination is formalized step by step and eventually results in a greater degree of integration and the creation of common structures, administered organizations, and central institutions of control. Although the network still retains important elements of decentralization and independence (affiliate banks are free to conduct their activities independently), control and strategic direction are increasingly assumed by the central institutions and their agencies, which identify basic choices and instruments common to the entire group. This thesis seems to be supported in several respects by the theory of the emergence of strategic networks in cooperative banks (Desrochers & Fischer, 2005), and also by the emphasis on the importance of horizontal networks where horizontal coordination is still the dominant feature of cooperative action even in the financial sector (Sacchetti & Tortia, 2016). However, this may not necessarily be so for all networks when regulatory overload is observed and central control and sanctions replace horizontal interaction.

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