

# The Mondragon System: Cooperation at Work

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## Introduction

Cooperativism "is the third way, distinct from egoist capitalism and from the mastodon of depersonalizing socialism."<sup>1</sup>

"From its genesis, development and success in a local and domestic market, (Mondragón) finds itself in a new competitive planetary scenario, where the validity of its socially oriented model will be tested."<sup>2</sup>

The Mondragón Cooperative Corporation is a 35 year old experiment in building a comprehensive cooperative society in which labor plays the primary and dominant role. The Cooperative Group has amassed technical, managerial and financial resources comparable to those of a major corporation and used those resources to further social as well as economic goals that emphasize the importance of community and small and medium scale enterprise.

Headquartered in the city of Mondragón, population 30,000, the Cooperative Corporation has member cooperatives in all four of Spain's Basque provinces. The Corporation consists of over 160 cooperative enterprises, of which 90 are industrial companies, and has over 21,000 worker-owners. Its economic activities represent 2 percent of the economy of the Basque provinces<sup>3</sup> and about 14 percent of the economy of the province of Guipuzcoa, in which Mondragón is located.<sup>4</sup> Within the municipal area of Mondragón, the Cooperative is the predominant employer and economic force. As much as 50 percent of the workforce in the city of Mondragón may be cooperative partners.<sup>5</sup>

In Mondragón, cooperative members could spend much of their lives and satisfy many of their needs within their own cooperative structures. They could attend school from day care through post graduate instruction within a cooperative structure. Members can shop in several hundred cooperative stores, some of them the size of K Marts with a similarly diverse merchandise selection. Although only a small proportion of the food products they buy might have been grown and processed in their own agricultural cooperatives, they could buy most of their appliances from cooperative factories. Medical care, home, auto, business and life insurance, disability benefits, family allowances, unemployment

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<sup>1</sup> Don José María Arizmendiarrreta, cited in William Foote Whyte and Kathleen King Whyte. *Making Mondragón: The Growth and Dynamics of the Mondragón Cooperative.* Ithaca, N.Y.: Cornell University Press, 1988.

<sup>2</sup> Jesús Larrañaga, one of Mondragón's founders. May 1992

<sup>3</sup> Roy Morrison, *We Build the Road As We Travel.* Philadelphia: New Society Publishers, 1991.

<sup>4</sup> Henk Thomas and Chris Logan. *Mondragón: An Economic Analysis.* London: George Allen & Unwin, 1982.

<sup>5</sup> Hans Wiener and Robert Oakeshott. *Worker-Owners Mondragón Revisited.* London: Anglo German Foundation, 1987.

insurance and pensions are all financed and managed through their cooperative system. Their bank is a cooperative. So is their travel agency.

These cooperative enterprises are owned and managed by their workers<sup>6</sup> but the services and products they provide reach out to a much larger community. Eroski, the Cooperative's retail chain, consists of more than 250 stores and almost 200,000 consumer members and wholesales to many small mom and pop stores in the region. The Caja Laboral Popular, the Cooperative's bank has branches in virtually every Basque neighborhood and boasts over 600,000 depositors and about \$4 billion in deposits.

The Mondragón Cooperative Corporation has evolved a structure that allows for democratic governance of business while enabling a level of individual initiative and technological innovation that has allowed its enterprises to compete not only in Spanish markets but in world markets. Thirty percent of the Cooperative's industrial products are exported. The Cooperative Corporation includes Spain's largest Spanish owned refrigerator manufacturer and machine tool manufacturer. Its Research and Development Center is the only one in Spain selected to be part of the European R&D consortium. The first Spanish robot was designed and built by several Mondragón cooperatives.

Virtually all of this development has been internally financed, in part from the surplus of individual enterprises, and in part by channelling a significant portion of the savings of the Basque region's 2.3 million people.

The Cooperative's economic performance has been impressive. After assessing the statistical evidence, one observer concluded, "Measured by the yardstick of 'profit', (the Cooperative Corporation's) record has been at least respectable. By the alternative measure of sales or value added per head it looks distinctly good. Measured either by the criteria of worthwhile jobs or by savings mobilization it is outstanding."<sup>7</sup> The average profitability of Mondragón coops in 1980 was reportedly twice that of the average Spanish corporation.<sup>8</sup>

The Cooperative has many of the attributes of a government in that it establishes the rules of conduct for a large part of the activities of the community, and makes fundamental decisions about the allocation of a very large portion of the community's income and assets through a one person, one vote democratic decisionmaking process.

Yet, the Cooperative is unlike a traditional government because citizenship is not a function of where people live. Instead, citizenship is reserved for those who have invested their capital and labor and are continually at risk as a result of the reinvestment of their portion of the profits.

The Cooperative also has many of the attributes of a corporation in that its individual cooperatives are increasingly coordinated by a central administration. Yet unlike traditional corporations, the Mondragón Cooperative Corporation's

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<sup>6</sup> See below for a discussion of the governance structure of Mondragón.

<sup>7</sup> Robert Oakeshott, "A Cooperative Sector in a Mixed Economy", in Alasdair Clayre(ed) *The Political Economy of Cooperation and Participation. A Third Sector.* Oxford, England: Oxford University Press, 1980.

<sup>8</sup> Terry Mollner, "The Relationship Age and a New Kind of Nation", *World Futures.* Vol. 31. 1991

labor force consists not of employees but of partners who share both profits and losses and help to make fundamental corporate decisions.

Now the Mondragón cooperative experiment is facing its greatest challenge. The unified European market has stripped Spanish industry of its defenses against large multinationals and has put a huge premium on access to continental and even global marketing and distribution networks. And a persistent economic slowdown in Spain and the Basque Country has made job creation more difficult.

Reacting to these external factors, the Third Cooperative Congress in December 1991 approved policies that substantially alter the structure, operation and some might say, the underlying nature of the Mondragón cooperative system. The changes are reflected in the cooperative's new name, the Mondragón Cooperative Corporation (MCC) rather than Mondragón Cooperative Group. Planning and decisionmaking has become more centralized. Cooperatives have been merged into functional product lines. And MCC for the first time, has begun to make substantial investments in non cooperative enterprises inside and outside of the Basque region.

To the leaders of the MCC, these changes are a necessary reaction to the new economic reality. José María Mendizabal, one of the early members of the cooperative community insists, "Our cooperativism is dynamic and modern, adaptable to the current times. We have not remained in the Rochdale era. That would not be beneficial. The capitalism of today is not the capitalism of the 19th century. Nor can the cooperativism of today be the same as before."

Whatever the outcome of the momentous changes currently occurring in the Mondragón cooperative community, we have much to learn from its experience. For those seeking strategies that marry social values and economic efficiency, the Mondragón experiment offers a rich source of inspiration and experience.

## **Basque Society: History and Culture**

Any examination of Mondragón must begin with a discussion of the larger regional society of which it is part.

The Basques may be the most rooted people on earth, living in the same region for 3,000-10,000 years, perhaps as far back as Cro Magnon man. The Pyrenees' mountainous terrain has not protected them from foreign invasions but it has protected them from foreign occupation. Their ancient, unique and difficult language, Euskera, is unrelated to any other Indo European tongue.

One historian described the Basques as "a race of hardy mountain folk with mountain virtues, who know their own mind and can defend their traditions and convictions with a courage and spirit of independence amounting almost to fanaticism..."<sup>9</sup>

The Basques have a strong sense of family and self-reliance and a history of democratic traditions. "All of this region has a simple type of rural economy that has come down more or less unchanged from early times and is not derived from

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<sup>9</sup> Rodney Gallop, A Book of the Basque. Reno. 1970

the decay of feudal institutions", wrote one observer in 1943. "It is a country of small proprietors or tenant farmers, working on a family basis and possessing sufficient land to maintain themselves adequately...(T)hey are not grouped in small towns or villages, but lie scattered in isolated farms and hamlets. As the rainfall is abundant and the soil adequate, they are fairly prosperous".<sup>10</sup>

Traditional Basque law and custom required that an entire farmstead be passed on to one chosen heir. Therefore land was not broken up into very small units and remained a viable economic entity. This also encouraged unusually stable family units.<sup>11</sup> According to some sources, the Basque tradition of group decisionmaking even invades the household. The head of household "does not abuse it(his position) for in all matters of importance affecting the welfare of the house, such as the purchase of a cow or the rotation of crops, he takes counsel not only with all the members of the family, but even with the servants."<sup>12</sup>

The Basques are tied together by small group social networks. "Social life is intense; one is seldom alone", writes sociologist Sally Hacker.<sup>13</sup> Every Basque schoolboy joins a cuadrilla, part drinking club and part mutual aid society composed of 10-20 members. There were 2500 private Basque drinking and eating clubs in the mid 1960s.<sup>14</sup> Hacker notes that more bars exist in Guipuzcoa province(headquarters of Mondragón) than in the whole of the European Common Market. In my own experience in the city of Mondragón, I discovered a dozen bars in a single block. Most consist of a small room or two whose main purpose is social rather than sexual or alcoholic. Groups roam the streets, walking from bar to bar, engaging in brief conversations, a ritual known as "chiquiteo".

The Basque region, as with several other regions of Spain, possessed significant political autonomy for much of its history. In the 16th and 17th century every male head of household was entitled to vote for members of the municipal government. In Guipuzcoa and Vizcaya municipalities elected representatives to a provincial government. General assemblies in these two provinces codified the common law into *fueros*--laws to govern and administer the provinces as autonomous units.<sup>15</sup>

Local governments had the sole power to tax property and mobilize soldiers. They had the right to review any laws promulgated by the central government before they could go into effect if the laws affected the province. The province could veto royal edicts.<sup>16</sup>

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<sup>10</sup> Gerald Brenan, The Spanish Labyrinth: An Account of the Social and Political Background of the Spanish Civil War. Cambridge University Press. Cambridge. 1960.

<sup>11</sup> Spanish law specifically dictates that property be divided among several heirs, but the Basques ignored the law. Morrison, Op. Cit.

<sup>12</sup> Gallop, Op. Cit.

<sup>13</sup> Sally Hacker, Pleasure, Power and Technology. Unwin Hyman. Boston . 1989.

<sup>14</sup> Ibid.

<sup>15</sup> Whyte and Whyte, Op. Cit.

<sup>16</sup> Robert P. Clark. The Basques: The Franco Years and Beyond. University of Nevada Press. Reno 1979.

Beginning in the 17th century the Spanish crown withdrew much of its support for local autonomy and restricted the right to vote in municipal elections to those who met a wealth requirement.<sup>17</sup> Yet local self-determination, until the late 19th century, continued to be a major element in Basque life.

The Basque territory was the first Spanish region to industrialize. Sturdy oak trees provided timber for vessels and the Basques quickly became a maritime culture, adventurous, and daring.<sup>18</sup> As early as the 16th century the coastal provinces of Vizcaya and Guipuzcoa became centers of commerce, trade and manufacturing. The Basque provinces were blessed with large amounts of low phosphorus iron<sup>19</sup> and nearby supplies of coal from Asturias to the west.

In 1766, the new Basque commercial and political elite formed the Basque Society of Friends of the Country. Its first goal was, "To cultivate the inclination and the taste of the Basque nation toward science, letters and fine arts, to banish idleness, ignorance and their fatal consequences and to tighten more the union of those Basque provinces of Alava, Guipuzcoa and Vizcaya." This was the first time the term Basque Nation was used.

In 1876, the foral law was overturned. One result was to end Vizcaya's prohibition on the extraction and export of provincial natural resources. British capital flooded in to exploit the iron deposits and to build ships and railroads. Iron exports soared. In 1876, one half million tons of iron was exported to Britain. The next year this jumped to 1 million tons. By 1899 iron exports totalled 6.5 million tons. Eighty percent was destined for the British market. Between 1874 and 1914, 180 million tons of iron ore were imported by Great Britain; almost 130 million came from Vizcaya.<sup>20</sup>

The major coastal cities of Bilbao and San Sebastian experienced dramatic industrialization. The area became Spain's center of steel making and metal processing. The 1929 Encyclopedia Britannica noted the "swords of Mondragón were renowned before those of Toledo".

Today the Basques are one of the world's top 12 producers of machine tools. They make nearly 80 percent of Spanish machine tools.<sup>21</sup> One reporter recently described the Basques as, "The only people in Spain historically capable of making capital goods with their own resources".<sup>22</sup>

In 1943, one historian commented, "The Basques, with their large industrial capital at Bilbao, their mercantile marine and their active commercial relations with foreign countries, are the most European of all Iberian races. Though

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<sup>17</sup> Whyte and Whyte. Op. Cit.

<sup>18</sup> Except for Navarra, a Basque southern plains province that relied on cattle and farming and remained isolated from most of the commercial endeavors of the coastal provinces.

<sup>19</sup> The Bessemer steel making process depended on low phosphorus iron, which was in short supply in England.

<sup>20</sup> Clark, Op. Cit.

<sup>21</sup> Financial Times. November 30, 1989

<sup>22</sup> Ibid.

conservative in a political sense, their conservatism is that of an active commercial race such as the English, which believes in individual effort."<sup>23</sup>

Almost 50 years later, *Financial Times* reporter Peter Bruce reinforced this sentiment. "The Basques are almost comically industrious", he remarked.<sup>24</sup> "Working with one's hands in industry or commerce is not looked down on in the Basque country as it is in some other regions of Spain", comment the Whytes.<sup>25</sup>

There are 10,000 or more manufacturing companies in the Basque country.

Although separated from the rest of Europe by high mountains, the Basque Country has excellent transportation networks. The Basque region has Spain's best road network. Bilbao is Spain's biggest port.

### **Basque Country as Proportion of Spanish Economy**

(1988)<sup>26</sup>

<b>Category</b>	<b>Percentage</b>
Population	7.0
Total Value added	10.5
Machinery and Equipment	22.1
Primary Metal Production	32.4
Metal Products	27.7
Rubber and Plastics	22.3
Paper	11.1

The Basque region of Spain contains about 2.3 million people. In 1989, its working population was 710,000.

In the early 1970s, the Basque provinces had 7 percent of the Spanish population, 25-33 percent of Spain's weapons manufacturing capacity, more than 17 percent of its bank accounts, and one third of its shipyards and shipping lines. The Basque provinces contribute 13 percent of Spain's taxes.<sup>27</sup>

### **Employment by Sector**

(%, 1986)<sup>28</sup>

<b>Region</b>	<b>Agriculture</b>	<b>Industry</b>	<b>Services</b>
Spain	16.1	24.3	51.9
Basque	4.9	37.2	51.9
Alava	9.6	41.9	42.6
Guipuzcoa	4.1	48.0	47.3
Vizcaya	4.3	32.4	57.0

<sup>23</sup> Cited in Morrison, *Op. Cit.*

<sup>24</sup> *Financial Times*. November 30, 1989. Peter Bruce is the journalist.

<sup>25</sup> Whyte and Whyte, *Op. Cit.*

<sup>26</sup> *Financial Times*. November 30, 1989

<sup>27</sup> *Ibid.*

<sup>28</sup> *Financial Times*. November 30, 1989.

In 1979 Guipuzcoa, Vizcaya and Alava ranked 1,2,3 in per capita income and Navarra ranked 7th among the 50 Spanish provinces in the late 1960s.<sup>29</sup>

The Basques are also distinguished by their willingness to fight for their values and their autonomy. The Basques have a long tradition of relying on their own resources when faced with an external threat. "The inclination of the (Basque) culture to cut itself off from all that is foreign, to turn inward when threatened and to derive the strength to resist from inner forces...."<sup>30</sup>

When the Asturias miners raised the flag of workers revolution at Oviedo in October 1934, the only armed contingent that marched to their support from outside the region came from Mondragón.<sup>31</sup> When the military under Francisco Franco rose up against the democratic Republic in the 1930s, most of the Basque region fought on the side of the Republic.<sup>32</sup> This included much of the Catholic Church structure, despite the Church's support of Franco in the rest of Spain.

The Spanish Civil War lasted until 1939. Bilbao, the final Basque outpost, fell in June 1937. Mondragón was overrun some months earlier.

During most of the Franco years, all public meetings were prohibited except those specifically approved by government. A few months after Franco's victory, he removed priests and higher Church officials not considered loyal. Basque Archbishop Matéo Mugica was deported. His successor, Archbishop Francisco Javier Lauzurica y Torralba publicly stated, "I am one more general under orders from the Generalissimo to smash(Basque) nationalism".<sup>33</sup>

If children were caught speaking Euskera, their parents were subject to financial penalties and often became subject to police surveillance. Only in 1968 did it become legal to speak Euskera and to publish in that language.

The Basque sense of separatism and nationalism has permeated many of its institutions. The region has a higher rate of unionization than the rest of Spain. In 1986, the conservative, nationalist union ELA-STV won almost as many votes as the two big national unions, the socialist UGT and the communist CCOO combined, in elections of union representatives to company workers' councils.

Over half of the parliamentary vote in 1979 went to two Basque political parties that represented Basque ethnicity and nationalism.

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<sup>29</sup> Clark, *Op. Cit.*

<sup>30</sup> Clark, *Op. Cit.*

<sup>31</sup> Three Mondragón battalions fought on the Republic side; one socialist, one nationalist, one made up of less directly affiliated "volunteers". Robert Oakeshott, "A Cooperative Sector in a Mixed Economy", in Alasdair Clayre(ed) The Political Economy of Cooperation and Participation: A Third Sector. Oxford University Press. Oxford. 1980.

<sup>32</sup> In the 1930s, the new Republic's Constitution made autonomy a right for all regions of Spain. The Basques drafted a Statute of Autonomy that made Euskera the official language. This was declared unconstitutional. Autonomy was not to come to the Basque region until the new Spanish Constitution was established in 1978 after the death of Franco.

<sup>33</sup> Whyte and Whyte, *Op. Cit.*

The Basque nationalist group, ETA Euskadi Ta Askatasuna (Basque Homeland and Liberty) was created on August 31, 1959. In the mid 1960s the group debated whether they would focus on national autonomy or pursue the internal revolutionary changes that were being pursued in Algeria, Cuba and Vietnam. They chose to emphasize Basque autonomy first. They embraced armed struggle as their strategy.

The Basque language is still extant. The numbers of people who speak or read it varies sharply by province. Only 10 percent of the population of Alava, for example, speak Basque. About 50 percent of the population of Guipuzcoa still understand Basque, perhaps as a result of the Mondragón Cooperative, which operates Basque language schools and uses Basque as the official language of the Cooperative.

