



Co-op Builder – User Guide 2017



Farm Co-operatives
& Collaboration

Pilot Program

Farming together.



BUSINESS COUNCIL
OF CO-OPERATIVES AND MUTUALS



Australian Government
Department of Agriculture
and Water Resources

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Introduction

The Co-op Builder is an online tool that simplifies the preparation of documents required for the formation of a distributing co-operative.

A distributing co-operative must have a constitution (set of internal rules) and a disclosure statement (a prospectus for members) that meet the requirements of legislation governing the registration of co-operatives.

This User Guide is designed as an introduction to the regulatory context for co-operatives in Australia and the processes required for formation and registration. It explains the purpose of the Co-op Builder and how it can assist groups of people or businesses to draft these important documents and better understand their meaning.

The Co-op Builder can be accessed at www.farmingtogether.com.au. Find it under 'Resources'.

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1. Why register a co-operative?

Choosing a business structure is important. The chosen structure should suit the functions of your enterprise and reflect how your group wishes to collaborate.

Co-operatives work for a different purpose

Co-operatives are autonomous enterprises that are owned and managed by their members. They are designed to provide services to their members in a cost-effective manner, thereby improving the economic bottom line for members. Members contribute to their co-operative by providing capital and transact with the co-operative by using its services. As owners, members benefit not only from the access to services, but also from the fact that a co-operative uses its profits only to benefit members.

Most business consultants, lawyers and accountants are likely to be familiar with the company structure and the relatively streamlined process for registering a new company. A company can be registered using an online service that is directly linked to the Australian Securities and Investments Commission (ASIC) in a very short time, at minimal cost and using a one-size-fits-all constitution.

Companies can be a suitable business structure for a collaborative enterprise. However, the basic purpose and design of a company is to maximise shareholder returns. Without careful drafting and redesign of a company's constitution, it may not suit the purpose of a collaborative endeavour.

Legislation governing co-operatives entrenches a mutual model that ensures that a co-operative works to serve its members. Only members who actively transact with the co-operative can hold shares, and they each have the same voting rights. They must operate in accordance with co-operative principles that ensure responsiveness to member needs. The relationship between a co-operative and its members is described as a 'mutual' relationship: co-operatives work for and with their members to achieve a mutually beneficial outcome.

Forming a co-operative is more complex than a company

As their name suggests, co-operatives rely on the co-operation of a group of people. They are not like a small enterprise such as the family farm where there is likely to be a desire for control in the hands of

some family members, the benefit of limited liability and the ability to split the income in a tax effective manner.

Co-operatives are about people or businesses collaborating to achieve a better outcome for their own enterprises by jointly securing a service (e.g. marketing, data collection processing, storage etc.), or resources that cannot be bought by a single person or business. In doing this they are agreeing to work together. Co-operatives require a minimum of 5 members to work together.

A proprietary company structure may be a better choice where the project involves less than 5 members and/or it is likely to be a closed project - i.e. the original business owners would prefer to control the project and are unlikely to be willing to take on new members and share control. A proprietary company, with its 'one size fits all' constitution, provides a simple legal vehicle for a business to be owned or run by one person or by many persons (up to 50). It doesn't, without substantial variation of the constitution, accommodate a collaborative approach to running an enterprise for the benefits of user members.

In some ways, a co-operative structure is like a partnership. It relies on a relationship of trust and confidence between the members to contribute to the enterprise and share in the profits or cost savings of the enterprise. In a partnership, partners may join and partners may leave, and they need to be able to settle how they make decisions that impact the enterprise. To accommodate how partners will contribute, share, make decisions and come and go in the partnership, there needs to be a formal agreement. Partnership agreements can be complex, and costly to draft.

A co-operative constitution deals with the same issues, and it is supported by legislation governing co-operatives. Importantly, it provides limited liability for members. If a collaborative enterprise is the goal, then a co-operative is well suited to this purpose.

Co-operatives also have many of the characteristics of an unlisted public company.

- There are no limits to the number of members of a co-operative
- They can issue shares
- They can issue other securities to raise finance – debentures and hybrid securities called Co-operative Capital Units

Founding members of a co-operative need to plan and agree how they will work together and how much capital they will contribute. This agreement and how they will work together become the two documents necessary for formation of the co-operative: the constitution and the disclosure statement. When these documents are settled, and the founding members have formally agreed to form a co-operative, the new entity is ready for registration. Once registered, new members can join the co-operative and they will join on the basis of the agreement in the constitution and the information in the disclosure statement.

