The "Soeharto Plan" of Share Owning Cooperatives: Possibilities and Limitations

Jochen Röpke

1. The "Soeharto Plan"

In his budget speech in January and in a meeting with leading Indonesian businessmen in March 1990, President Soeharto has asked the private sector to provide up to 25% of their capital (equity) as shares to cooperatives. This "Soeharto Plan"[1] has initiated a lively debate in Indonesia about the conditions, consequences and mechanisms for cooperative ownership of private and governmental (BUMN) companies.[2]

After initial hesitation, big companies, mainly Chinese controlled, have responded favorably. Just after half a year since the proposal they agreed to sell nearly 30 million shares with a nominal value of about US$ 16 million to cooperatives. About 40% of these shares will go to cooperatives of company employees.[3]

All of the bigger business groups have by now provided shares to cooperatives but a lot more are willing to follow the President's "instruction".[4]

While the remarks of the President have generally been interpreted by the Indonesian public as a "suggestion" (imbauan), some understand it as an "instruction", which has to be implemented.[5]

One motive for the "Plan" seems to have been the President's wish to defuse some of the criticism levelled against Indonesia's small but economically dominant ethnic Chinese minority[6] and the rapidly expanding business interests of the President's children.

In the Indonesian discussion, the Plan is connected with ideas about Indonesia's future economic order (Economic Democracy, Pancasila Economy) and the need for a "structural (= non-capitalistic) transformation" of the economy. According to one of the main proponents of Demokrasi Ekonomi - Edi Swasono - workers have a right to own shares in their firms; consequently they must be provided shares at prices substantially below their market value.

Two years before President Soeharto's address, Sri-Edi Swasono, the adviser to the President and head of the Indonesian Cooperative Council (DEKOPIN) has stressed the importance of employee share ownership in an Demokrasi Ekonomi (See Swasono, 1988, pp. 38-40).

In our following analysis, we discuss some of the more fundamental and farreaching aspects of the Soeharto plan, by trying to answer three questions:

1. What are the consequences of capital participation of workers/employees in their own or other companies?
2. How can capital ownership of employees be realized?
3. What role can "cooperatives" play in a transformation of capital ownership?[7]

As we shall see, no easy answers evolve from our discussion. Many topics - as the intensity of competition, the propensity to take over other companies and merge, profit sharing, industrial democracy and participation - are intimately connected with share ownership. A careful evaluation of these aspects will be necessary to prevent negative unintended repercussions.

While questions (1) and (2) have been discussed from time to time in the academic literature, the link up of share ownership with cooperatives seems to be an Indonesian peculiarity, which, as we will show, increases the difficulty of implementing sensible solutions to an already complex problem.

2. Attractions and problems of employee share ownership

Let us consider the situation of an ordinary employee in a company. This company is growing and prospering. As compensation for his work, the employee receives a salary and perhaps some other benefits as health insurance. The owners of "his" company become rich. Some day, they open the firm to the public by selling part of their equity to new shareholders. How valuable "the" firm really has become, the employee realizes, astonishingly and angrily, when the owners, for a nominal capital of Rp. 100, realize 1000 Rp. from the public, an agio of 1000%.

The dramatically increased visibility of wealth made possible by the public flotation of companies on the stock exchange, following the deregulation of the Indonesian capital market, seems one factor responsible for a renewed criticism against economic policy, a widening inequality in the distribution of wealth and increasingly ethnic Chinese businessmen.

For ordinary Indonesians, it is indeed difficult to understand how a firm with a nominal capital of say 500 Mill Rp. can float its shares for 10-times this value on the bourse. Within three years after deregulation, the number of companies quoted on the Jakarta exchange has quintupled.

Why, we may ask, the companies have not offered any shares to their employees, who dedicate their life to the firms, who are willing and eager to improve their skills, who are investing in their own - human - capital, for the benefit of themselfes, but also for the benefit of the companies.

If employees own part of the equity of a company, which employs them, they not only would become richer, their "assets" would increase, the distribution of assets would become more equal; they would also receive an additional income (dividends), and not to forget, they would feel not only proud because they work in a good company, but because they now own part of it. They would feel stronger motivated to work hard, improve there skill and increase their knowledge. If the company prospers, they will prosper also. But what, if the company fails, despite the dedication and hard work of its employees? They may loose not only their job, but the value of their shares will decline, and can become even worthless. Generally speaking: employees may find their jobs vanishing at the same time that their employer's earnings and hence the value of their shares are likewise declining. Employees face the double risk of loss of income and assets.

"I have told you so", is the response of the clever economist, "never put all your eggs into one basket." In technical economic language, that means "diversification of risk", an aspect rarely mentioned by advocates of employee ownership and similarly missing in the Indonesian debate.