### **Don José María Arizmendiarieta**

"The Mondragón phenomenon is only explainable as a result of the presence of someone with a capacity for teaching, and sufficient moral authority to instruct and involve the whole community".

Jesus Larrañaga

Don José María Arizmendiarieta<sup>34</sup> was born in 1915, in the village of Markina, about 30 miles from Mondragón. He was the eldest son of a farming family of modest means. In 1936 he was studying to enter the priesthood when the Spanish Civil War broke out. Since Arizmendi lost his left eye in childhood, he was unable to serve in the Republican army. Instead he promoted the Republican cause by writing for and editing newspapers written in Euskera. Near the end of the war he was imprisoned and was to have been executed, but eventually was freed.

During the Civil War, Franco's troops executed fourteen Basque priests, including Father Joaquin Arin, the priest of the little steel town of Mondragón.

Arizmendi returned to Vitoria to finish his studies for the priesthood. He wanted to study sociology in Belgium but the Church assigned him to Mondragón. He arrived on February 5, 1941.

When Arizmendi arrived in Mondragón, he found a city of 8,500, nestled in a valley, with poor roads and difficult access. It was an unappealing site for a major industrial complex. It was a community suffering profound problems: families with men in jail, hunger, bitterness.

Arizmendi was given the task of helping youth. "My concrete mission was to be the counselor and adviser of your working people", he later wrote.

Arizmendi was not a charismatic figure. "He spoke in a monotone with intricate and repetitive phraseology difficult to understand", recalls one of his students who later became one of the founders of the Mondragón experiment.

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<sup>34</sup> In this paper, consistent with many of the writings about this guiding spirit of Mondragón, I will use interchangeably his full name or Don José María or Arizmendi.

"Away with this priest that the Monsignor has imposed upon us. He hardly even reads with grace! That was the first reaction of the faithful".<sup>35</sup>

Arizmendi's skill was in his strategic vision, his patience, and his extraordinary aptitude for personal dialogue. His philosophy was a mixture of Robert Owen's and Rochdale's cooperativism, Karl Marx's class analysis and emphasis on the role of capital, and the Church's focus on the dignity and primacy of labor. To Arizmendi, cooperation, work, and education were the three foundations of a just society.

"One is not born a cooperator, because to be a cooperator requires social maturity, a training in social coexistence", he wrote. "One becomes a cooperator through education and the practice of virtue."<sup>36</sup> "People do not normally become co-operators spontaneously, they have to be taught--the soil may be fertile but it has to be cultivated."<sup>37</sup>

Education was the key. "Knowledge is power...socializing knowledge implies the democratization of power."<sup>38</sup>

In both education and cooperation, labor was to have the primary role. Founder José María Oramachea remembered that a key lesson of Don José María was the necessity of changing the sovereignty of capital to the sovereignty of labor".<sup>39</sup>

Arizmendi believed in the sovereignty of labor, but he also viewed capital an essential tool for development, and profits as an excellent measure of efficiency.

"To build cooperativism is not to do the opposite of capitalism", Arizmendi wrote, "as if this system did not have any useful features...Cooperativism must surpass it, and for this purpose must assimilate its methods and dynamism..."<sup>40</sup>

Arizmendi's greatest skill was in challenging people to do more than they thought they could while supporting their current efforts. He engaged the community in an almost continuous personal dialogue. By 1956 he had conducted over 2000 small group discussions, a study session every 2.7 days, in addition to his regular teaching schedule.<sup>41</sup>

Don José María was a teacher who believed fervently in action. One of his former students remembered a situation in which Arizmendi was talking about "distributive justice". The students continued to pepper him with clarifying questions until finally he said, "Look, whether you understand me well or not, what are we going to do? At some point you will act."<sup>42</sup>

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<sup>35</sup> Jesus Larrañaga, El Consejo Social: Pasado, Presente y Futuro. Caja Laboral Popular. Mondragón. 1986.

<sup>36</sup> Roy Morrison, Op. Cit.

<sup>37</sup> Cited in Wiener and Oakeshott, Op. Cit.

<sup>38</sup> Cited by Charles W. Sperry, "What Makes Mondragón Work?", Review of Social Economy. December, 1985.

<sup>39</sup> Ibid.

<sup>40</sup> Ibid

<sup>41</sup> Whyte and Whyte, Op. Cit.

<sup>42</sup> Trabajo y Union. November, 1986.

Arizmendi insisted on thorough research, careful planning and sound business practices. "There is a need to study the concrete realities of one's own town and neighborhoods and to define problems or projects which can be solved or undertaken", he said in a 1945 speech to youth leaders. "Once one has identified a line in which a production activity can be undertaken, one has to study the production, marketing etc. of that specific product, because every productive activity has its own difficulties that one needs to master step-by-step. But all the time, while one is almost completely absorbed by such practical problems, one should have a utopian vision through which one can then adjust projections and plans."<sup>43</sup>

Arizmendi guided the Mondragón Cooperative experiment until his death in 1976. He never held official office. He "studiously avoided participating in official meetings of any of the organs of cooperative governance". Instead he "shared information and ideas in informal individual or group discussions".<sup>44</sup>

## **Education, Manufacturing, Banking: The Three Foundations to Mondragón**

### **Education**

"Education is the heart and soul of the Mondragón experiment"<sup>45</sup>

If Don José María were only a great teacher, the Mondragón experiment would not have happened. He was also a gifted entrepreneur. He created new organizational forms, identified individuals who could undertake and manage projects. And sometimes, when persuasion failed, simply went it alone and presented his followers with a fait accompli.

In 1943 Mondragón had only primary schools. No son of a Mondragón worker had ever attended a university. The apprenticeship program at the largest local company, a steel works called Unión Cerrajera, was limited to the sons of employees and 12 outsiders, which amounted only to 15 percent of the eligible youth in area. Arizmendi taught religious instruction at the company.

When he asked Unión Cerrajera to expand its apprenticeship program, the company refused. He then decided to start a school.

The way in which he went about this task illustrated his gift for organizing.

Initially Don José María had organized through Acción Católica, a local Catholic association. But he decided to make his first project an organized sporting activity. Because of legal and bureaucratic constraints, he went outside

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<sup>43</sup> Henk Thomas and Chris Logan, Mondragón: An Economic Analysis. George Allen & Unwin. London. 1982.

<sup>44</sup> Whyte and Whyte, Op. Cit.

<sup>45</sup> Christopher B. Meek and Warner P. Woodworth, "Technical Training and Enterprise: Mondragón's Educational System and Its Implications for Other Cooperatives". Economic and Industrial Democracy. Vol. II. 1990 pp. 505-528.

the Catholic Church and established the Juventud Deportiva de Mondragón. The new association also raised funds for a school and purchased and operate a local movie theatre.

When Arizmendi asked José María Zubia to help build a new school by raising funds to build a soccer field, "I protested, telling Don José María that we needed a school, not a soccer field, and he answered me saying, 'Do you not understand, dummy? If we do not promote soccer we will never build a school'. That was all; even though I did not understand clearly why we had to promote soccer, I helped in the organization...the next year we inaugurated a new soccer field and in October the Technical School was inaugurated."<sup>46</sup>

In his campaign to start a school, Arizmendi had volunteers place ballot boxes on street corners. Members of the community were invited to drop pieces of paper inside, indicating whether they would support a new technical school with cash or labor. When the boxes were emptied, six hundred positive responses were found, 25 percent of the town's households.

The new school opened December 1943, with an enrollment of 20. The school was not a cooperative when it first opened, but a private technical school affiliated with Acción Católica, a social service agency formed at the end of the Civil War.

The school's close ties to the Church rendered it ineligible for government support from the Ministry of Education. Arizmendi searched for a legal framework that would allow the school to be independent of the Church and would allow for a cooperative organizational structure. He found one in an obscure 19th century statute that allowed private citizens to form "leagues" or "associations for education and culture". In 1948 the school was reorganized and named the Liga de Educación y Cultura. Don José María became Associate Consulting Dean. The school was recognized by the Spanish government and qualified for modest state financing.

The school's General Assembly had ultimate authority. It consisted of representatives of four constituencies: individuals with a desire to join; active members who paid dues or served as teachers; sponsors and firms who gave annual contributions of at least 1000 pesetas(about \$89 in 1948); and honorary members who were local government officials.<sup>47</sup> Each of these constituencies had the right to elect 10 representatives to the General Assembly. The General Assembly elected a 14 member Board of Directors.<sup>48</sup>

The school added a new level as soon as its students completed a previous one and thus expanded from a junior high school to a high school and then to an institution offering instruction comparable to the first three years of a U.S. undergraduate degree. In order to allow the students to achieve a full

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<sup>46</sup> Meek and Woodworth, *Op. Cit.*

<sup>47</sup> This last category was required by the legal statute. The school's charter required that 6 of the members of the Board be representatives from donor enterprises and that one member be the town mayor.

<sup>48</sup> Today, EPP's General Assembly had three constituencies: teachers; pupils and parents; and supporting institutions.

engineering degree, Arizmendi worked out an arrangement with the University of Zaragoza whereby students from Mondragón could study at night. Eleven of the 20 members of the technical school's first entering class went on to pass the engineering examination in 1952. These men continued to meet with Arizmendi every week for discussions.

By 1952 school enrollment was 170. A new building was needed. Arizmendi insisted that the new building be large enough to accommodate 1000 students, a seemingly unfillable capacity. After much persuasion, the community agreed. In 1953 the school was renamed the Escuela Profesional Politécnica(EPP).

EPP passed the 1000 student mark in the 1960s and by 1976 had 2,000 students. That year it became an accredited polytechnic institute. "Today the EPP is considered one of Spain's most prestigious educational centres and its graduates are among the most sought after and highest paid in industry."<sup>49</sup>

Don José María believed that the best way to teach cooperative values was to have students work in a factory while attending school. It also provide them an income to pay for school expenses and, if they were away from home, for board and lodging. In 1965 he persuaded EPP to establish Alecoop. Recalls Laurentino Gomez, former general manager of Alecoop, "Don José María used the same technique he used in other projects. First he had an idea, which he researched, refined and discussed with other people....But his contribution was also having the social statutes ready to avoid further delays in the Ministry of Labor"<sup>50</sup>

Alecoop was created in early 1966 as a "trabajo asociado". Its board represented three interests: student workers, teachers, and representatives from industrial coops who contributed money and advice. The EPP launched the new coop with a loan that was repaid within six months.<sup>51</sup> Students worked five hours a day, and studied five hours a day. Although students were not forced to work, about 50 percent of the student body worked in Alecoop during their time at EPP.

Alecoop charged customers on a cost basis, at 90 percent of the customers own members hourly rates.

By 1990, Alecoop had 601 students and 33 faculty. Sales in 1988 were \$9.2 million.<sup>52</sup>

Don José María was a fervent believer in the importance of technology and technological development as a key to a society's well-being and the Cooperative's competitiveness. In 1968, EPP relieved some of its faculty of their teaching responsibilities and established a research department. By 1972 EPP had its first automation lab. In 1974 Don José María, again in the face of serious reservations, persuaded the cooperatives to invest \$2 million for new offices,

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<sup>49</sup> Meek and Woodworth, *Op. Cit.* In 1971 Unión Cerrejera closed its apprenticeship school and began making contributions to the EPP.

<sup>50</sup> *Ibid.*

<sup>51</sup> *Ibid.*

<sup>52</sup> *Ibid.*

labs, and machine shops. In 1977, Ikerlan, the cooperative's central research and development center, opened its doors.

In 1984, Mondragón established Ikasbide, a School of Business Administration. It also established an Institute of Industrial Design. The Otorora training center offers management planning courses for members of the governing councils and the social councils.<sup>53</sup> In 1990, Mondragón offered the first master's program in cooperative management.

Continuing education is widespread within the Cooperative system. In 1987 its largest industrial group, FAGOR reported that 2,010 or 30 percent of its 6,602 workers were taking a technical or professional training courses. These courses lasted an average of almost 57 hours per person. The cost to FAGOR was \$2 million.

Today Mondragón's cooperative education system is comprehensive. The Educational Group coordinates educational cooperatives and associated institutes and training programs in the region around Mondragón. There are over 6,500 students in degree programs and 3,500 students in other types of training courses. The Ikastolas are Basque language primary schools. More than 40 of them are associated with the Mondragón system.<sup>54</sup>

## Manufacturing

Five of the original 11 graduates of the EPP went to work in Unión Cerrajera in 1952. When the firm decided to expand by selling new stock, Don José María's disciples asked top management to allow workers to invest in firm. Management refused. The five then travelled to Madrid to propose a federally sponsored program through which workers could gain shares in ownership. Again, they were rejected. They then decided to start a new company.

The five men, Usatorre, Larranaga, Gorrongoitia, Ormaechea and Ortubay, created a 'blind pool' of capital from the community's resources. They used 'chiquiteo', the Basque tradition of wandering with a group of friends from bar to bar after work to inform the townspeople about their plans.<sup>55</sup>

"With nothing more to go on than the personal promises of these men, about a hundred people in the community responded with pledges, basically as an expression of faith in the five pioneers and the guiding hand of Don José María. Including the commitments of the five founders, 11 million pesetas (\$361,604 in 1955 dollars) was pledged--an enormous sum at this time in a working-class community of Spain."<sup>56</sup>

In 1955 the five purchased a private firm in Vitoria that had gone bankrupt. They did this for two reasons. One was to avoid having to request a permit for a new manufacturing plant to a Madrid bureaucracy hostile to Basques. The second was to obtain the firm's broad license authorizing it to produce a line of

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<sup>53</sup> See below for discussion of the governance structures of Mondragón's cooperatives.

<sup>54</sup> Morrison, *Op. Cit.*

<sup>55</sup> Meek and Woodworth, *Op. Cit.*

<sup>56</sup> Whyte and Whyte, *Op. Cit.*

electrical and mechanical home appliances. The firm was renamed ULGOR, after the initials of the five founding members. ULGOR was housed in a Vitoria facility but on November 12, 1956, the firm moved into Mondragón. That date is considered the formal founding of the Mondragón experiment. Yet as Larrañaga later recalled, "There was no ambitious and well-considered project; what we needed was to start something, to wake up and to see what would be the outcome."<sup>57</sup>

ULGOR started with 24 employees and manufactured an Aladdin space heating stove. Demand proved strong and soon ULGOR was designing its own stoves. It bought an existing foundry and casting shop to free itself from outside suppliers.<sup>58</sup> ULGOR manufactured a line of electrical equipment under a foreign license, and built a new factory to produce butane cookers under the brand name, Fagor. By the end of 1958, ULGOR had 149 employees.

ULGOR's early success encouraged similar cooperative efforts in Mondragón and nearby towns. In the late 1950s Arrasate began by producing lawn mower parts in Mondragón, and would eventually become one of Spain's leading machine tool manufacturers. Comet, a steel foundry formed from two existing capitalist firms in Guipuzcoa. Funcor was a cooperative foundry in Vizcaya; Ochandiano Talleres, a cooperative manufacturer of food handling equipment. A retail cooperative store was also founded.<sup>59</sup>

Until 1959 none of these cooperatives had a fully developed organizational and legal structure. ULGOR functioned for more than three years without a legal constitution or bylaws. As Larrañaga explained, "At that time we didn't even know what a cooperative's legal form would look like. So we accepted the form of a joint stock company, but tried to operate the best we could on the basis of democratic principles."<sup>60</sup>

ULGOR's founders and Don José María had studied the 1942 Spanish law on cooperatives and found it inadequate for their purpose. So these companies operated informally along democratic lines on the basis of one worker, one vote.<sup>61</sup>

The Franco government offered cooperatives assistance.<sup>62</sup> All cooperatives came under the jurisdiction of one government agency, Obra de Cooperación. Arizmendi went to Madrid and met José Luís del Arco, an adviser in the agency. Arco later remembered, "Padre Arizmendi came to consult me on problems for which his reading of the text of the law did not provide any solution. I gave him

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<sup>57</sup> Thomas and Logan, *Op. Cit.*

<sup>58</sup> Roy Morrison, *Op. Cit.*

<sup>59</sup> *Ibid.*

<sup>60</sup> Meek and Woodworth, *Op. Cit.* There is some confusion in the literature about exactly how the voting process was structured in the early days. Oakeshott says that initially, the Ulgor general assembly provided for weighted voting. Morrison states that it was one man, one vote from the beginning.

<sup>61</sup> *Ibid.*

<sup>62</sup> See below for a discussion of the impact of Spain's legal and tax law on the Mondragón Cooperative.

the answers, because the letter of the law is one thing, and the spirit of the law is that which can bring the letter of the law to life."<sup>63</sup>

In 1959, with the assistance of experts like José Luís del Arco, Arizmendi fashioned the Cooperative's first bylaws and social statutes. These were adopted by ULGOR and became the model for all other cooperatives. "From the beginning", he said years later, "we bore in mind the needs of a modern enterprise, and a formula was adopted which would make its development viable from all points of view: economic, technical, social and financial; not as a second rate entity suitable for only a limited field of activity, but one which would be appropriate across a wide sector of the economy."<sup>64</sup>

Arizmendi developed five guiding principles to provide a framework for the bylaws and social statutes: solidarity; individual economic contributions; labor contribution by all members; democratic government; progressive expansion to incorporate other workers. The balancing of the needs of capital and of labor that have been a major preoccupation of the Mondragón Cooperative is clearly illustrated in this first "constitution" of the cooperative system. Article 1 of the Internal Regulations of ULGOR declared, "Manual labor should enjoy the prerogatives inherent in its dignity in all productive processes." The first chapter of ULGOR's Fundamental Guidelines just as specifically insists on the need for a "just reward" for capital.

By the late 1960s ULGOR was the leading Spanish producer of refrigerators. By the mid 1970s ULGOR had 3,500 worker-owners and was the engine that drove the Cooperative's economic development, both as an internal market for the products of new cooperatives, and as a source of capital for further economic expansion through its surplus.

Cooperatives formed to supply ULGOR and then began to upgrade their technical capacity and reduce costs. Finally, they began manufacturing for outside buyers. Arrasate moved into sophisticated mechanical presses, shears, transversal and longitudinal cutters. Copreci, formed in 1963 to make measurement and control instruments such as thermostats, valves and programmers for domestic appliances initially sold nearly all of its output to ULGOR. By the 1980s it was selling only 20 percent to ULGOR, and was exporting a substantial percentage of its output to European markets.<sup>65</sup> In the 1980s Copreci spun off a new coop, Orkli, to make control valves for gas appliances.