Co-operatives have a different purpose; need different management

Co-operatives don't suit every enterprise. Co-operative governance requires a management team focussed on member interests and engagement rather than dividends to shareholders. Successful co-operatives are those that recognise the different purpose of a co-operative. Co-operative enterprises can and do provide a stable business structure for farmers and the communities in which they operate as they are not prone to speculative short term gains for shareholders.

2. Co-operatives National Law

Legislation governing the registration of co-operatives is state based. Until 2014, co-operatives faced regulatory costs to carry on business across a state or territory border.

States and territories agreed to a uniform scheme of legislation that would allow freedom for co-operatives to carry on their business in any jurisdiction. The uniform scheme also updated legislative requirements for registration, financial reporting and accountability. The scheme is referred to as the Co-operatives National Law (CNL).

Parliaments in each State and Territory have their own way of participating in the CNL scheme.

- New South Wales, Victoria, South Australia, Tasmania, the Australian Capital Territory and the Northern Territory adopted a template or legislative code passed by the New South Wales Parliament and called the Co-operatives National Law.
- Western Australia passed the Co-operatives Act, which is consistent with the CNL.

- Queensland has not amended its Co-operatives Act at this stage. Basic registration and democratic principles under this legislation are similar to CNL requirements.

The CNL scheme brought about a change of name for co-operative types. Not-for-profit co-operatives are called **non-distributing co-operatives**, those co-operatives that can distribute profits to members are called **distributing co-operatives**.

Queensland registered co-operatives are referred to as **non-trading or trading** co-operatives respectively.

Co-operatives registered in a state or territory under the CNL scheme are able to carry on business in any other CNL state or territory without further regulatory requirement or cost.

New opportunities for capital raising

CNL co-operatives can now raise capital by issuing member shares in any CNL jurisdiction without further regulatory compliance.

The CNL also allows co-operatives to raise capital (from members or external investors) by issuing Co-operative Capital Units or CCUs. A CCU is defined as an interest in the capital (but not the share capital) of a co-operative. The availability of CCUs encourages the development of flexible financial instruments that meet the needs of co-operatives at different stages of their development. They can be structured to look like either debt or equity, but carry no voting rights in the co-operative's affairs.

CCUs can be freely traded on the ASX. Whilst not yet well known, CCUs await development and recognition in financial markets and as a means of encouraging strong and sustaining community investment.



3. Overview

The Co-op Builder can be accessed at www.farmingtogether.com.au.

Find it under 'Resources'.

The requirement to draft a constitution and a disclosure statement for a co-operative can impose a substantial cost for a start-up enterprise. The Co-op Builder is a user-friendly tool to put together the two legal documents that must be prepared before you can form a co-operative.

The Co-op Builder is two tools

Constitution Builder – a mix of standardised rules that meet legislative requirements and rules that require customising to suit the co-operative to be formed.

Disclosure Statement Builder – standardised text, prefilled text taken from the constitution, and text that requires customising to tell the story about the co-operative and its business and operations.

The documents you prepare using each tool are linked. You must complete the constitution before you start the disclosure statement. Information from the constitution is automatically saved into the disclosure statement.

Completing the Co-op Builder delivers draft documents ready to send to the Registrar for approval. Instructions to complete the necessary steps for formation, registration, and links to forms and resources complete the Co-op Builder package.

Constitution and disclosure statement – approval by Registrar

Under the legislation in all jurisdictions, a draft constitution and disclosure statement must be approved by the Registrar before a co-operative can be formed.

The Registrar has a responsibility under the legislation to ensure that the co-operative's constitution is designed to operate on co-operative principles and that it contains a clear description of the transactional relationship between the co-operative and each member: the active membership requirement.

The disclosure statement is a mandatory requirement for all distributing co-operatives. It must also be approved by the Registrar because it is the document that each member relies on, either at start-up or later, to decide to join and buy shares.

These are start-up documents!

To design a user-friendly tool to draft these two documents, standardised content and guidance

material is focussed on the preparation of documents that will meet the legislative requirements and the practical requirements of a co-operative at the point of start-up.

As a co-operative commences operations it may become apparent that there is a need to change or adjust its constitution. There are many reasons why this may happen, and the reasons may not be obvious during the planning stage. The constitution can be amended and the process for doing so is contained within the constitution itself.