"Employee stock ownership increases workers exposure to risk from fluctuations in the fortunes of their companies. Even without equity ownership, the wealth of most workers is poorly diversified because it's largely in the form of human capital tied to the success of their employers."[8]

But employee ownership may provide other advantages. With wider employee ownership, workers can demand a more active role in corporate governance, one example being decisions concerning take-overs and restructurings of firms. For instance, Polaroid Corporation in the United States succeeded in killing off takeover attempts by raiders and predators with the help of the shares of the company (15%) owned by Polaroid's employees.

Also Becker mentions this point - onesidedly - by stressing only the interests of the government: "ESOPs (employee shareownership plans) often become a management tool to fend off unfriendly takeovers and other efforts to oust current managers".

But what is wrong with this idea, we may ask? Why employees should not have a right to codetermine (the Germans call it "Mitbestimmung"), whether and to whom a company is sold. Employees may wish to support those of the managers, who want to manage the company in the long term interest of all stakeholders (the employees, the managers, the suppliers and buyers, and the owners), and not those asset strippers who are interested primarily in shortrun profit-making, in breaking up the company, selling its pieces, including the workers to the highest bidder, if only the price is right.

So we can conclude: If workers own part of the equity of a company, this is good as a takeover defense, and generally, as a right to participate in decision-making.

Unfortunately, this conclusion may not be universally valid. Japanese companies, for instance, are seldomly taken over (merged with) other firms. They have become vital competitive forces by internal growth. And Japanese employees own seldomly shares in their companies. So even without owning equity in their companies, Japanese employees can and do participate actively in decision making. The management is consensus oriented. It does not view itself as the agent of the owners and would never allow the company to be taken over, without asking the employees.[9]

3. Employee share ownership and cooperatives

A "company owning democracy", employee share ownership, should appeal to all shades of political opinion apart from that minority which still clinge to public ownership and bureaucratic socialism as offering the best world to the problems of the productive economy. But the promoters of employee share ownership have had to battle hard to win support for their ideas. The early supporters of ESOPs (Employee share ownership plans), as Louis Kelso, who pioneered employee ownership in the United States in the 1950s, argued, that ESOPs strenghten capitalism by attacking and breaking up the closed system of finance which concentrates wealth. The wealth distribution function of employee ownership of equity seems also to be a central aspect of the Soeharto Plan. "Demokrasi Ekonomi", says Prof. Swasono, "has also to be considered as an approach to prevent economic autocracy and economic kleptocracy."[10]

From our discussion so far, three main objectives of employee share ownership can be distinguished:

1. a more equal distribution of assets by spreading capital ownership;
2. greater performance of companies by motivating work-forces and participation;
3. take over defence: employee ownership induces companies to grow internally by innovation and competence enhancement.

In our subsequent analysis, we will treat only the first two objectives, despite our conviction, that in the long run, the third objective will be of equal or even greater importance concerning the performance of a company.[11]

Objectives (2) and (3) can only be realized, if some of the equity of a company is owned by their employees. The first objective does not need the identity of owners and employees.

Share distribution schemes exist in all capitalist countries. They have found their widest acceptance in economies with powerful capital market institutions. In the capital market based financial system of the US, it is estimated, that about 10 million workers are covered by employee ownership schemes. New research shows that employees have more than $ 150 Billion worth and control an average 12% of the 1000 largest US firms whose employee shareholdings exceed 4% (Bernstein 1991). In credit based financial systems as in Japan or the European continent, they are of less importance, for two reasons: 1. Companies are more controlled by their credit monitoring banks and less by shareholders; 2. participation of employees in the decision-making of their companies is institutionalized independently from the employees' ownership of equity in their companies.

It is therefore no historical accident that the recent serious proposals for redistributing the equity capital of Indonesian companies, culminating in the Soeharto Plan, come after the deregulation of the Indonesian capital markets and after the take off of the Jakarta Stock Exchange, whose capitalization has zoomed from $ 250 million to $ 7 billion within the last three years.

What is the connection between employee ownership of shares/equity and cooperatives?

The answer to this question depends critically on a meaningful definition of "cooperative". In Indonesia, this is a sensible, even political endeavour. In the following, we will employ a definition commonly found in the microeconomic theory of the firm and in cooperative science, but seldomly used in Indonesia. Our definition may therefore not cover the various other meanings of "cooperative" found in the Indonesian discussion and tradition, but nevertheless seems unavoidable to prevent confusion, ambiguity and essentialist reasoning.[12]

What differentiates a cooperative from other forms and types of organization? In a cooperative, the owners of the enterprise are also (or are identical with) the customers or users of the services or production of that same enterprise. Cooperatives are user-owned (and: ideally also user-controlled) businesses, that distribute benefits on the basis of use (not ownership). People form a cooperative to provide themselves with a needed service. If customers own a firm, their objective is not to profit from their ownership of the firm as investors, but as users of the services provided by their firm. The owners of a firm we define as a cooperative can be its customers (as when peasants buy fertilizer), or its suppliers (as when producers sell their shoes to a distributor they own), or employees (as when workers are employed, and derive advantages from their employment - for example not to be dismissed in a takeover - in a firm they own).