The Community created about 800 jobs per year from 1961 to 1976. By 1976 it had 57 industrial cooperatives(excluding housing, agricultural, consumer, educational and financial cooperatives) with over 13,000 worker owners. By 1976 the average cooperative had over 200 workers, a figure that rose slightly by 1988.<sup>66</sup>

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<sup>63</sup> Whyte and Whyte, Op. Cit.

<sup>64</sup> Roy Morrison, Op. Cit.

<sup>65</sup> Whyte and Whyte, Op. Cit.

<sup>66</sup> Avner Ben Ner, "Comparative Empirical Observations on Worker Owned and Capitalist Firms". Journal of Economic Behavior and Organization. 6:7-31. 1988.

## Banking and Finance

In 1958, with several industrial cooperatives, the rapidly growing economic might of ULGOR and several hundred workers in the cooperative system, Arizmendi urged members to establish a workers bank. He viewed a bank as a means to achieve three important ends: to overcome the single biggest barrier to cooperative growth--lack of access to large source of capital on reasonable terms; to provide the technical expertise needed to assist the budding cooperatives; to establish a social security system for the Cooperative Group.

Arizmendi discovered that an institution registered as a workers credit cooperative legally could pay a higher interest rate on deposits than other banks.<sup>67</sup> Thus the bank he proposed could attract local savings to finance cooperative expansion. Arizmendi was firmly convinced that a bank was essential for the Cooperative's survival and for local job creation. As he said, "Libreta o maleta"(a savings book or a suitcase; savings or migration).

Establishing a bank represented an enormous leap of faith and Don José María encountered strong reluctance from his former students who felt he was pushing them too far too fast. "We told him, yesterday we were craftsmen, foremen and engineers. Today we are learning how to be managers and executives. Tomorrow you want us to become bankers. That is impossible."<sup>68</sup>

Unsuccessful at persuading his associates, Arizmendi decided to go ahead without their permission. He prepared the bank's constitution and bylaws in consultation with José Luis del Arco. Then he fabricated the minutes of a purported meeting of the bank's founders, forged the signatures of Gorrongoitia and Ormaechea, and presented them with a *fait accompli*.

The Spanish Government recognized the Caja Laboral Popular(CLP), the Bank of the People's Labor, in July 1959. Two branches of the bank were established that year, one in Mondragón and one in Elorrio in Vizcaya.<sup>69</sup>

To head up the bank, Arizmendi wanted someone with connections to banking circles who possessed of an image of respectability and security. He turned to José Ayala, who in 1943 had been the first president of the youth sports club in Mondragón and had married a woman from a well-to-do local family. José Ayala had a good job with local company but Arizmendi persuaded him to launch the bank.

Arizmendi thought Ayala essential for establishing the right image for the bank but to manage the bank's entrepreneurial growth phase he persuaded Ormaechea, then head of manufacturing at ULGOR, to become CLP's chief executive. In May 1961, Arizmendi persuaded Gorrongoitia to chair the

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<sup>67</sup>Whyte and White, *Op. Cit.*

<sup>68</sup>Ana Guiterrez-Johnson and William Foote Whyte, "The Mondragón System of Worker Production Cooperatives", *Industrial and Labor Relations Review*. 31, no. 1. October, 1977.

<sup>69</sup> The reason for establishing two branches in two provinces was in case one province decided to revoke the license.

Governing Council of the Bank and later to become President. A month later Usatorre and Larrañaga joined the Council.<sup>70</sup>

For much of the Mondragón Cooperative's history, the CLP would be the hub of the Community, the glue that tied it together, and the managerial engine that drove its development.

The CLP was viewed as a cooperative whose primary mission was to serve other cooperatives. Therefore, its governance structure was divided between representatives of its own work force, the only owners represented in the other base cooperatives, and representatives of the work force of its customers, the associated cooperatives.<sup>71</sup> CLP heeds two voices.

The CLP established the basic rules of the Cooperative. Every associated cooperative signed a Contract of Association with the CLP that sets forth its responsibilities. Above all is its responsibility to think cooperatively. "The Associated Cooperative will respect the principles of intergroup loyalty and mutual assistance when formulating future plans...", one Article states.

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<sup>70</sup> The fifth founder, Ortubay had left Mondragón to found a private business in Vitoria.

<sup>71</sup> The individual depositor in the CLP does not have representation. CLP holds general depositor meetings on a regional basis. These meetings give depositors a voice, but not a vote, in company policy. See below for discussion of the Community's structure.

Member cooperatives are required to deposit their funds in the CLP. Article 31 of the section dealing with Economic Relations, for example, states that the capital of an associated coop shall be made available to CLP. "Hence, the member coop surrenders not only some degree of autonomy on association, but also is required to transfer equity."<sup>72</sup>

For most of the Cooperative's history, the CLP was restricted to financing cooperative members. In practice, the CLP offered cooperatives their only access to capital outside of their own members and also provided a mechanism for diversifying risk. Loans from the CLP comprised about 50 percent of the associated cooperatives' capital. And until the late 1970s the majority of CLP's funds were tied up in cooperatives. This gave the CLP a powerful weapon and attractive carrot to keep cooperatives within the system. Cooperatives in serious violation of the Contract of Association can be cut off from capital or expelled from the Cooperative.

Cooperative members received loans and other financial services at a low cost. Loans might be discounted below prevailing market rates to conventional firms. The CLP was able to do this because its administrative costs were lower, given lower management salaries, and also because its cost of capital was low, given that all cooperatives had to do their banking with CLP. Also, its lending costs were low because its entrepreneurial division closely monitored the economic condition of all its members. The CLP had no need to attract private and institutional shareholders nor to handle dividend payments.

From the very beginning, the CLP was an outstanding success. In 1966 it had 21,653 savings accounts. By 1975 it had 190,000 savings accounts and about 4 percent of the total workforce of the cooperative community. In the mid 1970s, a CLP staff analysis showed the Bank outperforming all conventional savings banks in the 10 years up to 1975.<sup>73</sup>

From 1977 to 1983, the inflation adjusted value of the CLP's deposits rose by 67 percent, far outpacing the growth of deposits in most financial institutions.<sup>74</sup> By 1979 CLP held 13 percent of total deposits in all banks in Guipuzcoa.<sup>75</sup> By the early 1980s the CLP was the 26th largest banking institution in Spain.

For much of the Cooperative's history, the CLP acted like the head office of a private holding company. CLP's Management Service Division was charged with promoting "cooperativism" throughout the region.<sup>76</sup> In 1969, with 46 associated cooperatives and nearly 8,000 members, the managerial activities of the CLP became a separate division, the División Empresarial.

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<sup>72</sup> Thomas and Logan, *Op. Cit.*

<sup>73</sup> Oakeshott, *Op. Cit.*

<sup>74</sup> Keith Bradley and Alan Gelb, "Cooperative Labour Relations". *British Journal of Industrial Relations*. 25: 77-97. 1987.

<sup>75</sup> Thomas and Logan, *Op. Cit.*

<sup>76</sup> David I. Levine, "Participation, Productivity and the Firm's Environment". *California Management Review*. Summer, 1990.

At no cost, the CLP provided a comprehensive audit of each base cooperative's affairs every 4 years. Upon request and for a fee, it would audit the cooperative more frequently.

Each enterprise had to provide the CLP with monthly financial reports. At the same time, there was a reciprocal exchange of information from the CLP to the enterprise.

In the early days of the Cooperative, the CLP largely responded to groups who approached it with a project. By the mid 1970s, the entrepreneurial division had developed a bank of pre-feasibility studies which were often used to guide cooperators.

The CLP began its assessment of a venture by selecting one of the individual entrepreneurs to be manager and paid him<sup>77</sup> a salary and made him a member of the feasibility team. This often meant visiting similar factories in Spain or Europe to learn the state of the art. CLP funded the feasibility study and provided 60 percent of the initial costs. Twenty percent came from the Spanish government's job creation program<sup>78</sup>, and 20 percent from the founding cooperators. The CLP underwrote any operating deficits for the ventures' first two years. All these costs were charged against the new cooperative's account for later repayment.

One CLP staff member was designated the new enterprise's "godfather" and normally attended all meetings of the Board of Directors of the new cooperative for the first year.

David Ellerman calls this process "social entrepreneurship" and described the abundant technical and managerial resources at the entrepreneurs' disposal.

"For details of the marketing part of the study the promoter can consult the Marketing Department. To explore export possibilities there is the Export Department, to plan out the production process there is the Production Department, and to design an appropriate factory for the manufacturing process, there is the Industrial Building Department. For information about the personnel system and member payment arrangements there is the Personnel Department. The Legal Department handles the incorporation procedures, obtaining the necessary licenses and patents and drafting the necessary contracts. The Auditing Department and Information and Control Department help to set up the accounting and management control systems so that the progress of the cooperatives can be monitored by the manager and the CLP."<sup>79</sup>

In the early 1980s, Ellerman estimated that, although the CLP required new firms to repay the costs of start up advanced by the bank, these repayments covered less than half the actual cost of the loans, given the large overhead of

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<sup>77</sup> The vast proportion of managers were men.

<sup>78</sup> State funds were loaned at a 3 percent interest rate and maximum repayment of 10 years. Oakeshott, *The Case for Workers' Co-ops*.

<sup>79</sup> David P. Ellerman, "Entrepreneurship in the Mondragón Cooperatives", [Review of Social Economy](#). December, 1984. See also David P. Ellerman, "The Mondragón Cooperative Movement", Harvard Business School case no. 1-384-270. Harvard Business School. Boston. 1984.

the CLP in engaging in ongoing research. The CLP recovered much of this subsidy by serving as the bank for the new firms.

The start up of Aneko, a manufacturer of seed drills, illuminates the process. Feasibility studies were jointly financed by CLP, the founders' own cooperatives and the founders themselves. Of the initial capital, 15 percent came from the founders and 15 percent from their respective cooperatives, which would acquire an interest in the new venture. CLP provided 60 percent of the funds at below market interest rate of 8 percent (the then going market rate was 15 percent). During the formative period members could pay salaries no higher than 85 percent of CLP's pay scale. About half of those joining the new cooperatives were to be from the existing cooperatives of the associated cooperative group. For the first three years the venture used the facilities of the existing cooperatives on contract, with the major investment in plant occurring only after the product's suitability was proven.

### **Social Security**

In October 1959, within months of formally registering as a bank, the CLP began to provide a social security service. At the time, cooperative members were considered self-employed and were ineligible for Spain's social security. At the end of 1966, the social security wing of the CLP, Lagun Aro began offering its services. In 1967 cooperatives were allowed to participate in a new Spanish system for self-employed workers, Mutualidades de Trabajadores Autónomos. In 1969 Lagun Aro registered as a separate but complementary fund with MA, but operated under its own rules.<sup>80</sup>

Lagun Aro, at first a division of the CLP, became an independent cooperative and later spun off its own sister cooperative, Seguros Aro. The two offer many types of insurance, from auto to home, life, business, accident and unemployment insurance. They also offer family allowances and death benefits, pensions and health care.

Until the late 1980s, when the Basque government assumed most of its financing, the Community operated its own health system. It controlled medical costs by establishing a set of norms--for absenteeism, sickness, use of medical facilities, etc.. Lagun Aro kept detailed sickness and accident statistics and calculated annual budgets for the cooperatives and Groups. If a cooperative or Group overspent its budget by more than 10 percent, it paid a surcharge. If it underspent it got back half of the system's savings. If the Community as a whole exceeded its norms, the norms were raised the next year.

The Community's social security system is fully funded.<sup>81</sup> The Community's pension averages 60 percent of final earnings, whereas the Spanish pension system averages 40 percent.

In 1990 Lagun Aro had 19,067 members from 134 cooperatives.

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<sup>80</sup> Cooperative members participate in MA on a "minimal" involvement basis in part because obtaining a comparable level of benefits from the national system would be 1.75 times as expensive as the current arrangement.

<sup>81</sup> Bradley and Gelb, Op. Cit.

## **The Three Stages of Development: Rapid Growth; Recession; The Single Europe Market**

The Mondragón cooperative system has experienced three distinct stages in its development. Each stage was characterized by the external economic environment in which the Cooperative Group found itself. The first stage, from 1956 to 1976, was one of national and European prosperity. The second, from 1977-1988 was one of regional depression, violence and restructuring. The third, from 1988 to the present, is one of increasing continental wide economic integration as well as a persistent slowdown in European as well as Spanish economies. This section describes the period of rapid growth and recession. At the end of this report is a major section on recent developments in Mondragón as a result of the European Union.

### **Rapid Growth: 1976-1976**

The Mondragón cooperative system had its birth and growth pangs during a period of unprecedented economic growth in Spain. From 1956 to 1976, Spain and its Basque provinces experienced rapid economic growth. Sheltered by protective tariffs, subsidized by targeted federal industrial development programs, the Spanish economy boomed. The Mondragón cooperative system blossomed. By 1976, the cooperative system had 57 industrial enterprises with more than 13,000 employees.

During this time ULGOR remained the economic motor for the entire industrial community, accounting for about 40 percent of total sales. ULGOR was the principal source of capital, funneled through the CLP, for industrial expansion. Export sales were modest. From 1969 to 1975 export sales fluctuated from 10 to 15 percent of total industrial sales.

#### **Industrial Cooperatives Started<sup>82</sup>**

(1961-1976)

<b>Year</b>	<b>Number</b>	<b>Year</b>	<b>Number</b>
1961	4	1969	3
1962	6	1970	0
1963	11	1971	2
1964	3	1972	1
1965	4	1973	3
1966	4	1974	7
1967	4	1975	1
1968	1	1976	2

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<sup>82</sup> Robert Oakeshott, The Case for Worker Cooperatives. Routledge and Kegan Paul. London. 1978.

**Sectoral Breakdown of Industrial Cooperatives**<sup>83</sup>  
(1976)

<b><u>Sector</u></b>	<b><u>Number</u></b>	<b><u>Employees</u></b>
Foundries and forges	6	1,809
Capital Goods	14	2,684
Consumer Durables and Furniture	9	4,324
<u>Intermediate Goods and Components</u>	<u>23</u>	<u>3,483</u>
Total	57	13,537

### **Coping with Recession**

The oil price hike of 1973 and the second oil shock of 1979, combined with the world wide recession of the early 1980s, shocked the Spanish economy.

Spanish industrialization policy had favored capital intensive sectors characterized by fairly simple production techniques. Metal working industries in particular were especially hard hit by the worldwide recession. From 1978 and 1982 Spanish industry lost 500,000 jobs, or 17 percent of its labor force. Fixed capital formation fell at a rate of about 1.2 percent.

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<sup>83</sup> ibid.

The Basque economy, dependent on heavy industry, was hit even harder. Between 1975 to 1983 the Basque economy lost 20 percent of its manufacturing jobs.<sup>84</sup> Heavy industry in the Basque region lost one half of its 40,000 jobs. Unemployment rose to 18 percent in 1983 from 6 percent in 1976.

For the first time in its history, the Mondragón Cooperative had to deal with contraction. Moreover, it had to do so without Don José María, its spiritual leader, who had died in 1976. And it had to do so in the turbulent years after the death of Franco in 1975, when the ETA initiated widespread violence in the region.

In 1973, the Cooperatives had a net surplus of 10 percent. In 1979, profits had dropped to zero. In 1981 the Cooperative suffered a loss.

In fashioning a policy to deal with economic contraction, the Cooperatives' primary objective was to preserve jobs. Given its emphasis on the inherent value of work and its use of labor as the key to membership in the community of cooperatives, losing a job was a most serious prospect.

The Cooperatives responded to the recession by developing several measures that for the first time created community-wide governance and financial structures. Previously, cooperatives might sell their products or services to one another and were connected by their Charter of Association and their links to the CLP, but they were still highly autonomous, independent entities. The recession forced them to give up some of this autonomy.

Four significant changes were introduced during the early 1980s: an unemployment insurance system; a community wide reserve fund; changes in the internal profit distribution formula to expand the amount of the collective reserve; community wide governance mechanisms.

In 1980 Lagun Aro established an unemployment fund financed by a 0.5 percent payroll tax on associated cooperatives. As the economic recession worsened, this tax was eventually raised to 2.35 percent by 1986. In 1986, 26 of 140 member cooperatives of Lagun Aro received unemployment assistance. The remaining 114 paid into the system.<sup>85</sup>

The unemployment fund was used primarily to transfer cooperative members among cooperatives rather than to pay them while they were not working. Before a cooperative could dip into central unemployment funds it had first: to prove that it needed to cut back by at least 40 people or a fifth of its workforce; to stop distributing profits, if any, to its members or paying out the interest on their individual shareholdings; and to reduce member wages, grade for grade, to 85 percent of the CLP scale.<sup>86</sup>

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<sup>84</sup> Bradley and Gelb, Op. Cit.

<sup>85</sup> An unemployed member of the system receives 80 percent of his or her anticipos plus 100 percent social insurance for 12 months in any two year period. This can be extended if more than 25 percent of the cooperative's members are unemployed. Lagun Aro paid 50 percent of more of these costs, with the rest coming from the unemployed workers' cooperative enterprise, depending on the enterprise's wage level. If the enterprise paid wages equal to 100 percent or greater of CLP, then the split was 50-50. Since many cooperatives cut their wages to cope with recession, Lagun Aro on average, paid a higher 72 percent of unemployment expenses.

<sup>86</sup> Wiener and Oakeshott, Op. Cit.

In 1984 some 3.5 percent of the Cooperative Group's members were reallocated among cooperatives from those hardest hit to those doing relatively well. Lagun Aro paid travel expenses<sup>87</sup> in cases of temporary transfer and provided cheap loans to help with housing if the transfer were permanent. For people transferred to a lower job classification Lagun Aro paid to maintain the previous earnings level. For people whose old cooperative had lost some or all of its capital Lagun Aro provided what they needed to create a capital stake in the new cooperative.

From 1979 to 1983, 1300 of 3500 positions were eliminated at ULGOR. One hundred forty five members split off to form a new cooperative, Fagorclima. Another 466 represented the departure from ULGOR of the after sales service department. They were offered a contract of work identical to existing their duties and in addition, were given the opportunity to represent other manufacturers. Members could also return to the group after a specific period, if desired.

The remaining redundant workers were reallocated within ULARCO, with the remaining ULGOR members compensating any differentials in grade levels through a special levy. All reallocations and spinoffs were voluntary in nature, although some moral suasion was needed for members to willingly transfer to a position with a lower status, even though their wages would not suffer. A small number of members without jobs were placed on 80 percent pay for two years to give them the opportunity to seek employment outside the group, but with the assurance that if unsuccessful, they would be reabsorbed.<sup>88</sup>

In 1980 the ULARCO group members took an effective 11 percent pay cut.<sup>89</sup>

During this period, CLP changed its function from one of creating new enterprises to a much more interventionist and managerial function of restructuring existing enterprises. During 1983, for example, 34 of 100 coops needed help from the intervention department of the CLP. Only after the Bank approved a five year plan developed by management and the Bank intervenor would the Bank make concessionary loans. The plan could include changes in the product line, size of the cooperative, management, wage levels, capital contribution.