Your disclosure statement will become a 'live' document. The disclosure statement sets out financial matters as well as costs and obligations for members. There is a legislative obligation to ensure that the disclosure statement remains *current*. This is because it is a document that will be relied on by persons who wish to become members at any time after the co-operative is formed.

What is needed before using the Co-op Builder?

Before you use the Co-op Builder, you need to have put in some time and effort to determine if your business proposal is viable and that you have 5 or more other people or businesses who will work together.

As this is a collaborative business enterprise, the plan should encompass the joint expectations and ideas of your founding members. You will find a basic guide for developing a *Business and Operations Plan* at the start of the Co-op Builder.

Developing a *Business and Operations Plan* may take some time. Start-up capital for the first year will primarily come from your members, so you will need to assess how much capital members are able or willing to commit to the co-operative. If member capital is not sufficient, you need to consider how best to obtain the necessary capital.

Co-operatives work best when they have clearly identified the services needed by members and members are ready, willing and committed to actively using those services. During planning, you need to produce forecast financials for the first year of operation of the co-operative that outlines the expected transactions with members.

The road map

This two-page document is downloadable at the beginning of the Co-op Builder. It provides a quick visual representation of the formation and registration process, and checklists to follow as you progress through each of the Constitution and Disclosure Statement Builders.



Saving and editing documents in the Co-op Builder

The Co-op Builder saves your document as you progress. If you stop and log out at any point, when you next log in it will take you back to where you were.

Completed documents will be saved in your Account with the name of the document and the date and time that you completed them.

Don't worry if you want to go back and change anything – as you draft your documents, they are saved within the account that you create when you register to use the Co-op Builder. You can go back and edit both documents, keeping in mind that changes you make to one document may need to be followed up and checked for consistency in the other document.

4. A closer look at the tools

The Co-op Builder tools will provide you with as much standardised content as possible for both the constitution and the disclosure statement. Key parts are left for you to complete, to tailor the documents to meet the design and business objectives of the co-operative.

The Constitution Builder

The Constitution Builder is the first tool that you must use.

The constitution that you will draft using this tool will have 61 rules, divided into 6 subject categories – 50 rules are standardised and cannot be changed.

The standardised rules meet the requirements of the legislation and are suitable for any co-operative at

the start-up stage. Each standardised rule will appear on the screen followed by an explanation of what the rule is about.

Eleven rules require customisation or drafting. For some rules, customising means simply choosing a reference to the legislation that applies in the state or territory in which the co-operative will be registered. Other rules may require you to choose between options; a few rules will require you to draft specific content.

For each rule that requires customisation, there is an explanation of what the rule is about, and guidance to help.

The Disclosure Statement Builder

When you have completed the constitution, you will be directed to the **Disclosure Statement Builder**.

The disclosure statement is set out in a different style from the constitution. There are 8 parts in the disclosure statement that address different aspects of the co-operatives' activities and business operations and how the membership relates to the co-operative.

A large portion of the disclosure statement comprises standardised text. The standardised text addresses information that is common to all co-operatives. Other text will have been automatically saved from your constitution.

The parts of the disclosure statement that you need to draft are those parts that directly describe what you have discovered in the process of settling your Business and Operations Plan. You will be instructed to include your plan as part of the disclosure statement.

5. Next steps – register your co-operative

Once you have finalised your documents using the Co-op Builder, you can download them in PDF format. There are links to each state and territory Registrar and the forms that you need to complete to start the registration process.

You will then be ready to submit the documents for approval by the Registrar.

Registrar approval

The Registrar will check to see that your documents reflect co-operative principles and meet legal requirements. Submitting the documents in the PDF format provided by the Builder will provide the Registrar with assurance that your documents contain compliant, standardised content.

Formation meeting

Once you have approval from the Registrar, you can hold a formation meeting with 5 (or more) members. This is when the first members of your co-op officially meet and agree to form the co-operative. The members will elect directors and appoint a secretary.

Registration

Using a form provided by your state or territory's Registrar, you will need to send proof of your formation meeting. Once processed, your co-operative will receive a Certificate of Registration and you will be ready to start.



6. Tips for drafting some of the more complex rules in the Constitution

Rule 1.3A: Primary activities

The primary activities rule (*rule 1.3A*) and the active membership (*rule 1.3B*) are the most important rules for a co-operative. They require careful consideration and drafting.