These distinctions and definitions are of utmost importance to understand and clarify the consequences of employee and cooperative ownership of companies.

Let us assume, employees of firm A own 100% of the equity of firm A. According to our definition, we could consider this firm as a pure (100%) cooperative (a producers or workers cooperative). If the employees own 25% of the equity, the cooperative nature of the firm would accordingly be reduced, being only a "25%"-cooperative (this simplifies of course, but in principle, the argument is still valid). The same holds, if shoeproducers would own 100%, or 25% etc. of the distributor of their shoes. But what happens to the cooperative character and extent of a firm, if not the employees themselves, but a cooperative of the employees (a koperasi karyawan, 'Kopkar') owns the equity of the firm A?

Kopkar A, itself 100% owned by the employees of firm A, owns 25% of firm A. What type of organization do we now have? Kopkar A can be without difficulty identified as a cooperative, a cooperative of investors, whose members are employees of the company in which it has invested. Makes the fact, that a cooperative of investors, whose members are also employees of the firm which they own (with 25%), the firm itself a cooperative? Not necessarily, as we will argue. Even in the case Kopkar A would own not 25%, but 100% of the equity of firm A.

Because, in our case, the members of the cooperative are at the same time also employees of the firm, we may still consider the company itself as being to some degree a cooperative. The reason is of course, that the members of the cooperative are identical with the employees of the same firm (we do not assume, that all employees are also members of the cooperative).

Let us consider another case: Kopkar B owns 100% of company B. Let us assume further, that 10% of the employees of firm B have become members of Kopkar B. In other words: Kopkar B owns 100% of the equity of company B in which members (10%) and nonmembers (90%) are employed. As the case demonstrates, even a 100% cooperative ownership does not make the owned firm itself a cooperative. 90 percent of the employees being nonmembers of the cooperative, the company can be considered overwhelmingly (90%) investor-owned and controlled. It depends therefore on two factors, to what extent a company can be considered a cooperative: On the number (percentage) of employees owning equity in their firm and on the percentage of shares owned by the employees (see table for more examples).

Table: Cooperative degree of a firm (in percent)

% of employees who are member	% of shares owned by Kopkar 10	25	100
10	1	2.5	10
50	5	12.5	50
100	10	25	100

The cooperative ownership of a firm does not make the firm in which it has invested necessarily a cooperative itself. If Kopkar Astra buys 25% of Unilever Indonesia, this ownership remains a pure capitalist investment, and Unilever stays a pure capitalist firm, even if all employees of P.T. Astra are members of Kopkar Astra. Cooperative ownership of a firm does not change the capitalistic nature of a firm - and of an economy.

Let us imagine an economy, whose equity capital is to 100% controlled (owned) by cooperatives. Despite this total cooperative control, the economy could remain or even become 100% 'free fight'-capitalistic.[13] Cooperative ownership in itself does not make an economy more "cooperative" at the level of production of goods and services.

And cooperative ownership in itself does not "harmonize" conflicting interests within a market economy. The interests of employees in firm A may to some extent overlap with those of the members of a cooperative of employees (Kopkar A), if and when the ownership of firm A by Kopkar A is seen by the members of the Kopkar not as a capital investment per se but as a means to better control an participation in the firm A in the interests of the members. Assuming a given equity stake of Kopkar A in firm A, the more employees of firm A will enter the Kopkar A the more dominant will be the need of the members as employees and not as investors; or the bigger will be the common interest; the Kopkar will gradually transform from a cooperative of investors (concerning its equity participation in A) into a cooperative of workers.

It is of course possible, and may even be highly beneficial for the members interest, if Kopkar A also is taking out equity participation in other firms, but in this case, the needs of the members will be guided - concerning their equity stakes in firm C, D, and so on - by their expectations as investors.

If Kopkar B owns a stake in firm A, or vice versa, the relationship becomes more complex. By assumption, the equity of firm A owned by Kopkar B has to be seen as a investment. Members from Kopkar B expect to profit from their equity in A as shareholders/investors/speculators.

The fact, that Kopkar B is cooperative, does not change this reasoning. The employees of A will expect and treat Kopkar B as external owners of their company, with interests as investors different from their interest as employees.

The relationship between Kopkar A and Kopkar B will overwhelmingly be one of competitors: firstly, their respective members are competing against each other with the products produced by their firms;[14] that means, Kopkar A and B will compete against each other to the extent that they are workers cooperatives (and not cooperatives of investors); secondly, they compete as cooperatives of investors in the capital market. Their succes in both areas of competition will determine the attractiveness for new members (assuming open membership).

In both fields of competition, Kopkar A and B may have some common interest as pressure groups (to seek more favourable legislation, tax privileges and so on in their function of workers and investors cooperatives).