The CLP also acted in solidarity with the Group by not fully adjusting its wages to inflation, despite high banking profits.<sup>90</sup> Real official CLP pay scales declined by over 3 percent between 1979 and 1983.<sup>91</sup>

Transferring workers out of a Group was sometimes traumatic for both the worker and the receiving cooperative. Groups tended to be territorial, that is, their member cooperatives were located in the same community. The rootedness of cooperatives and their basic mission of expanding employment in their own

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<sup>87</sup> Most associated cooperative groups were territorial in nature. Thus being transferred out of a group usually meant having much longer distances to travel to work.

<sup>88</sup> Bradley and Gelb, Op. Cit.

<sup>89</sup> See sections below on Distribution of Profits and on Governance

<sup>90</sup> Bradley and Gelb, Op. Cit.

<sup>91</sup> Bradley and Gelb, Op. Cit.

communities led some cooperatives to oppose offering jobs to those outside their immediate areas. As one manager of a small coop said in 1982, "I want to make clear that the motivation of the group of twelve people that formed the cooperative here was to seek a solution to the unemployment in these three municipalities...(W)ith 30,000 inhabitants, there are 1,500 unemployed...This year there will be more. The people here ask that we hire local people. The cooperatives ask that we do otherwise."

The strategies developed by the Cooperative Group to cope with the economic recession were remarkably successful. In the period, 1976 to 1986 the Basque region lost 150,000 jobs. Its unemployment rate rose to over 20 percent. Meanwhile the Mondragón Cooperative actually created 4,200 jobs, although the vast proportion of Mondragón's jobs were created in the service sector(Eroski and CLP).<sup>92</sup>

Of the total Cooperative membership, 6.9 percent saw their jobs eliminated. But as of 1985, two thirds of these were temporarily located as employees in other cooperatives. One quarter were still on the payrolls of their own cooperatives, even though their work was not needed. Only .6 percent of the members, or 104 workers were receiving unemployment payments and would be classified in the United States as unemployed.<sup>93</sup>

In 1982, the Community also established an Intercooperative Solidarity Fund(FISO), a reserve capital fund. It assessed each member to create a fund of 1 billion pesetas that could be used for emergency financing of ailing firms.

The recession in Spain ended in 1986. Mondragón came out of the recession having proved itself capable of responding to economic contraction as well as economic growth. It also had responded to the recession by developing its first community wide mechanisms for transferring labor and capital, and, in 1985, developed the first community wide governance structures. With the continuing increase in funds available to the CLP but with fewer opportunities for internal investment, the CLP was given authority to invest outside the community.

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<sup>92</sup> From 1980 to 1985 the number of positions in industrial cooperatives fell by 630. Trabajo y Union. November 1985.

<sup>93</sup> Whyte and Whyte, Op. Cit. This is from Trabajo y Union, November 1985, based on a June 1985 survey of members. There is some dispute concerning the number of cooperators actually laid off. The 1986 CLP Annual Report noted, "The cooperators of the associated Group, all of them, have come through the critical decade 1976-1986 without ever losing their jobs, nor--of course--their remuneration." Wiener and Oakeshott note that about 30 of 18,000 cooperative members became wholly dependent on unemployment fund.

From over 70 percent of its funds invested in cooperatives in the early 1970s less than a third of its funds were invested in cooperatives by the mid 1980s.

## **Governance and Structure**

The Mondragón Cooperative system has evolved over the years. Each iteration has bound the various elements of the system more tightly. Yet the basic organizational principles remain.

Mondragón consists of base cooperatives and second degree cooperatives. The former produce products and services primarily for consumption outside the membership. The latter primarily serve the cooperative community(e.g. the bank, social security cooperative, retail store, etc.)

Base cooperatives are governed by general assemblies, comprised of all worker-members: one person one vote. The assemblies meet once or twice a year and elect the Board of Directors. The Board appoints top managers, who appoint middle level managers.

Board members serve for 4 years at no pay. The Chair of the Board of Directors is comparable to a Chief Operating Officer of a private firm. Managers are appointed for at least 4 year terms. They have a voice but no vote in Board meetings and cannot be prematurely dismissed except for grave offenses. A Watchdog Council is elected directly by the General Assembly. It monitors the conduct of top management.

The Social Council is comprised of individuals chosen at the shop floor level. Each group of 20-50 workers conducts at least a monthly group meeting to discuss issues. Each group has a representative who meets with other representatives on the Social Council.

In 1966, Don José María wrote, "From the point of view of membership, we are all represented in the Governing Council, but if that were the only organ for representation, our participation in the firm would be very little, at least regarding the ordinary matters(of working life). To avoid this passivity, and to facilitate direct experience with many problems, what we call the Social Council came into existence."<sup>94</sup>

The Social Council's authority is somewhat vague, but it has played an increasingly important role since 1975, when the strike at ULGOR revealed

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<sup>94</sup>Whyte and Whyte, *Op. Cit.* It should be pointed out that after Franco banned trade unions, to substitute for collective bargaining, the Spanish government authorized the creation in each plant or company of a jurado de empresa(jury of the plant). This was a consultative body, consisting of a president or chairperson appointed by management and no more than 10 members elected from administrators, technicians and workers in proportion to their number in the work force. In 1958, the government legalized collective bargaining but only through these jurados de empresa at the firm level. These functioned in some measure similar to the social councils, although the workers had no direct vote on management structure, nor were they owners of the enterprise. Also, Spanish law under Franco made it very difficult for employers to fire employees or even to transfer them to new tasks.

significant discontent at the shop floor.<sup>95</sup> The Social Council has traditionally dealt with issues like personnel matters, job descriptions, salary scales, fringe benefits, accident prevention, work safety.

Article 53 of ULGOR's bylaws, for example, had for much of its history defined social council as advisory and consultative body with a relatively narrow and delineated list of activities. In 1982, ULGOR revised this Article, eliminated the list of topics and instead defined the council broadly as "the spokesman for the social aspirations and concerns of the members" and declared that the Social Council would provide "guidance on all general matters of a societal or labor character that affect the work community."

In 1986, the CLP gave its Social Council an additional function, "To study and analyze experiments in new forms of organization of work to overcome Taylorism and the dependent relations it involves, and to achieve full participation through self-management work teams."

Until the mid 1980s, the Social Council's Chair was appointed by management. At that time Social Councils were given the right to elect their own Chairs.

The Mondragón structure balances individual and collective interests, management and worker interests. Unlike conventional worker cooperatives, Mondragón's management is not directly elected. Management is treated as a special skill. A hierarchy is accepted. Article 4 of the Social Statutes of ULGOR, written by Arizmendi, declares, "work is the means adopted for attaining a higher level of satisfaction for human aspirations and demonstrating collaboration with the other members of the community to promote the common good. To ensure that it is contributed fully, productively and in a manner that makes everyone's collaboration viable, the members shall respect its discipline, namely a hierarchy..."

Thus, writes one observer, "the capitalist system's equivalent of management and union are each present in Mondragón and (each are) distinct: however, they both are inside the 'us' of the cooperative, and are subservient to the Board, which assures their total integration and coordination. If the Board ever fails the task, the general assembly of all the owner workers, which wields ultimate power within the cooperative, can overrule the board."<sup>96</sup>

Although the general assembly of all owner workers has ultimate authority even this body lacks the authority to alter the basic structure of the cooperative.<sup>97</sup> By terms of the Cooperative Charter, which all members must sign, individual cooperatives cannot have a direct member vote on the size of the initial contribution required of new members or the minimum percentage of cooperative earnings which must be retained for investment or the conditions under which workers can reclaim their own capital accounts or the sanctions for

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<sup>95</sup>See below for a discussion of the Ulgor strike.

<sup>96</sup>Terry Mollner, "The Relationship Age and a new Kind of Nation", World Futures. Vol 31. 1991

<sup>97</sup> A cooperative does have the authority to leave the Community, an option exercised by only one enterprise.

employee misconduct, or maximum wage rates, layoff procedures or profit payouts. The charter establishes these in advance.<sup>98</sup>

Each second degree cooperative's General Assembly and Board of Directors may have a different composition, depending on the circumstances, in order to balance the interests of the workers and the enterprise's customers.

The CLP Board, for example, consists of 12 members, two thirds of them representatives from borrowing cooperatives and one third representatives of the bank's workers.<sup>99</sup>

Eroski's Board consists of 6 members elected by its workers, and 6 elected by consumers. The Chair is always from the consumer side. Eroski has an annual assembly for its workers, and four regional assemblies of consumers.<sup>100</sup> Both the workers and the consumers elect 250 delegates to the overall general assembly and the general assembly elects the Board.

The Board of Ikerlan, the research and development center, has 12 members, 4 representatives of Ikerlan's workers, 6 representatives of industrial cooperatives, and two representatives of other second level cooperatives. Of the six representatives of industrial cooperatives, four represent cooperatives whose technologies are closely associated with the research activities undertaken at Ikerlan and two seats for cooperatives which are not active in research areas by staff.<sup>101</sup>

In 1964, the first inter-group structure was formed. Four industrial coops joined to form ULARCO. The Group engaged in common sales, marketing, finance, work organization, scheduling, purchasing and planning. By the early 1980s, about 70 of the industrial cooperatives were associated in 12 regional groups. The Groups formulated common social policies and working conditions, arranged transfers of members among them, and shared some legal and financial administration.

Groups were primarily territorial in nature, linking together related industries in the same community.

The process of decisionmaking within the cooperatives is sometimes a matter of what Quakers call, "a loving struggle to agreement". It involves a long consultative process between management, workers, and other outside interests as well. Consider the following example.

In November 1978, ULARCO's governing council, that is, its Board of Directors, faced with the looming economic downturn, proposed a new means of

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<sup>98</sup>Philip Keefer and Lee Benham, "Voting in Firms: The Role of Agenda Control, Size and Voter Homogeneity", *Economic Inquiry*. October 1991.

<sup>99</sup>In the early years, community savers were represented in the general assembly, but this was ultimately rejected on the grounds that "making shareholders out of all savers would have hindered the administration of the credit institution". See Morrison.

<sup>100</sup>Spanish law does not permit consumer cooperatives to sell to other than their members, so Eroski charges a few pesetas more for a customer's initial purchase to make him or her a member. Eroski's consumers do not have a vote in management decisions. Eroski does not give dividends or rebates to its customers the way traditional consumer cooperatives in the U.S. do.

<sup>101</sup>In cases of conflict, the Supervisory Board will decide which cooperative gets the right to introduce the innovation. If no interest is expressed, then the news is made public.

calculating wages. The Board justified this modification by pointing to the combination of worsening general economic conditions, a poor internal cash flow and a 31 percent increase in wages as a percentage of sales compared with a 20 percent increase in productivity.

The new plan was sent to the Central Permanent Commission(CPC) of ULARCO.<sup>102</sup> This body was composed of representatives of the social councils of all member cooperatives of ULARCO. Its function was not advocacy, but education, explaining management's proposal to the workers, and eliciting their responses.

Under management's plan, wages would still be adjusted annually in line with the cost of living<sup>103</sup>, but they would also be connected to the cooperatives' economic performance. The plan also suggested reducing the wages to finance the economic restructuring of the member cooperatives.

The ULARCO Board proposal began a extended and extensive consultative process. The CPC responded to the Board's proposal with a detailed Critical Report. CPC developed training and educational materials for the social councils of the individual enterprises and sent representatives to explain the proposal and obtain responses.

Discussions lasted several weeks. During this period, cooperative members organized interest groups that included the participation of the Basque trade union, ELA-STV, and other independent parties. In all, four alternative proposals to that of ULARCO's governing council were developed: one by the Copreci Social Council; one by a group connected to ELA-STV; a third by a faction connected with Basque political groups and other unions. A final proposal was by members calling for no change in the current system.

The CPC polled all ULARCO members on possible options . About 68 percent responded. Ninety percent of them supported in principle the change in the calculation of wages. The faction connected with Basque political groups won a plurality in the advisory vote of the social councils, with the governing council's proposal coming in a close second.

The ULARCO governing council then adjusted its own proposal. In a final and binding vote, the cooperative general assembly was asked to choose between a modified governing council proposal and no change. The governing council's proposal received the two thirds majority vote required.

After the vote, ULGOR's social council reviewed the decision making process and expressed concern about the need for earlier participation by the CPC and the low involvement of women in the process.

The entire process took 4 months.

Often a management proposal will initially be rejected and later approved. In 1980, ULARCO's management decided that it needed to increase total capitalization by \$12 million over the next three years.<sup>104</sup> ULGOR represented

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<sup>102</sup> At the time ULARCO had about 6,000 worker-owners.

<sup>103</sup> See discussion on Distribution of Surplus and community finances.

<sup>104</sup> Someone with 3.0 pay level would contribute twice as much as someone with 1.5 pay level. The average contribution per cooperator would be \$600 per year for three years to attain the \$12

half of ULARCO's membership. To prevent ULGOR from having undue influence on the decision, ULARCO counted the vote in two ways. One was based on unweighted total votes. The other gave smaller firms somewhat increased weight. Sums from the two methods were added and divided by two.

In April 1980, 61.9 percent of ULARCO's members voted in favor of the management proposal, less than the two-thirds needed. In 1981, management came back with the same proposal, but with a different and more exhaustive financial analysis, and more consultation. There was also increasing recognition of the extent and duration of the recession. This time the proposal was approved by the requisite number of voters.

In the mid 1980s, for the first time the Cooperative Group developed community wide governance structures. These mirrored the governance structures within individual cooperatives.

The 350 member Cooperative Congress corresponds to the General Assembly. Each cooperative has at least one representative in the Congress. To limit the total number attending, larger cooperatives do not have representation in direct proportion to their size.

The 17 member Council of Groups acts like the Community's Board of Directors. There is the equivalent of a Watchdog Council. And a Central Social Council.

The Congress must meet at least once every two years. It is the policy body, determining social statutes and the internal rules regulations of the cooperatives, the Community's position on social issues, and all relationships with national and international governments.

The Council of Groups is composed of managers of the 12 regional Groups plus the managers of Eroski, Lagun Aro, Ikerlan, and the President of the Congress. The Council focuses on maintaining a unified industrial policy for all enterprises. It coordinates finance, investment, promotion, and research and development strategies. The Council meets at least once every three months. Each council representative has number of votes equal to number of members he or she represents.

In October 1987, the first meeting of the Cooperative Congress took place. Gorrongoitia was elected Chair of the Governing Council and Ormaechea became Chair of the Council of Cooperative Groups. That these people, founders and managers of ULGOR, founders and managers of the CLP and of FAGOR, are still in positions of leadership of the new community wide governance structures illustrates one of Mondragón's strengths, the continuity of leadership.

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million required by ULARCO. Cooperators could appeal on the basis of personal hardship for partial or complete abatement of contribution. Cooperators chose to make capital contributions from a combination of withholding from wages and withholding interest payments normally received as cash on internal capital accounts. For newer members without large capital accounts withholding from wages would be increased to create the required amount.

## Distributing Surplus: Wages, Profits, and Investment

The Mondragón system for distributing profits balances many interests: the desire for egalitarianism and the need for individual initiative; the desire for individual income maximization and the need for enterprises for sufficient capital for reserves and expansion; the desire for individual enterprises to maximize their own reserves and the need for the community as a whole to maintain full employment.

Community wages are called "anticipos", advances on profits. The CLP establishes the basic wage rates. All associated enterprises are permitted to set their basic wages modestly lower or higher than the CLP wage scale. The Contract of Association also establishes maximum wage differentials. Initially the Community established a wage differential of 3 to 1, from the highest to lowest paid worker. In the late 1970s individual cooperatives were permitted to raise the top pay by 50 percent, to a 4.5 to 1 differential in special cases. In the mid 1980s the maximum differential was raised again, to 6 to 1.

The wages of the vast majority of workers are still within a narrow range. A study done of the Fagor group in the mid 1980s found that although a 4.5 to 1 range was permissible, if one leaves out the 1 percent of members with the highest pay, and the 11 percent with lowest, the remaining 98 percent were within a two to one differential.<sup>105</sup>

Wages are established on the basis of job evaluation points. Twenty percent of the points are given for "relational skills", up from 10 percent in the early years of the Community, emphasizing the importance it places on cooperation. Twenty five percent of the points awarded are for theoretical knowledge, up from 20 percent in earlier years, emphasizing the increasing importance of knowledge intensive operations. Twenty five percent of the points are awarded on the basis of experience, 8 percent for decision making skills, 7 percent for leadership, and 15 percent for the position's physical and visual stress. Managers can also reward workers for above average performance with a modest point bonus.<sup>106</sup>

Job evaluation points may run from 122 to 383.5. The lowest score translates into an index of 1.15, while the highest scores translate into an index of 2.80, the index being the multiplier of the minimum wage.<sup>107</sup>

Within the Community, lower paid workers on average receive higher wages than their counterparts in the private sector in the region. However, management receives substantially lower wages. A study by CLP in 1985 found that the salary

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<sup>105</sup>Whyte and Whyte, *Op. Cit.*

<sup>106</sup> Thomas and Logan, *Op. Cit.*

<sup>107</sup> In the selection process for new members, extra points are given for fluency in Basque or Basque origin. Extra points are also given to those who live in the same town where the firm is located. Points are also awarded to those with kinship ties. In 1979 all managers were Basque. On the shop floor 25 percent of members were not Basque, about the same proportion as the non-Basques in the region's population. Philip Keefer and Lee Benham, "Voting in Firms: The Role of Agenda Control, Size and Voter Homogeneity", *Economic Inquiry*. October 1991.

scale for executives in the cooperatives was 18-43 percent lower than that of comparable personnel in Spain and 3-42 percent less than their counterparts in the Basque region.<sup>108</sup>

Net profits, that is, net revenues minus payroll costs, interest and depreciation, are allocated to one individual and two collective accounts.

One of the collective accounts is required by Spanish cooperative law. Ten percent of the net profits must be spent on charitable purposes that benefit more than just the members of the Community. Most of these funds are spent on educational endeavors, although they have also been spent on building sports fields and on cultural pursuits. The other collective account is the enterprise's reinvested earnings. The individual account is the capital account of the individual worker.