Rules 1.3A and *1.3B* together represent the core reason for the co-operative's existence because they describe precisely what the co-operative will do in practice (primary activity or activities) and what each

member will do to support the primary activities of their co-operative (active membership).

In your *Business and Operations Plan* you should have identified ***the main income producing activity of the co-operative***. This will form the basis of the primary activities rule. The drafting of this rule will determine the membership base of the co-op (who will join and benefit from membership?). It is recommended that you identify 2 or 3 core activities that underpin the co-operative's reason for being. These primary activities should be the ones that the members ***are mostly likely*** to need and therefore most likely to support. They must be activities that the co-op can deliver.

Checklist – for drafting a primary activities rule

- ✓ Is the primary activity expressed as a phrase that involves the actual doing of an activity or performance of a function?
- ✓ Is the stated primary activity one that all potential members are able to support through a transaction with the co-operative?

*Note: **if not all of the potential members are able to support the primary activity through a transaction with the co-operative, you will likely need to include a second or third primary activity.***

- ✓ Are the activities that you have described the main income producing activities of the co-operative according to the *Business and Operations Plan*?

Checklist – for drafting a primary activities rule

The primary activities of the co-operative are

- *to dry, process, market and sell spirulina on behalf of members,*
- *to implement standards for the testing, grading, packaging, labelling, processing and shipping of spirulina in powder form.*
- *to provide training and consultancy services to Australian spirulina growers and associated industries, and*
- *to develop allied support services for members*

Rule 1.3B: Active membership

Once you have identified the co-operative's primary activities it will be easier to clearly articulate the minimum requirements for members to support the primary activities of the co-operative. The

active membership rule is the transaction that is the 'other side' of the co-operative's primary activity and thereby creates the mutuality of interests that is the basis of the co-operative business model.

Checklist – for drafting active membership rule

- ✓ Does the active membership rule relate to specific primary activities?
- ✓ Is it expressed in simple terms?
- ✓ Is it measurable as to quantity and time?
- ✓ If there are multiple active membership requirements, are they expressed as alternatives or additional requirements?
- ✓ Is it a reasonable requirement – that is, not too onerous and yet sufficient to ensure an ongoing transactional relationship between the co-operative and its members?

Sample Rule 1.3B:

In order to establish and maintain active membership of the co-operative a member must

- *supply 10kgs of fresh spirulina to the co-operative each year, or*
- *purchase consultancy services from the co-operative to the value of \$100 each year.*

Rule 4.1.2: Board of directors

The Co-op Builder requires you to select a number between 3 and 9, to indicate how many directors there will be on the co-operative's board. The decision on the number of directors can sometimes be difficult. The number of directors required at start-

up may be different from the number considered to be adequate after a period of operation. This rule can be amended later. To help determine an appropriate board size at start-up, it is useful to consider the pros and cons of a small board compared with a larger board.

Advantages & disadvantages of a small or a large board

For example

- *A larger board may suit the needs of a co-operative at start-up because of the need to establish policies and systems.*
- *A larger number of directors may cost more in director fees than employing a business consultant to set up policies etc.*
- *It is easier to get a small board together to meet.*

Remember: For specific matters such as audit & risk, governance, workplace health & safety, strategic planning (to name but a few) a co-operative board may decide to establish one or more **committees** (perhaps comprised of directors, members and key staff) to deal with the issue at hand. Committees of

this kind can report back to the board of directors, which has the authority to make decisions on matters considered by that committee. A board of directors may also delegate authority to key management staff, where appropriate.

Rule 6.3: Member financial statements and audit

In CNL jurisdictions, small co-operatives may decide on the preferred method of annual financial

reporting to members – either audited financial statements or basic financial reports. To make a choice, you should list the pros and cons.

Advantages & disadvantages of a small co-operative undertaking an annual audit?

For example

- *An audit process provides members with an external check on internal record keeping and processes.*
- *Annual audits potentially involve a significant cost for a smaller sized co-operative. Can risk be managed differently?*



Farming Together

Cathy Byrne cathy.byrne@scu.edu.au

02 6626 9505

Or Farming Together program

02 6620 3020

Business Council of Co-operatives and Mutuals

Anthony Taylor info@bccm.coop

02 9239 5931