The overriding difficulty of a cooperative restructuring of ownership remains the potential for conflict between the role of being a cooperative of workers (increasing the welfare of members in their role of working employees) and the role of being a cooperative of investors (increasing the welfare of members in their role of investing employees).

This structural conflict is difficult to be resolved because it is built into every single Kopkar, which invests in their own firm.

The main suggestion of the "Soeharto Plan" can therefore mean several things:

1. ownership of the economy by cooperatives to a higher extent;
2. the restructuring of the economy according to cooperative principles in the production and distribution of goods and services.
3. the internal transformation of firms by empowerment of employees to initiate improvements and change in their interest.

To implement the first suggestion (or instruction) is a necessary but by no means sufficient condition for realizing the second objective and as the Japanese and German example demonstrate, not even a necessary condition for the third objective. At least in theory, cooperative ownership could strengthen the capitalistic, free-fight nature elements in the Indonesian economy, moving it further away from UUD 1945, pasal 33.[15]

The reader might rightly ask, why it does make a difference at all if equity is owned by cooperatives, instead of by individual employees or the general public.

Providing shares to the individual employees would be the direct way to provide stronger cooperative incentives. Providing equity to a Kopkar may result in a thinning out of the cooperative impact at the firm level, since the cooperative will represent the members in their interest of owners and not in their interest as employees. The decisions taken by the Kopkar will deviate from the decisions taken by the employees respectively their decision-making organs. Only if the interests of the employees would be identical with that of the owners, we could expect otherwise. Providing shares to the general public including employee cooperatives of other enterprises would contribute to "democratize" equity-ownership, but the new shareholders would be ordinary investors.

The main objective of a cooperative of employees owning shares in other enterprises, i.e. a cooperative of investors, is to satisfy the needs of its own members and these needs can definitely be different from the needs of the employees of the company in which the Kopkar has invested.

An interesting question, which has to be answered positively by those who want to provide incentives and facilities for those employee cooperatives investing not in their own company, is, whether cooperatives of investors can provide any additional or comparative advantage than other organizations engaged in the capital market (investment trusts, mutual funds, investment/ merchant banks, and others). What could be the causes for comparative advantages of cooperatives of investors? To answer this question would be the stuff for a new paper.

So long as we do not know the answer to this question, there can be only one way to find out; let cooperatives of investors freely compete with other institutions. The competitive process of discovery will find out and select the more efficient organizations. This of course requires, as Christianto Wibisono has rightly stressed,[16] deregulative measures from the Indonesian authorities. The cooperatives must be free to enter the capital market. Because cooperatives are new players in this area, it may, under specific conditions, be economically wise, to treat them as an infant industry.

We are sceptical, that the authorities will follow this approach. Traditionally, the Indonesian government, and the public, have seen in cooperatives more a social and political institution than an economic solution to predominantly economically caused problems. Government intervention and regulation of the cooperative sector have more often than not hampered initiatives by cooperative entrepreneurs.[17]

All Indonesian proposals we are aware of, concerning the roles of cooperatives in the capital markets, do not even consider the idea, that cooperatives could also be self-help institutions.[18]

4. The dilemma of employee share ownership

After discussing some of the more definitional and typological difficulties connected with the recent proposals to restructure the Indonesian economy on cooperative lines, we have now to come back to the fundamental question: How can employees, by owning equity in the company they work with, improve their economic welfare?

Any improvement has to result from the cooperative organization of employees, either directly (by using elements of a workers cooperative, as in a ESOP); or indirectly, by making use of a cooperative of employees (koperasi karyawan) within but seperately from the firm.

That these two cooperative institutions must be carefully distinguished we have discussed at length.

We are limiting our analysis intendedly to one but crucial aspect of the Soeharto Plan. In the discussion, following the President's appeal, the scope of cooperative involvement has been continously extended, culminating in the proposal of Prof. Swasono[19] to use the impetus created by the President in the area of cooperative ownership of companies for a fundamental uplifting of the role of cooperatives in general:

- Employees own shares in their own companies (the ESOP model);
- Cooperatives of employees own shares in their own companies (the Kopkar model);
- Cooperatives of employees own equity in other firms (the investment trust model);
- KUDs and other non-worker cooperatives own equity in other firms (investment trust model);
- Cooperatives of producers own shares of suppliers and/or sellers of their members products (vertical integration "keiretsu" or foster parents/bapak angkat model).

Can a worker improve his economic welfare by becoming a co-owner of the firm which employs him?
Can a cengkeh (clove) farmer get better prices and other advantages by becoming a co-owner in a cigarette factory?
Can a shoeproducer sell more shoes and/or at higher prices by co-owning the retailer/distributor which markets his product?

Generally speaking: How can we demonstrate, that by owning part of a company, with which I am engaged in contractual relations (as a worker, buyer, seller, consumer, saver, investor, and so on), my economic welfare will improve?[20]

If we can demonstrate how/why this is possible, it will make sense to ask by what mechanisms the potential increase in welfare can be realized.