General guidelines for how much of the profits must be invested in each account are established by the Community, except for the 10 percent social and educational account, which is mandated by the State.

Until 1990, at least 20 percent of the net surplus had to be invested in cooperative reserves and a maximum of 70 percent could be paid into member accounts. This is often given as a 10-20-70 disbursement.

Profits distributed to individual accounts in the 1970s were frequently equal to 3 months pay.

Although money invested in the individual's capital accounts is owned by the individual, he or she cannot withdraw it until retirement.<sup>109</sup> On retirement, the accumulated profits, by Spanish law, must be paid out within two years. Voluntary departure could involve a penalty of up to 30 percent of accumulated profits, and a significant penalty can be imposed if a worker is fired for a grave offense.<sup>110</sup>

The worker's internal capital account is usually increased by the cost of living each year. It also earns interest. The account is regarded as a loan from the worker to the enterprise. Interest paid on the capital account is set by the General Assembly each year, but it cannot exceed the interbank rate of interest set by the Bank of Spain by more than 3 percentage points.

Interest payments on capital contribution can be cashed up to 6 percent maximum. Thus the worker received a basic wage and two cash payments on a semi-annual basis each year, for 14 monthly paychecks. In the early years part of the profits were disbursed in cash. In 1960, 10 percent of the profits were distributed in cash, rising to 25 percent in 1961 and 30 percent in 1962-65. However, since 1966 all shares of profits have gone into members' capital accounts, a vigorously debated decision by the Community.<sup>111</sup>

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<sup>108</sup>Whyte and Whyte, Op. Cit.

<sup>109</sup>In 1960 10 percent of the enterprises' profits were paid to members in cash, 25 percent in 1961 and 30 percent in 1962 through 1965. But in 1966 all shares of profits have gone into the member's capital account, a decision that was vigorously debated.

<sup>110</sup>Bradley and Gelb, Op. Cit.

<sup>111</sup>Whyte and Whyte, Op. Cit.

This disbursement formula and regulations means that the enterprise effectively controls 90 percent of its net surplus. The individual capital account might be considered a long term, low interest loan to an enterprise that might not have the collateral to be able to borrow money outside.

The worker can use his or her internal account as collateral for a bank loan at CLP at an interest rate a point or two above the 6 percent the account is earning.

Spanish cooperative law prevents workers from benefitting from the increased value of their enterprise's assets if they should sell the firm or liquidate it. If a cooperative enterprise is liquidated, the revenue goes to the state. In return for this limitation, and in return for requiring that 10 percent of the net surplus be spent on charitable pursuits, Spain reduces by 50 percent the income tax rate on cooperative generated income.

Much of the major decisions in the Community, not surprising, have concerned the relationship between the amount of surplus going into the collective reserve fund versus that going into the individual capital account. From 1959 through 1969 the amount allocated to the reserve fund fluctuated between 35 and 53 percent. Through the 1970s it ranged from 11 to 29 percent. In the 1980s it was in the 50 percent or higher range.<sup>112</sup> Overall, the proportion of individual accounts of the enterprises total capital reserves has fallen dramatically, from 95 percent in 1965 to 38 percent in 1985.

Within the overall guidelines established by the CLP and the Community, each Cooperative may vary its disbursement formula.

Alecoop, for example, the nature of its situation, suffers a very high turnover in its workforce. Every three years an entirely new body of student workers is employed. Exiting workers can take their capital with them. The threat of decapitalization, led Alecoop to change the 10-20-70 traditional formula to a 10-60-30 distribution. The greater part of the net profits thus becomes reserves to strengthen the factory.

In 1989 the Community changed the basic distribution formula so that the minimum contribution of 50 percent of net surplus to mandatory reserve fund up from 20 percent.<sup>113</sup>

Mondragón firmly believes that every member should risk his or her own capital. Every new member must make a financial investment in the enterprise. In the early years, this contribution has been the equivalent of one year's salary at the lowest wage level. The entry fee has risen considerably, both in nominal and real terms but in terms of its overall economic contribution, it has been significantly reduced. By the mid 1980s, the contribution was about 4 months' wages.<sup>114</sup>

The entry fee has not dissuaded potential entrants. There has always been a long waiting list for residents wanting to obtain a job in the Community.

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<sup>112</sup> Ibid.

<sup>113</sup> Annual Report of the Caja Laboral Popular. 1990.

<sup>114</sup> Alecoop requires entry fees equivalent to 2 months student salaries.

New members can sign a note and the capital will be withheld from their salary over time, with no interest attached. For those starting a new enterprise, the capital contribution is about twice the capital contribution to existing enterprises.

In 1975, new members' contributions were about 20 percent of the cost of creating a new job. By 1982, because of the increased capital intensity per job, this had dropped to 10 percent.<sup>115</sup>

In 1964, Ulgo and its associated cooperatives formed the Community's first associated group, ULARCO. In the late 1960s, it began partially pooling its members' enterprise profits. In 1976, profits were completely pooled. Pooling surplus dilutes incentives because it weakens the link between enterprise performance and the accumulation of individual capital. On the other hand, the increasing coordination between enterprises and the imperatives of job security argued in favor of pooling.

The 1992 restructuring of the Community is promoting a much greater pooling of profits. Profits will be pooled on the basis of the new sectors and divisions that comprise the new Cooperative Corporation. The Community has established that a minimum of 15 percent of the profits and a maximum of 40 percent maximum will be shared. This process of financial pooling is to take place over a four year period.

One intriguing aspect of Mondragón's internal financial system is that it has relied on a metal production price index, not a consumer price index, to adjust its capital accounts. Metal production is the predominant area of the Community's activity and the metal products index is considered more rational since it tends to more closely reflect changes in the cooperatives' income rather than changes in the consumer price index(CPI).

The CPI would more closely track the cooperators actual cost of living rather than the cooperatives' cash flows. In times of slack demand and inflation, the metal price index might lag the CPI . Wages would rise less rapidly than if the Community used the CPI base. In boom times for metal products, the Community's wages would exceed the CPI adjustment.

New Spanish law requires cooperatives to use the Consumer Price Index. Today the Community uses a mix of both indices.

## **Management and Worker**

In any enterprises there is a tension between management and worker and Mondragón's enterprises are no exception. In many private firms, labor unions represent the workers before management. Trade unions are not permitted within Mondragón's cooperatives, the theory being that workers are owners and have the right to vote in the overall management of the firm. Unions were outlawed by Franco. They were legalized in the mid 1970s but cooperative members voted overwhelmingly against allowing union organizing within their

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<sup>115</sup> Whyte and Whyte, *Op. Cit.*

enterprises. Organizing a strike against the enterprise is considered one of the gravest offenses.

A strike at ULGOR and Fagor Electrotécnica, the only strike ever to occur in the Community, had important implications for the development of the Mondragón system. Following a long running dispute over a two year job-reevaluation program, more than 400 workers struck for eight days in July 1974. Management of the two cooperatives expelled the strikers and were supported by their general assemblies.

The strikers were demanding greater equality of wages. Also, they were angered by the power given to supervisors by the introduction of a "merit factor" based on the immediate supervisor's judgement. This amounted to a 15 percent pay differential for the lowest paid cooperator and a 5 percent differential for the highest paid. These matters particularly concerned women, who had experienced substantial discrimination within the cooperative system.<sup>116</sup>

The ULGOR strikers' petition to be readmitted was denied by a 61 percent positive vote by the general assembly in March 1977, but in April 1978 the assembly approved their re-entry by a 67 percent vote.<sup>117</sup>

The Mondragón Cooperative responded to the ULGOR strike in two ways. First, it significantly strengthened the role of the social councils as an alternative to unions, a strengthening process that continued for a decade. Second, it concluded that a major cause of the problems in ULGOR were a result of its size(3,500 workers). In the future, the Community planned that cooperatives should be limited to no more than a few hundred workers to minimize the distance between workers and management and to maximize the sense of personal community in the enterprises.

In 1981, Bradley and Gelb reported that 21 percent of the Mondragón workers reported a "large division" between management and workers, compared to 62 percent of workers in private firms. Thirty percent of Mondragón respondents said they did not participate at all in important decisions, compared to 80 percent in private firms.<sup>118</sup> The gap between worker and management may be widening. This is in part a result of the need for more specialized management, and the increasing recruitment of managers from outside the community.

Before 1980, the recruitment for higher level positions primarily came from within. Now the Cooperative may have to socialize highly educated newcomers into cooperative ways. That may prove difficult.

In 1975, the turnover in higher levels of Mondragón's management was less than 10 percent per year despite major differences in salaries. Of those who left, few had gone through the EPP before beginning to work in the complex. "In other words, those who had been socialized into the cooperative way of life as

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<sup>116</sup> Of the 24 strike leaders expelled by the two cooperatives, 18 were women, an astonishing percentage given the extremely low percentage of women workers in cooperatives at the time. Morrison, Op. Cit.

<sup>117</sup> Ibid.

<sup>118</sup> Keith Bradley and Alan Gelb, "Motivation and Control in the Mondragón Experiment". British Journal of Industrial Relations. 19:211-31.

youths, found sufficient social and psychological satisfaction within the complex to outweigh the lure of higher pay elsewhere", the Whytes conclude.<sup>119</sup>

In the period 1980 to 1985, there was a very high turnover among management staff: 80 percent among administrative directors, 112-115 percent for three other executive positions. Most went to other cooperatives within the Community. Marketing directors, however, with the highest frequency of contact with outsiders, were most likely to leave the Cooperative system.<sup>120</sup>

There has been an increase in the prestige and authority accorded professional training. Most typical members in the early days were skilled craftsmen and semi-skilled assembly line workers. Now specialized skills required. Technical degree or degree in economics is necessary to perform complicated work of managing, directing, making decisions. One of the directors Hacker interviewed said that in the early days of the cooperatives "we were all in it together". Now the director perceived lower level workers are ungrateful, wanting only security rather than the participation and responsibility that comes with cooperation. Workers, meanwhile, resented increasingly distant management that moves them around from job to job, increases or decreases work, speeds it up or slows it down. Attendance at general assembly meetings had been dwindling in the mid 1980s.<sup>121</sup>

### **The Mondragón Cooperative as a Community Wide System: Present and Future**

On the enterprise level, the Mondragón Cooperative has successfully overcome the principal problems afflicting most producer cooperatives.

- The inability to attract and train good managers
- The inability to develop adequate financing for internal investment and cooperative expansion
- The inability to develop structures that allow for managerial decisionmaking autonomy while making management ultimately responsible to its worker-owners
- The inability to achieve sufficient scale to compete in global markets

On the community level, Mondragón's system has blurred the boundary lines between labor and capital and between public and private sectors. Decisions related to health, education and welfare are made under the same umbrella governance structure that makes decisions related to investment and employment.

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<sup>119</sup>Whyte and Whyte, Op. Cit.

<sup>120</sup> Ibid.

<sup>121</sup>Sally Hacker, Pleasure, Power and Technology. Unwin Hyman. Boston. 1989.

Ordinarily, these activities are divided up not only into public and private sectors, each of which has different decisionmaking apparatuses and criteria, but in the public sector, jurisdiction is fragmented by agency, and by level of government.

Typically, most decisions about public spending and private investment are made outside of the communities affected by the decisions. Much of the money spent in the private sector leaves the local community. Of the one third to one half of a worker's earnings that goes to government, the majority does return to the community but from a bewildering array of agencies guided by an equally bewildering array of directives that are rarely designed to the needs of that particular community. Most of the savings deposited in local financial institutions are similarly not invested within the community or are invested without community-wide goals in mind.

In Mondragón, a community focus is apparent in virtually all its decisions. A large portion of the productive assets of the community are owned by the community. Much of the revenue generated from these productive assets remains within the community. A significant amount of the spending by community residents may occur within community owned institutions. Private savings are deposited within community oriented, cooperative institutions.

Decisions about the allocation of private sector earnings are increasingly coordinated by a single decision making umbrella that takes into account the impact on the community as a whole. In the past, decisions concerning the allocation of what have traditionally been public sector earnings(i.e. tax revenue) have also been taken by the Community through its financing and operation of many social services(unemployment insurance, health, pensions, education)

This unusual influence over its internal economy and the consolidation of many sectors under one decisionmaking apparatus offers Mondragón the opportunity to make resource allocation decisions that are comprehensive and community-wide.

In all communities, everything is connected to everything else. Crime results from poverty and the breakdown of community. Poverty results from a lack of jobs. Unemployment results from a lack of education or the inability to generate capital internally. The inability to generate capital internally stems from a lack of community owned productive assets and a poorly skilled and educated workforce.

In conventional communities, the policy connection between these sectors is not direct, and jurisdiction over these areas is fragmented. In Mondragón, the jurisdiction is increasingly under a common decisionmaking mechanism that is guided by common social values. This allows for a decisionmaking process that accounts for the full community wide costs of decisions.

At least in theory, this could translate into wiser use of resources and lower overall costs. Mondragón's Lagun Aro cooperative, for example, closely monitors disease and accident rates, and intervenes to improve worker safety through the cooperatives' social councils. Lagun Aro also works with Eroski, the chain of retail stores, to communicate dietary information via the latter's monthly newsletter. Cooperatives are rewarded for using the medical system less than

the Community average, and are penalized for using the medical system more than the average.

Mondragón's technical schools are connected to the cooperatives in many ways. Alecoop, the student run factory, is itself an industrial cooperative whose governance structure includes representatives of other factories. Alecoop's products are primarily sold to Mondragón cooperatives. The technical schools also have representatives of other cooperatives on their governing boards. The schools' faculty works closely with the industrial cooperatives to update the textbooks and the curriculum. "Faculties write their own textbooks updating materials as the technology and theory of manufacturing and engineering changes within the cooperatives. They work with the industrial cooperatives to ensure that methods taught are the most current in each field. They also strive to keep the equipment for students in the laboratories and workshops as modern as possible."<sup>122</sup>

One result of the combination of scarce resources in the Mondragón cooperative for education, and the close relationship between the schools and the industrial enterprises, is that the education system is heavy on technical training and light on the social sciences.

Mondragón's unemployment insurance program illustrates its ability to make the best use of existing resources. The unemployment insurance will pay 80 percent of a worker's salary. This is considered the maximum financial cost the Community is willing to underwrite. Yet paying the full 80 percent to a fully unemployed person is viewed as a system failure. The objective is to maintain work for the member.

The first line of defense against unemployment occurs in the individual cooperative. If the cooperative cannot handle the problem by reducing wages or restructuring work, the cooperative group is asked to solve the problem. Within its associated cooperatives, the Group has some who are doing well even during hard economic times, and others that are very hard hit, so it can reallocate resources within the Group to reduce layoffs. Only when the individual cooperative and the associated cooperatives within a Group have exhausted their capacities, does the unemployment fund kick in. Even then, it first pays for the relocation costs of transferring workers outside of the associated cooperatives, costs that usually include travel costs and making up for the lower wage rate these workers might receive at the new cooperative. Only as a last resort, does the unemployment fund pay a laid off worker 80 percent of his or her salary.

Mondragón is an egalitarian community, but it is not a leveller community. Wage differentials are permitted, even though by American standards they are very modest. Even at a 6 to one differential from top to bottom, the range is from about \$13,000 to about \$78,000. However, the vast majority of workers are within a 2 to 1 wage differential. Information on the wages of all workers is available to everyone.

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<sup>122</sup> Meek and Woodworth, Op. Cit.

Mondragón has some of the characteristics of a private enterprise system. Members are required to invest their own money in their enterprises when they enter the Cooperative. Members starting up new cooperative have traditionally been required to invest twice as much as those entering existing cooperatives. Having its members at risk is one of the basic principles of the Mondragón Cooperative.

Workers share in their enterprise's profits(or losses), and increasingly, they share in the Community's profits(or losses). Yet these profits are not available to them until they retire. This balances the individual interest in maximizing current income and the enterprise's interest in maximizing the capital available for long term investment or as emergency reserves.

Mondragón's worker-owners have been willing to subordinate their desire for higher immediate incomes to the needs of their enterprises. In the 1960s, workers agreed to end the practice of distributing some of the enterprise's net surplus as cash payments to individual workers. This was done to bolster the enterprise's capital reserves.

In the 1980s, initially in individual enterprises facing the worsening economic recession, and then on a Community wide basis because of the need for heavy investment to cope with global competition, workers agreed to change the basic distribution formula to substantially increase the amount of the net surplus that went into the enterprise's collective reserves.

Managers are given significant autonomy. Top managers are not elected by the General Assembly. They are appointed by the Board of Directors for fixed terms and cannot be easily dismissed. Workers are involved in day to day operations of the plant through the Social Council. Unions are prohibited, although outside unions can and have worked with members to formulate proposals to the General Assembly in response to management initiatives. The Social Council acts somewhat like the works councils in Germany, and somewhat like a representative of workers in regard to overall management policy. Unlike the co-determination design of large German firms, in Mondragón the workers are the shareholders and can replace the entire Board of Directors. The role and autonomy of the Social Council has been strengthened over the last 15 years. Yet it remains true that the Social Councils are largely reactive, rarely pro-active. They respond to management initiatives rather than developing their own bottom up major policy initiatives.

Today, the Mondragón system is facing its greatest challenge. The globalization of competition and Spain's full membership in the European Community<sup>123</sup> has convinced Mondragón to reorganize itself into a much more corporate and centralized structure. The President of the new Corporation concedes, "it will require a large dose of confidence in those in leadership positions and a willingness to change the culture implicit in the project".<sup>124</sup>

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<sup>123</sup> Spain, as with all members, was given provisional status at first. It becomes a full member in 1992.

<sup>124</sup> Trabajo y Union. January, 1992.

The Mondragón Community is also opening up to its hitherto remarkably closed system to outside forces. In the past, investment capital, except for government funds, was largely generated internally. Worker mobility was limited. Non-members were prohibited from long term employment in the cooperatives. All enterprises operated under the same cooperative rules. Virtually all enterprises were in the Basque region.<sup>125</sup> In the hiring process, extra points are awarded for fluency in Euskera or for Basque origin.<sup>126</sup> Within the cooperatives the official language is Basque.<sup>127</sup> As of 1979, all Mondragón's managers were Basque, although 20-25 percent of its labor force were non-Basque residents of the region.

Even within the Basque region, Mondragón's cooperatives have been very community oriented.<sup>128</sup> Extra points for hiring purposes were also awarded for those who live in the same town where the firm is located or who are related to existing workers. Most cooperative groups have been territorial in nature, with associated enterprises within a short distance of one another.