Our main topic will be, as stated, to show, how the ownership of shares/equity can improve the welfare of employees. We leave for further discussion the question, how cooperatives of producers or consumers can improve the welfare of their members by buying equity in related or unrelated firms.

At the core of share ownership plans for employees (ESOP) is the idea that the benefits of growth be shared between the employer and the employees. By making the workers owners they can share in the growth and they will have a strong economic incentive to make the business successful.

There is no question that equity ownership allows workers to participate in the creation of wealth to which they as employees contribute.[21]

But share ownership makes employees bearers of entrepreneurial risk in addition to the employment and income risks they face in their role of workers. The same holds for profit sharing contracts, proposed by Becker and others[22] as a superior solution.

Can we provide employees a more equal participation in wealth creation and at the same time prevent, to some extent, to burden employees with entrepreneurial risks they are not well equipped to bear?

We see two ways to overcome part of the dilemma. The first way consists in conventional diversification of assets: employees own equity in the firm which employs them, but in addition own shares in other, if possible unrelated companies (for every 1000 Rp. invested in their own firm they invest a similar amount in a well diversified portfolio of shares).[23]

The second solution needs a fuller analysis.[24] Every firm is confronted with uncertainty/risk. We can split up this risk into two components, according to its sources; uncertainty can be caused by exogenous or environmental factors, or it can be caused by factors internal to the firm, especially by the firms entrepreneurs/innovators.

The first risk is environmental: changing prices of input and output, governmental regulation and intervention. The second type of uncertainty results from entrepreneurial/innovative activity. It can be eliminated only be eliminating economic development. The negative side of true uncertainty is what Schumpeter called "creative destruction": products, markets, companies are destroyed by innovative competition, while new markets, firms and technologies evolve. To protect workers against the forces of creative destruction, welfare institutions who provide displaced (jobless) workers with assistance, are needed.

How can companies and their workforces adapt to environmental risk?

If environmental factors turn more positive for a company (for example better prices for its products, lower prices for raw materials), the company will prosper, independently of the entrepreneurial contribution. Workers can participate in the good fortune of their firm in two ways:

If they own shares, their value may rise and the workers' assets increase; and workers can participate in higher wages/salaries. It is important for our argument, how workers participate with higher incomes:

a) Employees receive an increase in their basic salary.
   (Problem: will the salaries decline if the company environment becomes unfavorable?)

b) Employees participate in profit sharing.
(Problem: profits result from changes in environmental and entrepreneurial uncertainty; the contribution of the last is difficult to calculate; with profit sharing, employees are burdened with entrepreneurial risk.)

c) Employees receive a bonus payment.[25]
(Advantage: calculation of bonus is rather simple, because it is independent of entrepreneurial influences; the bonus can be adapted to environmental conditions, and reduced to nil if the external conditions worsen.)

We are able now to distinguish between several alternative systems of an employee share-owning economy:

System A:
Employees own shares in firms which employ them; as a consequence, they face high risks for their equity and human capital invested in the firm; they are burdened with external (environmental) and internal (entrepreneurial) uncertainty. This is the system now discussed and implemented in Indonesia.

System B:
Employees own equity in their own company and receive bonus payments in addition to their core salary.

System C:
In addition to owning equity in their company and receiving bonus payments, the employees reduce their exposure to risk by investing in other firms.

System D:
In system D, equity investment is again combined with bonus payment, but employees do not buy equity in their own or other firms directly, and immediately, but acquire a share option i.e. the right to acquire shares at some future date. System D is, as we have argued elsewhere (Röpke 1990c), most suitable for cooperative self-help, but will not be discussed here in detail.

The systems which combine equity with bonus allow employees to participate in the wealth created by their companies: but in addition, these arrangements reduce the risk of severe human capital and equity capital destruction which is due to non-foreseeable environmental uncertainty. The reasons for a reduced risk are attributable to the bonus scheme, which in itself is a risk sharing contract between the employees and the employers/owners. If the environmental conditions should deteriorate, the workers share part of this risk by accepting a lower bonus payment. This gives the company, which is co-owned by the employees, a better chance to adapt and to survive. In the short run, the flexible adaption to environmental change made possible by the bonus scheme can prevent a more serious reduction of the value of the assets owned by the workers (declining share price, unemployment); and in the long run the assets of the workers will be higher than without a bonus system.[26] The sharing of the exogenous risks associated with price and other environmental uncertainties will result in more stable profits and the equity of the company becomes more valuable for external investors, which provides additional advantages for the assets owned by the employees.

The reduced variability of a firm's performance will - by reducing the risk for external lenders - also lower the cost of the debt.

The larger the bonus in total employee compensation, the lower is the cost of equity and debt capital of a firm.

Unfortunately, the evolving Indonesian practise will have the opposite consequences.