These basic features of the Mondragón Cooperative may be changing.

Managers may increasingly come in from outside the Community. The expertise and global experience necessary may reduce the numbers of top managers who come up from the ranks. This means managers who have not been socialized into the cooperative experience by attending the cooperative education system or working in cooperative enterprises.

The European Community is abolishing most barriers to labor mobility. This probably will not affect the movement of most workers, but it may boost top management mobility.<sup>129</sup> In the past, marketing managers have been most prone to leave the Cooperative system, and marketing is now a major emphasis in competing in the European market.

To attract and retain top management, Mondragón may widen its wage differentials. From 1975 to 1985 pay differentials widened from 3 to 1, to 4.5 to 1, and then to 6 to 1 from bottom to top. This was done in the face of significant opposition. A further widening would exacerbate tensions within the Cooperative system.

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<sup>125</sup> A few enterprises had established foreign ventures. In the early 1970s Ulgor, for example, built a subsidiary factory in Mexico.

<sup>126</sup> Benham and Keefer, Op. Cit.

<sup>127</sup> Some 20-25 percent of Mondragón's workforce is non-Basque, about the same as the overall Basque region population, but the vast majority of managers have been Basque.

<sup>128</sup> In drawing up short lists of applicants the most important variable is their ability and willingness to integrate, both into the local community and potentially into the cooperative. Workers undergo a six month trial period in which their supervisors' reports heavily stress social acceptability. This is also stressed for promotions. Keith Bradley and Alan Gelb. "The Mondragón Cooperatives. Guidelines for a Cooperative Economy?" in Derek C. Jones, and Jan Svejnar. Participatory and Self-Managed Firm. Lexington Books 1982.

<sup>129</sup> "We contend that a more significant obstacle (than Basqueness) to the widespread establishment of Mondragón style cooperatives is the difficulty of reconciling them with labor mobility", two observers conclude. Bradley and Gelb, "The Mondragón Cooperatives: Guidelines for a Cooperative Economy?", Op. Cit.

To compete in the European and global market, Mondragón is emphasizing knowledge intensive and capital intensive technologies. This new emphasis, begun in the mid 1980s, mean that fewer jobs may be created, and that each job created will become more costly. This could pose a serious problem for a Community one of whose basic tenets has been to expand employment so as to integrate into more and more of the surrounding economy.

For the first time, Mondragón is owning and operating enterprises that do not conform to its basic cooperative structure. Eroski has embarked on an ambitious program of expansion in other parts of Spain, with many of the individual stores having conventional employees. The Cooperative is negotiating joint ventures with several large European corporations. Fagor has purchased a factory whose union structure will be kept intact.<sup>130</sup>

The Cooperative has established an investment group that will invest in private enterprises outside the region, and the Cooperative is negotiating several joint ventures with large European Corporations.

The increasing autonomy of the Basque government and its ability to control its tax revenue, is bringing in a potentially large source of outside funds into the Mondragón Cooperative. Since the Statute of Autonomy signed with the Basque region in 1982, more authority has been delegated to the region from Madrid. This allows it to legislate and to retain and spend internally generated tax revenue. The Basque government now finances significant portions of Mondragón's previously internally financed schools, health and research and development sectors.

The scale of the Basque region, and the Mondragón Cooperative's influence and prestige within the region, means that Mondragón's members will have a significant participation and perhaps influence over policy decisions at the governmental level. Indeed, a 1989 meeting of Basque National Congress adopted Mondragón's "third way" as the official economic policy of the new Basque nation.<sup>131</sup>

The Basque region's population of 2.3 million people, is equivalent to the population of Chicago, Philadelphia, the San Francisco Bay area, or the Twin Cities in Minnesota. It is unclear whether, in the long term, this will lead to the Mondragónization of the Basque economy, or whether the traditional public-private dichotomy will reappear. One possibility is that Mondragón's influence in the Basque region, and the Basque region's expanding authority, may lead the regional government to change some basic rules related to the cooperative structure.

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<sup>130</sup> Fagor purchased the enterprise, Victor Luzuriaga, an automobile parts maker, as a defense measure, to thwart its falling into the hands of a global corporate competitor.

<sup>131</sup> Mollner, Op. Cit.

## Mondragón In An Era of Free Trade

"From its genesis, development and success in a local and domestic market, (Mondragón) finds itself in a new competitive planetary scenario, where the validity of its socially oriented model will be tested."

Jesús Larrañaga, one of Mondragón's founders. May 1992

"We will continue being cooperativists. We have created the most impressive cooperative system that exists in the world....Our cooperativism is dynamic and modern, adaptable to the current times. We have not remained in the Rochdale era. That would not be beneficial. The capitalism of today is not the capitalism of the 19th century. Nor can the cooperativism of today be the same as before....A more complex world requires a more complex cooperativism. Difficult situations don't engender easy solutions."

José María Mendizabal, an early member. May 1992.

The nature of this change is clear from the Cooperative's new name: Mondragón Cooperative Corporation instead of Mondragón Cooperative Group.

"(T)he profound change in the global reality (of)international competition (is) so important that it forces us to develop a more cohesive Group", writes Jesus M. Herrasti, the new President of the Congress of the Corporation. "The objective of this restructuring is to achieve a more cohesive integration of the cooperatives focussed on a common project", says another leader.<sup>132</sup>

The Corporation will be divided into three divisions: financing, industrial and distribution. Each division will be further divided into 8 sector groupings: automobile parts, food, construction, finance, domestic electrical components, machine goods, distribution, industrial components. These will replace the current largely territorial groupings.

A vice president will oversee each division. Each sectoral group will have its own general assembly, and council. there will be a vice president in charge of each division.

This change was approved at the second Cooperative Congress in December 1991. It will consolidate the Community and will centralize authority. There will continue to be a Cooperative Congress, a Permanent Commission and a Governing Council but management will be more centralized and more remote from individual enterprises.

In gearing up for global competition, Mondragón has opened its formerly impermeable boundaries in many areas. Its Bank now invests largely outside the Cooperative system. Its new investment house will specifically focus on investments outside the Community. The new distribution group will include the Eroski-Consum Business Group, headquartered in San Sebastian, a joint venture with the new Valencia cooperative. The Community has decided to dramatically expand Eroski's presence in non-Basque markets, increasing overall sales sixfold by the year 2000. A massive \$249 million investment program was

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<sup>132</sup> Trabajo y Union. January, 1992

approved in 1990, the largest ever undertaken, and a 36 percent increase over the previous year. More than 40 percent of that investment is for the expansion of Eroski.<sup>133</sup>

Outside the Iberian Peninsula, the Cooperative has taken a majority interest in Altis, a joint venture with the Adour Pyrenees Consumer Cooperative to manage commercial establishments in the south of France. The Community is negotiating a joint venture between Fagor and the French company Thomson and AEG of Germany in the field of domestic electric products.

For the first time, the Cooperative is owning and operating facilities which are not worker-owned. Eroski is establishing stores outside the Basque area that are not worker-owned. Fagor has purchased the Basque based Victor Luzuriaga, an automobile parts concern, because Fagor was worried that the firm might otherwise be purchased by a European competitor. Mondragón's stake in Luzuriaga will be only 50.16 percent, and Luzuriaga's union will be maintained.

## Introduction

1992 marks a time of great reflection for the Mondragón cooperative system. The unified European market has stripped Spanish industry of its defenses against the large multinationals and has put a huge premium on access to continental and even global marketing and distribution networks. And the persistent economic slowdown in the Basque Country and Spain has made job creation more difficult and increased the reliance on exports.

These dramatic ongoing changes have engendered a great deal of introspection and reflection by long term members of the community. Many now insist that the Mondragón experiment could not be repeated in the Basque Country today.

Jesús Larrañaga, one of the founders of ULGOR asks, "Would the cooperative system of Mondragón have been born and developed, given the present conditions?" He answers his own question, "A resounding no."<sup>134</sup> José María Ormaechea, another founder, asks a similar question, "Today, with the level of economic well-being that has been achieved...would we, in April 14 1992, have laid the first stone for the construction of the first workshop of ULGOR, as was done in 1956? Probably not...the passage of time has weakened the influences that favored the germination of the cooperative idea. Thus one must ask oneself, what can be done now, not to recreate this desire for cooperativism, but simply to maintain its prosperity?"

Mondragón's is a system born of a time of scarcity. In 1956 workers in Spain labored for 2750 hours a year. Annual per capita income was \$150. Only one in a thousand in the Basque Country attended a university.

And it was born of leaders driven by a passion for social justice. Don José María Arizmendiarieta was President of Catholic Action, a social service agency

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<sup>133</sup> This compared with \$696 million in fixed assets for the Community at the start of 1990. Annual Report of Caja Laboral Popular. 1990.

<sup>134</sup> T.U. Lankide. May, 1992.

formed at the end of the Civil War. So were three of the four founders of ULGOR. A sense of social christianity pervaded the private sector in the area in the 1940s and early 1950s. Indeed, one founder recently described the Mondragón effort as having "started as a sociological experiment and evolved into a business enterprise".

Today's average income, in nominal dollars, is \$13,000. This translates into a real increase in buying power since 1956 of 500 percent. In 1992 the national standard is 1770 hours. "Who doesn't own a car? Who doesn't own a refrigerator? Who can't send his children to a university?", Ormaechea asks.

Materialism has replaced idealism. Religion is a much smaller part of community life. The initial cooperative enterprises demanded a high level of personal risk by members. They invested their life savings, or borrowed from close friends and relatives in starting up a business. Caught up in the spirit of what they were trying to accomplish, the worker-owners were willing to forego immediate earnings out of a sense of solidarity and also to strengthen their own enterprises. José María Sarasua, director of Ederlan, a long time cooperative foundry, recalls, "In the beginning the cooperative made an extraordinary gesture of solidarity with the community by maintaining its clearly inadequate salary level at that of the time even though our profits would have permitted us much higher salary levels."

Such a spirit of solidarity would be more difficult to extract in today's more materialistic and less idealistic workforce. Today's entering workers assume a far lower level of risk and personal sacrifice. They are not building enterprises. They are maintaining enterprises. Sarasua worries that "the consciousness of being partners is being lost".

The economic slowdown also undermines the pursuit of solidarity. The solidarity principle, written into the Basic Principles of the Mondragón Contract of Association, is inherently expansionary. Not in the sense of preaching or proselytizing, but with respect to job creation.<sup>135</sup> Don Jose Maria Arizmendiarieta, the spiritual father of the Mondragón cooperative system, used to say that the creation of jobs not only integrates broader numbers into the cooperative life, but also is a sign that the system is competitive and healthy.

Yet since the mid 1980s, Mondragón has created few if any industrial jobs, although it has created many new jobs in the food and banking sectors. Mostly, it has been concerned with restructuring existing resources, or, in a couple of cases, in converting privately owned firms to cooperatives. The new expansion under the recently adopted business plan will be outside of the Basque County and will involve non-cooperative ventures. Thus today's workers are not participating in a rapidly expanding cooperative environment.

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<sup>135</sup> The Mondragón cooperative group has not promoted itself and its model. Indeed, it is not well known in Spain. A recent Basque t.v. crew interviewed people at the opening of Eroski's first hypermarket store south of Madrid. They discovered that the shoppers had no idea that Eroski was a Basque based enterprise, let alone that it functioned as a cooperative. One Mondragón member told me, "The Americans and British have been much more interested in Mondragón than the Spanish."

## **A Brief Review of the Evolution of the Mondragón Cooperative Corporation**

The Mondragón system has evolved from a loose collection of individual enterprises to a more coordinated collection of individual enterprise groups to a centrally coordinated, but decentralized corporate structure.

Initially, the cooperatives were tied together through their Contract of Association with the Caja Laboral Popular (CLP). The Contract of Association spelled out members' duties and obligations. The cooperative members represented a majority on the Board of Directors of the CLP.

The mutual dependence of the Bank and the industrial cooperatives was direct and complete in the early days. The Contract of Association required cooperatives to bank with the CLP. And by Spanish law and Mondragón's own bylaws, CLP could provide loans only to the cooperatives. In the late 1960s, about 75 percent of CLP's investments were in the cooperatives.

The CLP harnessed the surpluses generated by the industrial enterprises, primarily ULGOR, the first industrial enterprise, which grew from a few dozen members in the mid 1950s to a few thousand members by 1970, and channeled these surpluses to finance new business creation. Seventy five percent of the CLP loans in 1970 went to cooperative expansion. But most of the financing for expansion in the first 15 years came from internally generated capital.

For both Mondragón and Spain, the period of 1956-1976 was one of rapid economic growth. The national market was protected by tariffs and import restrictions, and large subsidies were offered to industrial firms.

Indeed, some of the original founders now say that relatively few management or marketing skills were needed to be successful in those days.<sup>136</sup> "In a market of 28 million people, poorly provisioned during almost the first 20 years, management was easy, without great burdens, and profitability flowed with abundance", observes Ormaechea. Each worker-owner's annual share of profits was equal, on average, to a 20 percent increase in wages, and in some peak years, an 80 percent increase.

The second phase in Mondragón's evolution occurred in the late 1970s. The Spanish recession forced Mondragón's cooperatives to close ranks and to develop community wide mechanisms. For three years in a row, the industrial cooperatives, as a whole, lost money. The Bank became much more interventionist. Its business division, initially established to start businesses became involved in saving businesses. The Bank booted out managers, changed product lines, merged companies, and enabled the transfer of workers among cooperatives. The Bank's business development division thus began to acquire a much broader managerial perspective.

In 1982 the Bank completed an exhaustive analysis of the structure of the Basque economy and identified important trends in global economic development. Its report became a blueprint for restructuring the cooperatives. That blueprint wasn't fully adopted until the December 1991 meeting of the Community Congress.

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<sup>136</sup> Others disagree, pointing out that many privately held firms went bankrupt or were not nearly as successful as Mondragón's cooperatives, despite the favorable national economic climate.

During the 1980s, CLP's deposits swelled far beyond the needs of the cooperative community. Whereas in the 1960s CLP was largely supported by the bigger industrial cooperatives, in the 1980s its much larger deposit base may have saved the cooperatives. The CLP wrote off \$160 million in loans, a remarkable amount given the size of the industrial cooperatives overall asset base.

In the early 1980s, as a result of changes in the Basque cooperative law, the CLP for the first time was able to offer depositors services like mortgages and car loans. This led to a major expansion in its deposit base. It also led to a dramatic diversification in its investment portfolio. Today only 15 percent of the Bank's loans are to cooperatives. About 40 percent is to non-cooperative enterprises in the Basque Country. About 45 percent consists of personal consumer loans or home mortgages.

The recession in Spain forced the industrial enterprises to seek foreign markets. The export share of total industrial sales rose from 10 percent in the mid 1970s to more than 20 percent in the early 1980s. This led the cooperatives to confront their lack of marketing skills. As one member remembers, "We were good at making things" but knew little about marketing, especially outside the region.

The 1980s saw the blossoming of several intercooperative institutions. One was the comarcales, or territorial based industrial cooperative groups. The first group, ULARCO, had been formed in 1964, but the process of group formation was significantly boosted in the recession. About 70 percent of the industrial enterprises were part of a group by 1991. Groups engaged in common marketing, common purchasing and centralized accounting and administration. By the end of the 1980s, most groups also shared part or all of their companies' profits among their various members.

The early 1980s also saw the creation of community wide institutions and mechanisms. One was the unemployment insurance fund, operated by Lagun Aro. Financed by a payroll tax, this fund primarily financed inter-cooperative transfers of personnel.

In 1984, the cooperatives formed their first community wide governance structure. The Cooperative Congress met every other year and elected a Board of Directors. December 1991 marked the third and by far the most significant meeting of the Congress. It also marked the birth of the Mondragón Cooperative Corporation.

In 1992, Mondragón's cooperatives find themselves in a different environment. Three changes stand out as particularly important.

1. The demographics of the cooperatives are changing. The founding generation is aging. Some are retiring.

Retirees are becoming more numerous. Recently they have raised the question of having representation in the Community Congress. If this were granted, they could rapidly become a significant voting force.

An older generation views history with a different, perhaps more jaundiced eye. José Agustín Arrupe, head of the engineering school observes, "When I came, people were 35 and idealistic and forward looking. Now faculty are older

and ready for retirement and are looking backward and are frustrated and critical and this affects the culture."<sup>137</sup>

A new generation, with little or no institutional memory, and a very different psychological and social attitude, is entering the managerial ranks at a time of rising income but stagnating overall employment levels. More than a third of those who work in cooperatives today were not born in the 1950s. Javier Marcos, editor of *Trabajo y Unión*, the cooperatives' magazine, describes the present generation as "more materialistic and individualistic". "We are trying to figure out how to educate the younger generation about our history." <sup>2.</sup> The advent of the fully integrated European market means that Mondragón will now compete directly against the largest corporations in the world, not only outside Spain, but in its backyard as well. In 1980, for example, domestic appliances were protected from imports by a 35 percent tariff. In 1991 it was 5 percent, and by the end of this year it will completely disappear. Multinationals are buying up key Spanish industries at a breathtaking rate, while the parent companies themselves are engaged in a frenzy of mergers and acquisitions in all of Europe. The manufacturing of domestic appliances, for example, constitutes the Mondragón cooperatives' largest single industrial sector. In recent years the number 2 and number three Spanish domestic appliance manufacturing firms have been purchased by foreign corporations (Sweden's Electrolux and Germany's Bosch-Siemens). Le Clerc, the French supermarket company, has opened hypermarket in Pamplona. In 1980 the import tariff on refrigerators, for example, was 35 percent.

3. The opening up of Europe to continental wide flows of capital and corporate concentration is occurring as a second economic slowdown hits Spain only a few years after the severe recession of 1979-1986. Basque unemployment levels in 1985 reached 25 percent. Spanish economic annual growth rates were above 4 percent in 1987, 1988 and 1989, but dropped to 2.5 percent in 1990 and to less than 2 percent in 1991. There has been no job expansion in the cooperative industrial enterprises since the mid 1980s. Markets are tight. Profits are suffering. Unemployment hovers around 16 percent.<sup>138</sup>

These three factors, and others, provided the background and context for the third convention of the Community Congress, the community wide legislative body, in December 1991.

Decisions taken at that session mark a dramatic departure from past cooperative practices. The change is best reflected in the adoption of a new name, the Mondragón Cooperative Corporation (MCC) to replace Mondragón Cooperative Group.<sup>139</sup> The basic 12 page Contract of Association, which contains the community's basic rules and obligations used to be signed with the

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<sup>137</sup> Arrupe himself now reflects this more sober attitude. "The idea is to make the least bad system possible", he tells visitors.

<sup>138</sup> On a tour of FAGOR's refrigerator manufacturing plant, the FAGOR representative was asked, "Is it a privilege to hold a job in FAGOR". She responded, "It is a privilege to have a job".

<sup>139</sup> Originally, the leaders wanted to call the new organization, *Corporación Cooperativa Mondragón* but this would have resulted in the initials CCM, the same initials as another Spanish confederation. So they chose *Mondragón Corporación Cooperativa*, whose initials, MCC, are similar to the English.

Caja Laboral Popular, the system's Bank. It will now be signed with the MCC.<sup>140</sup>

## Changing the Rules

The Congress made several important changes in the Contract of Association.

For the first time since the early 1970s, it allowed workers to withdraw a part of their profits in cash. Worker-owners can now withdraw 30 percent of their annual share of the company's profits in cash.<sup>141</sup> This year, CLP's workers voted to distribute about 5 percent of the Bank's profits in cash.

The revised Contract of Association all but eliminates salary ceilings. The limitation on top salaries had been major innovation of the Mondragón cooperative system.<sup>142</sup> Neither Spanish nor Basque cooperative laws, at the time Mondragón's cooperatives were created, required any limitation.<sup>143</sup>

From 1956 to 1973, the salary range was a maximum of 1:3 from lowest paid to highest paid. From 1973 to 1987 it expanded to 1: 4.5. From 1987 to 1991 it was 1:6. In December 1991, the Congress recommended that cooperatives allow top salaries to be as high as 70 percent of prevailing comparable managerial wages.<sup>144</sup>

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<sup>140</sup> The business division of the CLP spun off and became an independent cooperative, LKS, and is housed in the same building as the MCC headquarters. LKS will perform the audits and the other responsibilities contained in the Contract of Association that heretofore it performed as part of the CLP.

<sup>141</sup> Spanish cooperative law offers worker cooperatives a substantial tax break if they meet certain conditions. They can receive a reduction in their corporate income taxes from 35 percent to 20 percent but to do so they have to give 10 percent of their profits to charitable endeavors, and at least 20 percent of their profits must go in the enterprise reserve account. Today, most Mondragón cooperatives invest 35 percent in the enterprise reserve account. That leaves 45 percent of gross profits for individual accounts. Thirty percent of this is 13.5 percent of gross profits.

<sup>142</sup> Three other innovations on the existing Spanish and Basque law made by the Mondragón cooperatives are worth noting. 1)The creation of worker cooperatives out of consumer cooperatives. Spanish law had viewed banks, for example, as consumer cooperatives where the workers had no representation. 2)The creation of intercooperative cooperatives, like the second tier service cooperatives, CLP and the university and the research and development center. These have representatives of both workers and cooperative members on their Boards. 3)The Social Councils. These are not required by Spanish or Basque Country cooperative law. "With the creation of this organization, it has recognized that partners are at the same time workers, and as such, subject to the desire to participate in decisions affecting their work." says Juan Larrañaga, of Otalora.

<sup>143</sup> Under Spanish law, the autonomous regions, like the Basque Country, have exclusive authority over cooperatives. The most recent Basque County cooperative law, based on the Mondragón experience, does require a salary differential provision for cooperatives who benefit from tax advantages. But it does not specify the range.

<sup>144</sup> In the past the CLP established a base salary, based on prevailing entry level wages, and this base salary was considered to have an index number of 1.(The LKS, with the MCC will now

An average worker gets paid about \$1,800 a month.<sup>145</sup>

The maximum salary spread of 6 to 1 is rarely reached. Each cooperative can adopt a narrower differential and most have. Most still operate under the 1:3 or 1:4.5 rules. Indeed, since no one in Mondragón seems to be paid at the 1.0 scale (the lowest wage tends to be around 1.3) the actual range, becomes 4.3 to 1 at the widest (6 in relation to 1.3). This compares with a Spanish average of 15 to 1 in all industries, and a U.S. differential of 115 to 1.

For Spanish companies equivalent in size to Eroski or FAGOR Electrodomesticos, each with more than 3,000 workers, the salary of top management might be 22 times that of an entering worker. Under the new 70 percent rule, this means that Eroski could pay its president a salary 14 times greater than index number 1.

This spring Eroski approved the new differential. It previously had kept to the original 3 to 1 scale. FAGOR refused to approve the expanded salary range in a tumultuous meeting in May.<sup>146</sup>

The leaders of the MCC insist the new salary differentials are needed, not to attract new managers, but to retain existing managers. As with many of Mondragón's changes, this one is defensive in nature.

## Changing the Structure

The structure of the new Corporation is taking on a form that wouldn't be unfamiliar to U.S. corporations. The Community Congress, which had been meeting every other year, will now meet every year as a General Assembly. It will approve broad policies and elect the Board of Directors, which in turn will appoint top management.

MCC is divided into three major groups: finance, industry and distribution. The finance group is essentially the CLP and Lagun Aro, the social security and insurance fund. The distribution group consists of Eroski. The industrial group is further divided into 8 divisions, and into 23 sectors (e.g. car parts, domestic appliances, capital goods).

In essence, Mondragón has created a corporate structure above the existing cooperatives and is forcing them to organize themselves into the new structure.

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establish the basic salary scale.) All other salaries are given as an index number related to the basic index of 1. Currently 1.8 is the average salary in the cooperative system.

<sup>145</sup> 1.4 million Pesetas per month is wage scale I. That's equivalent to about \$15,000 per year. This is also the amount that is needed to buy into the cooperative. Of this amount, 25 percent is considered a joining fee and 75 percent goes into the enterprise's reserve capital account. If the worker left on day two he or she would receive back 75 percent. Usually members borrow this initial investment and pay it off in two to three years.

<sup>146</sup> Normally, general assembly meetings are 3-4 hours long. FAGOR's meeting took 10 hours. Reportedly, there was a confrontation between the President of the MCC, who was formerly head of the FAGOR group and is still a FAGOR member, and the rank and file. As a result of the refusal of the workers to agree with management's recommendations, the governing council might resign. FAGOR did finally approve joining the new Corporation.

The territorial based existing Grupos Comarcales, is being replaced by a sectoral basis for association. By the end of June 1992, all cooperatives were supposed to enlist in a sector.

This reorganization is onerous, complicated and painful. For example, there are 8 cooperatives that make plastic parts. Some of them make parts for cars. Others don't. Which should become part of the plastics fabrication sectoral group and which should become part of the automotive parts sector?

Cooperative groupings will be split up. FAGOR, for example, has 9 individual cooperatives under its group umbrella. Those cooperatives that work in plastic might be in a different sector from those that make iron products. Mikel Lezamiz, a sociologist at Otalora says, "it is a constant debate" about which sector an enterprise will join.

Many cooperatives are signing up very reluctantly to the new reorganization plan. Some think that their willingness to accept the new situation is less out of enthusiasm than out of desperation. The stagnating economy makes them open to new ways. One official predicts, "If the economy improves they might well oppose the new structure".<sup>147</sup>

Everyone agrees that there is a need to substantially reduce in number the current 90 odd industrial cooperatives. Some envision each of the 23 sectors of the industrial division eventually becoming single cooperatives,<sup>148</sup> using the evolution of FAGOR as an analogy. ULGOR formed the first group, ULARCO, in the mid 1960s. It was a loose arrangement, mostly for sharing overhead and some marketing costs. In the mid 1980s Ularco became FAGOR. FAGOR consisted of over 14 cooperatives that engaged not only in common marketing around a common brand name, but in substantial profit sharing among its members. In the late 1980s FAGOR's central management office, with about 70 members, itself became a cooperative, the only case where this has happened in a group.

Meanwhile, within the FAGOR group, FAGOR Electrodomesticos was born out of five existing cooperatives. Some of the production facilities of the individual cooperatives, moved into a single building complex in Mondragón and produced refrigerators, dishwashers and other appliances. The former cooperatives lost their individual identities. Each former cooperative within Electrodomesticos no longer has its own plant manager, nor its own Board of

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<sup>147</sup> Some territorial orientation might be retained. For example, one member of Otalora suggested that workers transferred from a money-losing enterprise to a profitable enterprise might not necessarily be forced to go to another enterprise in their own sector if it is a long commuting distance. However, the receiving firm will have to pay for the costs of retraining the worker, and these costs may be higher for a firm not in the specific sector.

<sup>148</sup> Each sector will probably have its own research and development arm. Currently only the machine tool cooperatives have their own R&C Center, the only such facility in Spain. Ikerlan is the R&D branch of the entire cooperative system. In the future sectoral R&D branches will focussed only on the needs of their sectors, while Ikerlan, which already does a significant amount of contract work with outside companies, will do more broadly oriented R&D.

Directors, although it still has its own Social Councils. FAGOR Electrodomesticos has become, in effect, a single cooperative.<sup>149</sup>

MCC also expects to dramatically reduce the number of products its enterprise members offer. The cooperatives currently produce 800 different products. This might be pared down to 200-300, while retaining their most profitable lines.<sup>150</sup>

Merging companies, breaking up and reconstituting enterprise groups, reducing product lines, extending brand names, all involve a massive reorganization of resources, a reorganization that can be accomplished only with the approval of each individual cooperative.<sup>151</sup> Jesús Larrañaga, one of the founders of the Mondragón system, and currently the head of AENOR, the Spanish standards institute, because of his great prestige, has reportedly been given the primary task of working with companies to effect this transformation.

The effort required to bring about this dramatic restructuring has led MCC to "close its doors" for the next 2 to 3 years, in the words of one official from Otalora, to either new cooperatives or the conversion of private firms.<sup>152</sup>

## Striving for Economies of Scale

Mondragón's leaders believe that the new single European market demands an increased scale of operation, particularly with regard to marketing. "Size now constitutes an important factor in success, but it can only be achieved by establishing alliances with other enterprises, and these are not going to be, they could not be, cooperatives", says Ormaechea. José María Larrañaga, an engineer with Otalora insists, "Small companies cannot compete". Lezamiz agrees, "It is clear that we cannot compete with 40-60 member cooperatives".<sup>153</sup>

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<sup>149</sup> The other individual cooperatives in the FAGOR group have retained their own Boards of Directors and plant managers.

<sup>150</sup> In those product sectors where a full product line is important for marketing purposes, MCC might enter into agreements with private firms to jointly market their products under a single brand name.

<sup>151</sup> Although the pressures on the reluctant cooperative will be very strong. For those cooperatives that don't agree with MCC's reorganization plans, the alternative is to leave the system and compete on its own.

<sup>152</sup> However, Saiolan, the entrepreneurial training institute, has as its objective to start enterprises. It doesn't give degrees. Its students do not have to create cooperative enterprises. So far they have began 13 businesses of which 7 are cooperatives, although by far the largest number of jobs have been created by the private firms.

<sup>153</sup> MCC has large individual enterprises: CLP has 1,300 worker-owners, Eroski has 3,000, FAGOR Electrodomesticos has 3,000, Ederlan has 900, but 60 percent of the worker-owners belong to cooperatives with 80 to 100 members. Some believe that the five or six small agricultural cooperatives might be closed and their workers absorbed into Eroski. These cooperatives have always been small. Most of the Basque Country is not conducive to raising livestock. The vast majority of milk sold in Eroski is imported from France. The Mondragón leaders point out that Europe is already suffering from an agricultural surplus, and European agricultural policies are moving toward reducing this production in a variety of ways. Thus, since several of the

To achieve a sufficient marketing scale, manufacturing enterprises are entering into joint ventures with private firms. In 1990, Mondragón exported about 40 percent of its capital goods and expects this to rise to 50-70 percent by the mid 1990s. To position itself for this type of expansion, FAGOR, whose workforce represents 40 percent of the total industrial workforce of Mondragón's cooperatives, has developed joint agreements with European appliance manufacturers.<sup>154</sup> An agreement with Thomson and Hot Point will include common marketing and distribution, a sharing of technical knowledge, and a division of product production. FAGOR will make hot plates for Thomson and also refrigerators. Presumably Hot Point and Thomson will drop their own production of these products. It is rumored that FAGOR will stop producing dishwashers.

This belief in the need to expand and the willingness to take on private partners in order to be able to do so, also characterizes the distribution sector. In 1990, 7 of the 10 largest Spanish supermarkets were multinationals. Antonio Cancelo, president of the Eroski Group notes, "It is not difficult to foresee that within a few years, 6-8 companies will control 60-80 percent of the total market. Not to form part of that privileged group of companies would signify accepting an increasingly marginal role...To adapt means to lose something and one must be conscious of that; but not to adapt implies a more painful loss: disappearance."<sup>155</sup>

Eroski, in association with Consum, a Valencia based cooperative, has established a holding company, called CECOSA. Eroski owns 70 percent; Consum owns 30 percent. CECOSA, in turn, owns 51 percent of a subsidiary, EROSMER. The rest of EROSMER will be owned by other Spanish financial institutions.

EROSMER will own 51 percent of each store; 49 percent will be owned by a variety of investors, the primary one being ONCE, the Spanish non profit organization of the blind.<sup>156</sup> Three percent of the shares in the individual stores will be owned by the managers in those stores.

The Eroski Group has established geographic divisions: North, East, South and France and Portugal. In France, Eroski is developing joint ventures with a French cooperative.

Eroski expects to triple sales from 1990 to 1993 and to almost double its workforce. In the spring of 1992 Eroski opened its first hypermarket in Ciudad Real, south of Madrid. By 1995, it expects to have 48 new hypermarkets. This year, expansion investments will be three times expected profits. A key element of Eroski's expansion is that it will be done on a non-cooperative basis.

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agricultural cooperatives have been only marginally profitable, and since there is no major growth potential in the sector, the MCC might shift these resources to another area.

<sup>154</sup> FAGOR has 35 percent of the Spanish refrigerator market, but only a 1 percent share of the English market.

<sup>155</sup> JARDUN. January/April 1992.

<sup>156</sup> ONCE gets most of its money from a national lottery. It has enormous investment capital, and is the target now of criticism because it is still a tax exempt organization.

Grupo Eroski is legally structured as a Sociedad Anónima, a private firm, not a Sociedad Cooperativa.

The financial, group, which consists of more than \$3 billion in deposits from CLP and a billion dollars in investment capital from Lagun Aro's pension funds, has established a Sociedad de Cartera, an investment holding company, which will enter money markets and buy shares of companies. The newly formed financial group is also looking into major real estate development ventures, maybe as part of Eroski's expansion. Lagun Aro, the social security and insurance affiliate has entered into a joint venture with FILO, a real estate development company in Catalonia, to finance and build these immense "leisure centers", with areas of 200-300,000 square feet.

Mondragón's decisions to enter into agreements with privately owned firms for the first time is based on its belief that it must achieve even greater size to compete in future global markets. Officials at MCC do not seem to believe they need to expand their size in order to improve their purchasing economies of scale nor even their engineering scale economies. Their enterprises are already of sufficient size that their buying power allows them to obtain about the lowest price possible. Eroski is a very big business. It has 45 percent of the food market in the Basque Country, and sells 18 percent of that region's consumer goods. It has its own slaughterhouse, and owns one of only three automated warehouses in Europe.

FAGOR sells 35 percent of all Spanish refrigerators. Mondragón produces 25 percent of all Spain's machine tools. Its foundries, in sum, are the third largest in Europe.

There is some worry that Mondragón's enterprises have a lower productivity compared to international competitors and this could hurt them in foreign competition.<sup>157</sup> But it isn't clear that getting larger would result in more rapid productivity improvements than are now occurring. The FAGOR refrigerator manufacturing facility, from 1987 to 1991, for example, had a 40 percent increase in production while reducing its work force by about 20 percent. Ederlan, Mondragón's largest car parts manufacturing, was recognized by General Motors as its best European supplier last year.

The specific justification offered for getting bigger is to gain greater marketing clout. There are two ways to use this clout. One is positive, having the ability to widely market a single brand name. The other is negative, having the ability to pressure suppliers not to sell to one's competitors.<sup>158</sup> Eroski, for example, notes that the French hypermarket company, LeClerc, has just opened a store in Pamplona. It fears that LeClerc could enter into contracts with British or Dutch producers, whereby LeClerc, in return for guaranteeing these producers access

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<sup>157</sup> Ormaechea has observed that their productivity ratios, measured by value added, "are lower than those achieved by German, Italian, French by each industrial job, and considerably behind Japan." T.U. Lankide. May 1992.

<sup>158</sup> This can be done by obtaining an exclusive contract with a supplier, or by exercising market power to prevent a competitor from having access to certain products. For example, in the U.S., Pillsbury told stores that were buying its Haagen Daz ice cream that they could not also stock Ben and Jerrys.

to the entire Spanish market would receive an exclusive contract to sell their produce.<sup>159</sup>

With respect to Eroski, there is another reason for increasing in size, and that is for it to offer the one stop shopping centers that are claiming an increasing amount of the food and non-food market. According to Eroski, 25 percent of all domestic appliances are sold in big, multi-purpose centers already in Spain. An ever greater portion of its store sales are in non-grocery items, so to compete its stores must become larger.

Eroski has expanded into maxi stores, with 25,000 square feet, and very recently, into hypermarkets with as much as 100,000 square feet. This will "cannibalize", in the words of a top manager at Eroski, some of the 200 existing small stores which now have an Eroski franchise and use the name Erosle. These are neighborhood stores which use Eroski's purchasing power to stay competitive.

Eroski, for example, established a maxi store on the outskirts of Mondragón and two years ago began a free bus service, on the hour, which toured the city, picking up shoppers. The bus ride is free to the maxi store, but to get back on the bus one needs a receipt, showing one has purchased something. About 10 percent of the maxi store's total customers use the bus. People tend to shop in corner stores, within walking distance of their homes. This takes business away from these stores. Eroski's manager acknowledged this, but also pointed out that the Erosle workers will be transferred to Eroski stores.<sup>160</sup>

### **Loosening the Cooperative Bonds, Opening Up the Cooperative System**

Mondragón's cooperative system, once completely self-financed, populated only by worker-owners, and serving virtually only the Basque market, is now opening up to new forces. Its boundaries are becoming more and more permeable. A growing percentage of its workforce are not worker-owners. Its financing is coming from outside the cooperative system, and even from outside the Basque Country. It has entered into joint ventures with privately held companies, and many of its new ventures will be outside the Basque Country and will be structured as privately owned ventures. Profits, once generated almost entirely derived from worker-owner labor, may soon be substantially derived from financial investments.