The compensation and wealth sharing plans now contemplated in Indonesia (provision of shares at nominal value, payment with interest-free loans provided by the firm) will tend to increase the employees' risk and the cost of capital for the companies.

The first consequence may be negligable at the moment: Because of gratis disbursement of equity employees do not risk their own money. The increasing cost of capital will be real, and will tend to weaken the international competitiveness of the Indonesian economy and specifically reduce the relative ability to compete of the share distributing conglomerates (mainly Chinese controlled) vis-a-vis the pribumi sector of the economy.

The increasing cost of capital results from three interacting characteristics of the presently practised implementation of the Soeharto-Plan:

1. Shares are provided to employees below market value. With the pattern now beginning to be practiced - provision of shares at nominal value - the equity cooperatives of employees receive and have to pay for, has a market value 5 to 10 times higher. A share with a nominal value of Rupiah 1.000 could be sold to investors in the capital market for between Rp. 5.000 and Rp. 10.000. In other words: with every Rp. 1.000 share given to employees, Rp. 4.000 to Rp. 9.000 of financial funds are lost for the company, funds which could have been used to finance current production, expansion, acquisition of assets or retiring outstanding debt.
2. By distributing equity capital to their employees at nominal value companies, in need of finance capital, have to use other - higher - cost sources of funds.
3. When the share acquisition by cooperatives is financed by loans from the company, these are burdened with the difference between interest rate for loans (in Indonesia in recent years between 20% and 30% p.a.) and the interest charged to the cooperatives (in most cases nil).

The system of share acquisition by cooperatives now beginning to be installed in Indonesia is therefore

a) a method of gratis disbursement as seen from the cooperative
b) whose costs are born by the companies, and
c) the general public, who has no access to cheap/gratis equity but will be burdened with the higher costs and prices charged by the firms.

We can summarize our argument so far: Share ownership allows employees to participate in the wealth created by their companies, but at the cost of high risk to the value of their equity and human capital assets invested in their firms.

These risks can be substantially reduced if the employees are willing to share in the exogenous risks associated with output price and input cost uncertainties. A bonus system allows this type of risk sharing, if the returns from entrepreneurial risk-taking are excluded from the conctractual arrangements.

By giving workers the chance to participate in wealth creation, they must be willing to share in the external risks. Even in the short run, this can result in greater income stability, but also in a lower probability of losing their jobs. The bonus scheme will result therefore in higher security of the workers core income. The per saldo positive income and asset contributions of such a scheme can be further improved by adequate tax incentives (lower tax rates on bonus income relative to core income).

5. The contribution of cooperatives

One major reason for the existence of cooperatives is their ability to reduce uncertainty for their members. But owning equity in a firm which employs you, either directly (workers cooperative) or indirectly (cooperative of employees, kopkar), will increase the uncertainty (variability) of your income and assets substantially.

If your real income and the value of your assets is still low, you will probably be risk averse. Your incentives to buy shares in your company may for good economic reasons be weak.

What could it make attractive for you to enter a cooperative of employees (Kopkar)?

If the cooperative distributes to you equity of your company "free of charge", the preferred Indonesian solution, you would, no doubt, like to participate. But not with your own money.

Are cooperatives of employees as self-help organizations (not as lembaga karitas) doomed to failure?

All the proposals concerning the implementation of the Soeharto Plan seem to assume this implicitly. Where does the money come from to buy shares? Definitely not from the (prospective) members. Solutions based on the self-help of the member-employees seem to be ruled out:

- companies are assumed to give away shares to their employees gratis, more or less;
- companies provide equity with a lower price than its market value (the difference could be used to back part of the loaned funds etc.);
- state enterprises (BUMN) channel part of their profits to cooperatives in order to enable them buying equity;
- debts of private companies with government banks are switched into equity, which is then provided to the cooperatives (Wibisono);
- firms are subsidizing employee equity buying through low interest loans.

This list is for illustrative purposes only and not exhaustive. It may well be remembered, that the ESOP arrangements in the US are critically dependent on tax privileges to companies, employees and the financing banks. Tax advantages are also available in the United Kingdom and in Germany for employee share buying schemes.

In the solution now evolving in Indonesia, a company will give the cooperatives open-ended, interest-free loans to buy the company's shares. The loans will be repaid from withholdings of future dividends. The cooperatives will not be allowed to trade the shares until full payment has been made.

If our argument contains some merits, the modest interest of employees and their cooperatives to acquire equity, in their own companies, with their own means, i.e. via individual or cooperative self-help, is not surprising.

Providing external funds or other privileges to the cooperatives may make them attractive for members, but only by destroying their souls: self-help activity.

In Indonesia, there exists a substantial number of primary savings and credit cooperatives, whose memers are company employees. I am not aware of any, who has voluntary become involved in share transactions on behalf of its members.[27]

The difficulties of relying on pure cooperative self-help in acquiring shares are evident. Since this type of cooperative tries to promote member interests by common self-help, the members may have no interest in acquiring equity in their own company - with their own money. If they prefer to diversify their assets and if they have more rewarding alternatives for their funds, their action is easy to understand.

In addition, the prospect of receiving equity, more or less at no cost ("free shares"), will kill off any incentive for cooperative self-help. And without cooperative self-help, the Soeharto-Plan will not only increase economic inefficiences in the Indonesian economy but lead the economy - as is demonstrated elsewhere (Röpke, 1990c) - further away from the goal of distributive justice, so prominent in recent Indonesian discussion concerning a more equal distribution of economic wealth.

Jalan keluar: Solutions

To make equity owning cooperatives at the company level viable organizations based on self-help will require to make them attractive to employees, and this requires to make equity ownership attractive to employees.

In general, simple systems of equity ownership (system A) may not achieve this and may do more harm than good.[28]

The introduction of more complex schemes (systems B, C, D, equity/-options/bonus) seems necessary. If such arrangements are adopted, the role of cooperatives could definitely augmented.

But we do not have to be dogmatic about this system B. If employees see advantages in owning equity, they will be willing to provide their own resources. If they are willing to contribute, self-help based cooperatives can exist, if they offer their member-employees additional advantages. If not, what is the reason for their existence?

The potential role of cooperatives could consist of

- monitoring and eventually managing the employees equity position in his firm or in other companies he or the cooperative has invested;
- providing the members with information on investment alternatives;
- arranging the financing (savings, loans).

Since contractual arrangements which include equity and bonus-payments may improve the incentive structure of an employee substantially, his greater willingness to provide resources and to participate will improve the chances for cooperative self-help.

A rich field for cooperative ventures would be opened up, which could result in rapid accumulation of members and cooperatives assets.

Savings and loan business extending to house financing and insurance could be done under one cooperative roof. There is no guarantee, that a cooperative of employees can handle these tasks. Cooperatives outside a company or non-cooperative institutions may perform better and should be allowed to do the job. Cooperatives have a right for existence, when they satisfy the needs of their members. But this to decide is up to the members themselves.

The diversification problem can be overcome by allowing Kopkars the acquisition of equity in other companies, or the acquisition of a bundle of shares, for example in form of a unit trust or mutual fund. In the field of small volume share transactions, cooperatives may even possess a comparative competitive advantage.

For those who prefer a more rapid redistribution of corporate assets based on cooperative self-help, the second possibility, the deferred acquisition of equity via share options may offer a promising route.

To make the Soeharto Plan successfull then does require:

1. an extended reform of employee compensation at the firm level;
2. a further deregulation of capital and financial markets in order to give cooperatives a right to compete;
3. the deregulation of the cooperative sector itself, to give cooperative entrepreneurs better chances to come up and implement ideas, which satisfy the needs of prospective members better than available alternatives;
4. if these conditions are met, there are no reasons, why, in order to create a share owning economic democracy, the government should not provide special incentives for all parties willing to engage themselves in such a social contract;
5. but: no external help either by companies or the government should be made available if not substantical self-help by the employee (or other kind of) cooperative is coming forth. As Raiffeisen, the European cooperative pioneer once said: "Better no cooperative, than a bad cooperative" (Besser kein Verein, als ein schlechter Verein).

Bibliography:

Aoki, Masahiko: **Information, Incentives, and Bargaining in the Japanese Economy**. Cambridge: Cambridge University Press, 1988

Barney, Jay B.: "Profit Sharing Bonuses and the Cost of Debt: Business Finance and Compensation Policy in Japanese Electronics Firms", **Asia Pacific Journal of Management**, 7 (1990)1, pp. 49-64

Becker, Gary S.: "Esops Aren't the Magic Key to Anything", **Business Week**, October 23, 1989, p.10

Bernstein, Aaron: "Employee Ownership: Joe Sixpack's Grip on Corporate America", **Business Week**, July 29, 1991, p.48B-E and 48C-E

Buletin BK 3 (Jakarta), (1990)1, p.7: "Rat Koperasi Karyawan P.T. Indocement"

Editor, 31.03.1990, Berita Utama, pp.11-24

Far Eastern Economic Review, August 9, 1990, p.57: "Indonesian Firms Agree to Transfer Shares"

Grubel, Herbert G.: "Capitalism Needs Risk-, not Profit-sharing", **Kyklos**, 40(1987), pp.163-175