Mondragón members told me that some visitors have gone away thinking that the Mondragón experiment is dead. That seems a premature judgment, but it is true that in the future the experiment will be taking on a very different form and dynamic.

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<sup>159</sup> Eroski has reportedly told suppliers that it will no longer carry their merchandise if they sell to Pamplona.

<sup>160</sup> From the perspective of these workers, given that they will now be cooperative members, this could be a step up. But if they were formerly owners of the Erosle franchised stores then this might be a step down.

The loosening of the bonds of cooperation and community is evident in many areas.

1. Most new jobs, even within the MCC, are being created outside the cooperative heartland in and around the city of Mondragón.

In Mondragón, about 40 percent of the total workforce works in cooperatives, while in Bilbao or San Sebastian the figure is probably closer to 1-5 percent. New worker-owners are thus more removed, not only from interaction with members who have a long institutional memory, but also from interaction with various parts of the cooperative system.

2. The influence and role of the Basque Government has expanded considerably. This both strengthens and weakens the Mondragón system.<sup>161</sup>

The 1978 Constitution brought democracy to Spain and autonomy to several Spanish regions. In 1982, the Basque Government signed a contract of autonomy with Madrid, and during the 1980s more and more authority was delegated to this government. One key development is that the autonomous regions have exclusive authority over cooperative law.

The Basque government now controls most of the taxes generated within its region. This substantially increases its financial clout and reach. The Basque government now finances and manages Mondragón's health and educational system. Ikerlan, the R&D cooperative, receives 47 percent of its funds from the Basque government.

This outside assistance has returned a slice of the tax revenue generated by Mondragón back to its service system. But it has also led to a greater dependence on outside policy decisions.

With regard to education, the Basque government offers three types of public schools. One is taught in Spanish only, one is bilingual (Spanish-Basque) and the other is Basque speaking only. The Ikastolas are Basque speaking schools, originally developed as part of the cooperatives. Some are still cooperatives but most are not. They are also subject to the changing policies and funding levels of the Basque government.

A few weeks before I visited Mondragón the Basque Minister of Education, a member of the Basque Socialist Party, had given a speech indicating that English was a more important language to learn in the Basque public schools than Basque. This led to an uproar, and they have signed petitions with 20,000 names to have him removed<sup>162</sup>.

Basque governmental decisions will clearly have a growing influence on Mondragón's evolution. The Basque government has exclusive authority over

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<sup>161</sup> For the first 20 years of cooperative development, the Basque Country had no political authority and was discriminated against by the Franco regime. The majority of taxes generated inside its boundaries was not returned from Madrid, or was returned in a form that was incompatible to the needs of the region. For example, a significant amount of funds were returned to the Guipuzcoa province in the form of financing for the Spanish police force, a military force that many in the province believed was an army of occupation.

<sup>162</sup> Lagun Aro reportedly had established a cooperative hospital in Mondragón in the early 1980s as part of an expected expansion into direct medical delivery services, but this was abandoned as the Basque government took over this sector. The medical system in Mondragón is not organized as a cooperative.

changes in the cooperative law. It also has asserted a growing role in regional economic development activities. It may be that a symbiotic relationship will evolve between the Basque government and the MCC. This is already occurring. José María Ormaechea, one of the founders of ULGOR and the president of CLP until 1988 is now president of the SPRI, the Basque industry development arm. Alfonso Gorroñoitía, also one of the founders of ULGOR and the CLP is president of the Basque Federation of Worker Cooperatives.

The Basque Prime Minister, Ardanza, was a former mayor of the city of Mondragón and a legal adviser to the CLP and is still a member of the CLP. When asked what he thought the role of the MCC would be in the formation of the Social Economy of the Basque County, Ardanza recently described the MCC as "the fundamental tractor for the rest of the Basque Social Economy."

The Basque Country has developed its own aggressive economic development strategy in the face of renewed recession and the single European market. The Basque government was heavily involved in MCC's buyouts of two private firms: Luzzuriaga and Fabricec. Both are car part manufacturers and both were near bankrupt. Luzzuriaga is a large enterprise. Both were targets of foreign purchasers. To defend a locally owned manufacturing capacity, the Basque government provided financing and an exemption from pension and other liabilities, to the MCC.

3. The sectoral groups will weaken the community basis for enterprise association, and this longer distance may weaken the bonds of association and the willingness to sacrifice for one another. Mondragón's cooperatives were initially linked to one another only through their Contract of Association with the CLP. In 1964 ULGOR and its suppliers formed ULARCO and in the 1980s, FAGOR, and by the late 1980s, most cooperatives were part of comarcales, or territorial based cooperative groupings. Many of these pooled their profits as well as their marketing and purchasing and accounting divisions.

The new sectoral foundation for MCC will rend these territorial relationships. It may also reduce the initiative for profitable firms to divert their profits to other firms. Within the community groupings, firms rarely directly competed against one another. But in the new sectoral groupings there may be a great deal of direct competition. A wood furniture cooperative in Vitoria that is profitable might be reluctant to share its profits with a money-losing wood furniture manufacturing cooperative in San Sebastian, 60 miles away.

4. Mondragón has in some degree been based on the assumption that its members would be dependent on the fruits of their own labor. Today MCC has set in motion decisions that might change this. Eroski's new venture, for example, in the long term might generate substantial profits to Eroski's worker-owners. These will be profits derived from other people's labor, people who are not owner-members. The new financial holding company will also generate profits derived from other people's labor. The financing company is expected to invest heavily in real estate development, and also, conceivably, in currency markets. Thus a larger proportion of total profits might be derived from land appreciation, currency exchange rates, direct investments and other people's labor.

5. The MCC's new structure removes management further away from the shop floor and substitutes representative democracy for direct democracy with regard to important business policy decisions.<sup>163</sup>

Examples of representative democracy have occurred before. The second tier cooperatives are example. For example, in the CLP, all workers have the right to attend the General Assembly, but cooperatives elect representatives.<sup>164</sup>

The Community Congress has, since 1985, been a community wide representative legislature, but only now is it becoming the legislature for a corporation. The change in its reach and function is indicated by the fact that it will now meet annually rather than biennially.

How will representative government change Mondragón? It will probably mean broad policy decisions will be made by those who are more active and better informed. It may also mean that decisions are made more from a managerial than a shop floor basis.<sup>165</sup>

6. The rise in the number of non worker-owners who are working in the cooperatives may also loosen the bonds of cooperation. For most of its history, Mondragón had very few contract workers.<sup>166</sup> Ormaechea has noted, "even 15 years ago, it was inconceivable to have a worker who was not a partner in the cooperative and in 1969 various cooperatives...were not permitted to associate with the Caja Laboral Popular, that is to say, with the Group, because they had some workers who were not partners." Now the cooperatives depend on a temporary, contract work force as a buffer against the business cycles and the tight economy. "Today, the tightness of the market, and the cycles of demand, have convinced us that in order to safeguard the cooperatives and to assure permanent employment, we should have at least 10 percent, or 2000 workers on temporary and external contract." For the first time, workers in the

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<sup>163</sup> It is hard to say how often worker-owners actively participate in decision making. Certainly there is real power given to the Social Councils and the General Assembly. Social Councils are required for all cooperatives with more than 50 members, and Social Councils comprise as many as 50 people, who meet monthly and are actively involved in most of the important immediate worker concerns (e.g. plant safety, work schedules, pay, etc.). General Assemblies are open to all workers. There is reportedly a high participation rate. However, a few cooperatives deny members the right to vote in a succeeding general assembly if they did not attend the previous one.

<sup>164</sup> The size of the General Assembly is increased as the number of workers is increased, in order to maintain the proper ratio. For example, in 1992's Assembly there were 2571 attendees, 1271 worker-owners and 1300 others. If the CLP workforce grows, the number of outside cooperativists would also increase.

<sup>165</sup> Evidence of this might be the difference in the voting on the issue of maximum salaries by the Congress and the FAGOR rank and file. By the necessary two thirds vote, the Congress agreed to change the basic rules of the community to abolish the old salary differential scales. But FAGOR, which represents 40 percent of the industrial workforce couldn't muster the votes to approve this. It is possible that FAGOR's votes were overwhelmed by votes from the service cooperatives (Eroski and CLP), or it might have been that FAGOR's representatives at the Community Congress were more managerially oriented than the rank and file that elected them.

<sup>166</sup> Spanish and Basque cooperative law prohibits enterprises receiving tax benefits from having more than 10 percent of their permanent workforce as non-members.

cooperatives can work without investing their own money, that is, without assuming a risk and without being full participants.

The acquisition of private firms may exacerbate this tension. Fabriltec, for example, a car parts manufacturing enterprise, was acquired recently by FAGOR. It will eventually be converted to a cooperative but its lower managers currently earn more than top managers at FAGOR. Luzurriaga, a major car parts manufacturer, will retain not only its private firm status, but its union as the representative of its workers.

7. The newly expanded range of salaries could undermine the sense of solidarity between workers and management. The Third Congress also agreed that not only the highest salaries should be established at the sectoral level based on sectoral comparability but the base salaries as well. This makes sense from a market perspective, but again, undermines the solidarity of the cooperative system.

8. The Bank is no longer the hub of the system. Tying enterprises to a source of financing and requiring them to use the bank was a practical way to tie the system together. The hub was also the engine and the source of financing. Now the Bank is expanding beyond the cooperatives. Indeed, only 15 percent of its funds are invested in the cooperatives, although the vast amount of money to date is still invested in the Basque region, either as business or consumer loans.

The Bank may soon begin to move away from the other cooperatives in another sense. The workers of the CLP have already stopped relying on the metalworkers' wage and hour agreement as the basis for their own, as is the case with other Mondragón cooperatives, and has instead adopted the bank unions' agreement. Banking hours tend to be more consistent with their sector, and it makes sense for them to move in this direction, but it also means that there is less unity and uniformity among the cooperatives.

In 1992 the CLP workers requested that they be given equal representation on the Board of Directors, rather than the one third that is currently the case. That was voted down by their General Assembly, but the argument may have increasing validity, since the direct link between cooperatives and the Bank is much weaker now.

## **Conclusions**

The MCC is an attempt to harness the resources of the entire cooperative system in a way that will allow it to achieve the scale necessary to compete with global firms and in global markets. At the same time, it wants to allow for sufficient autonomy among the enterprises, and to encourage maximum participation and solidarity. These goals are often not harmonious. The corporate form is, in some ways, a way to further bind the Community together, given the centrifugal forces that have been at work on it.

One key way to bond the Community together is the institution of mandatory, system wide profit sharing as part of the Basic Principles.<sup>167</sup> This was adopted by the December 1991 Congress.

After July 1, 1992, profit sharing will occur among sectors and among divisions. The sectoral share will be a minimum of 10 percent and a maximum of 35 percent share of cooperative profits. The divisional level will be a minimum of 5 percent and a maximum of 20 percent. The overall limits on profit sharing will be 15 percent minimum and 40 percent maximum.

Those sectoral groupings which share 100 percent will be exempt from these provisions.

It will be interesting to see how or whether the Mondragón cooperatives favor one another more under the corporate form than they did as a federation. Throughout their history, except in the closely knit groups, the cooperatives have never favored one another for contracts or purchases. Eroski, for example, carries mostly non-cooperative brands, even when competing products are available within the cooperative system. Until six months ago, for example, Eroski did not carry FAGOR appliances, but did carry German and British appliances.

Cooperatives must be competitive. Mondragón believes that the individual cooperative must live or die based on strict marketplace criteria. On the other hand, it has created community wide mechanisms, like intercooperative transfers, the unemployment insurance fund, and the intercooperative solidarity reserve fund, and now, the profit sharing plan. These protect or at least minimize the pain of the market to the worker, although not to the enterprise.

The Mondragón cooperative system increasingly looks similar to some decentralized U.S. corporations (e.g. Johnson & Johnson). However, there is a key difference. The MCC is ultimately owned by its workers and these worker-owners not only have ultimate say at the top management level, but significant participation and influence at the shop floor level, through their Social Councils. The tension between workers as employees and as owners has characterized all of Mondragón's history.

In this regard, a recent story might be instructive. Last year Fagorelectrodomésticos discovered that most of its sales were in the last half of the year. But the 4 week August holiday, and several mid summer and early fall national holidays means that its workforce might well have 5 weeks off in the second half of the year. Management proposed to the workers that it take a week of these holidays in the first part of the year to mesh production with customer demand more closely. The General Assembly, as is its right, refused, preferring to continue the old way. The workers were viewing themselves as employees.

A year later the workers reviewed their decision and changed their minds. Management had done more education, and the workers themselves had realized the validity of management's position. The General Assembly reversed its previous decision. The workers were viewing themselves as owners.

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<sup>167</sup> Javier Erdozia, Secretary General of the MCC has called this part of a "renewed sense of the necessity of strengthening the cooperatives' cohesive links". T.U. Lankide. January 1992.

This healthy and inevitable internal tension between two roles, and two perspectives, is now complicated by other tensions. Workers are now, for the first time, owners of external productive capacity that has employees but not worker-owners. Thus a conflict begins to arise between channeling surpluses within the enterprise into more cooperative expansion or into more investments in private firms.

The division of authority between MCC's top management, the individual enterprise management, the sectoral management and the divisional management, is still evolving. One person envisioned that the sector would decide whether to sell refrigerators in Russia, while MCC top management would decide whether to produce refrigerators.

MCC has established a 3-4 year time frame for it to work out the final details in its new corporate organization. Many decisions have yet to be made, from the strategic investment plan for the new financial holding company to the specific sectoral groupings, to the scope of authority of divisional heads.

It is an important moment in Mondragón's cooperative development. Its members have responded to changes in the external environment in ways consistent with their historical inclination toward pragmatism and flexibility. They are trying to re-invent cooperativism for the 21st century. Whether they will succeed is something no one can predict.

## **Building A Mondragón Type Cooperative in the United States**

It is easy to be pessimistic about the chances of developing a Mondragón type cooperative system in parts of the United States. The soil here is peculiarly infertile for such an experiment.

---Unlike Basque society, ours may be the most individualist in history. Cooperation itself is often perceived as unamerican.

---Unlike in Spain, a cooperative community in the United States would have little or no special support from the federal government.

---Unlike in Spain, start up and small manufacturing enterprises here would have no protection against global competition

---The U.S. lacks laws similar to those in Spain that discourage cooperative members from undermining cooperative principles. For example, most worker cooperatives, over time, tend to hire a significant portion of their work force as non-cooperators. The initial workers become eventual owners. Also cooperative enterprises in the U.S. have the right to sell or liquidate their assets and divide up the proceeds among individual members, an attractive proposition in cases when the value of the plant is high and the enterprise faces difficult economic prospects.

---U.S. communities have many strong leaders, but few have the staying power, vision, the entrepreneurial spirit, and the

association with community based institutions that command respect(i.e. the Church) as did Don José María Arizmendiarieta.

----Few communities in the United States have the binding characteristics of Mondragón: linguistic, geographic, cultural.

----The Mondragón Cooperative system evolved over many years, behind protective tariffs, insulated by language and geography, able to make mistakes and learn from them. In the United States, there would be few protections in infancy. The Cooperative system would have to be developed more fully and faster, than was the experience in Mondragón.<sup>168</sup>

The two key elements in Mondragón's structure was its significant manufacturing base and its central bank. Industry came first. By 1960 there were half a dozen industrial cooperatives and almost 400 industrial workers. ULGOR itself had over 200 workers by 1960, and over 3,500 by the early 1970s. It acted as the Community's economic development engine, generating surpluses that were used to finance new enterprises, and acting as an internal market for enterprises making intermediate industrial components. The Bank therefore was able to begin with substantial enterprise funds, and as a second degree cooperative that made it a subsidiary to the enterprises.

The U.S. experience with cooperatives has been largely with consumer cooperatives in which the workers have no authority and in which surplus is paid to the customers in the form of dividends or rebates.<sup>169</sup> There are a growing number of worker owned firms through the creation of Employee Stock Ownership Plans (ESOPs), but these do not operate under the cooperative rules that have made Mondragón so successful. There is no cooperative bank in the United States that is community based and oriented.<sup>170</sup>

Thus, if a bank were the first cooperative enterprise established, as would be likely in the United States, it would be autonomous, with no links to existing enterprises. Given its initial lack of capital, its investments, as with most community banks, would tend to be in housing or office or small retail enterprises. After the initial startup, lending might extend to small industrial facilities.

Given these obstacles, what might be a strategy for creating a Mondragón type cooperative system in the United States? The first step would be to identify the best type of host community. Inner city neighborhoods in industrial communities are one possible host community, especially if they have some linguistic or cultural affinity, and if some of the enterprises are already worker owned. The difficulty is that neighborhoods are completely permeable. Thus they operate in an environment in which all other enterprises lack their structure

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<sup>168</sup> Yet it is also true the the Mondragón cooperative created its fundamental elements relatively quickly. By 1960 it had all of the basic pieces in place: manufacturing, bank, social security, technical education.

<sup>169</sup> When the Mondragón Cooperative began, there were consumer cooperatives in the community, and consumer cooperatives were not part of the original vision. In the 1960s, the existing consumer cooperatives asked to associate with Mondragón, and Eroski was born. Consumers become members of Eroski by paying a few pesetas more on their original purchases. This does not give them voting power. They do not receive dividends.

<sup>170</sup> Some banks, like the Farm Credit Banks, are cooperatively owned, but these have neither the community base nor the governance structure that would make them models for a Mondragón type cooperative system.

and their members can easily move from the cooperative to the non-cooperative sector.<sup>171</sup>

Another attractive host community might be Indian reservations. These tend to lack the industrial base, but they have a cultural affinity, increasing amounts of local autonomy, and some centralized control over various community activities(e.g. education, economic development). The recent entry of many tribes into income generating pursuits like casinos means that, unlike in most of their history, there is a source of revenue that could capitalize a bank and an entrepreneurial function.

A strategy to create a Mondragón type cooperative probably cannot and should not be designed as an incremental strategy, beginning with one piece of the puzzle and adding other pieces later on. It is clear that the Mondragón system cannot be transferred in whole to a U.S. community. Our history, culture, and legal and economic systems are so very different. On the other hand, the basic Mondragón structure has proven remarkably capable of adopting to changes in its external environment. That flexibility may mean that an American community could transfer significant pieces of the Mondragón bylaws and Contracts of Association and amend them as the need arises.

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<sup>171</sup>"The potential for cooperatives is greatest when applied to regional development. The anonymity of a larger urban environment and the closeness of alternative reference groups" diminishes that potential. Bradley and Gelb, "Cooperative Labour Relations", Op. Cit.