Hülsmeier, Christan: "Betriebsfonds: Unternehmen fördern Vermögensbildung", **Wirtschaftswoche**, Nr. 17, 20.04.1990, p.144-146
Kompas, 15.03.1990: "Penjualan saham ke koperasi sesuai pemikiran Bung Hatta"
Kompas, 21.03.1990: "Laba BUMN untuk koperasi agar dihimpun dalam lembaga"
Kwik Kian Gie: "Koperasi karyawan perusahaan", **Kompas**, 12.03.1990, pp.IV, V
Mubyarto: **Sistem dan moral ekonomi Indonesia**. LP3ES Jakarta, 1988
Reuter, Dieter: "Rechtliche und rechtspolitische Probleme der Mitarbeiterbeteiligung", **Betriebsberater: Zeitschrift für Recht und Wirtschaft**, (1990)11, pp.713-726
Röpke, Jochen: "Cooperatives in a Pancasila Economy", **Prisma** (The Indonesian Indicator), (1984)34, pp.67-82
Röpke, Jochen: "Externes Unternehmenswachstum im ökonomischen Evolutionsprozeß", **ORDO**, (1990a)41, pp.167-189
Röpke, Jochen: "Deregulasi dan Kewiraswastaan Koperasi", **Kompas**, 07.05.1990b
Röpke, Jochen: **Growth with Equity: Cooperatives and Employee Share Ownership**, unpublished mimeograph, Marburg 1990c
Swasono, Sri-Edi: **Demokrasi Ekonomi: Komitmen dan Pembangunan Indonesia**, Jakarta: Penerbit Universitas Indonesia 1988
Warta Ekonomi, II(16. Juli 1990)7, pp.22-34: "Setelah Tapos, Apalagi untuk koperasi"
Weitzman, Martin: **The Share Economy**, Harvard University Press 1984
Wibisono, Christianto: "Dari Marshall Plan ke Soeharto Plan", **Kompas**, 20.03.1990a
Wibisono, Christianto: "Dari 'Go Public' ke 'Go' Rakyat", **Kompas**, 21.03.1990b

Notes:

1) See Wibisono 1990a.
2) See for instance Kwik Kian Gie 1990; Wibisono 1990a, 1990b; **Editor** 1990; **Kompas** 1990; **Warta Ekonomi** 1990.
3) **Far Eastern Economic Review**, 9.8.1990, p.57.
4) See **Warta Ekonomi**, 4.2.1991, p.16, for specific data, and names of companies
5) "...according to me, its more than a suggestion. Its more, consisting of an instruction, which cannot not be implemented" (Sri-Edi Swasono); for the citation see **Kompas** 15.03.1990, p.1.
6) In 1988, the turnover of Indonesia's 10-largest, Chinese controlled conglomerates was equivalent to 15% of Gross National Product. The largest, the Salim Group, controlled by Liem Sioe Liong, accounts for 5% of Indonesia's GNP. While the Chinese account for 2.8% of Indonesia's population, they own 75% of private (non-governmental) assets. (**Warta Ekonomi**, 1.10.1990, p.15; **FEER**, 27.08.1991, p.58; **The Economist**, 10.08.1991, p. 52).
7) For reasons of space, we concentrate our analysis on "workers cooperatives" or koperasi karyawan - 'Kopkar' (cooperatives of employees), well knowing that other types of cooperatives, as KUDs (Koperasi Unit Desa; village cooperative), are part of the intended scheme of restructuring capital ownership in Indonesia. Entitled for reciving shares are, according to the Department of Cooperatives (**Kompas**, 2. Juli 1990, p.8) KUDs (6000), Kopkars (457), cooperatives of government employees (2150), industrial cooperatives/Kopinkra (387), youth and student cooperatives (51) and cooperatives within the Armed Forces /ABRI (135), which together are about one fourth of all registered cooperatives existing and with exception of some Kopkars belong to the group of "officialized" (government assisted, connected and often managed) cooperatives.
8) Becker 1989.
9) In Japanese companies (and to a somewhat lesser extent in Germany), the enterprise-based union has acquired substantial bargaining power over strategic managerial issues as employment and relocation. According to Aoki (1988, p.153), in the Japanese firm, "considerably wide issues are subject to explicit and implicit consensus making." In Germany most companies provide their employees with shares in their companies (Belegschaftsaktien) at - compared to the market valuation - substantially reduced prices, and additional tax privileges are available. But compared to the rights from "codetermination" and the rights obtained by the "Betriebsräte" the influence of employee share ownership in decision-making is insignificant. According to § 71 AktG, Belegschaftsaktien are not allowed to exceed 10 percent of the equity capital. As an example, at Deutsche Bank, 2,9% of the equity was owned, 1990, by employees (**Frankfurter Allgemeine Zeitung, Blick durch die Wirtschaft**, 30.03.1990, p.3). For a discussion of the problems of employee share ownership in Germany see Reuter, 1990.
10) Citation in **Kompas**, 21.03.1990, p.2.
11) This aspect has been discussed extensively by Röpke 1990a.

12) For a discussion of these points see Röpke 1984.
13) 'Free fight capitalism/liberalism' is a term often used in Indonesia to describe a free (liberal) market economy. See for instance Mubyarto 1988, p.114.
14) Quite often, there is a misunderstanding on the relationship between cooperatives and the intensity of competition, in the sense, that by patterning relationship more "cooperatively", the intensity of competition declines, and the economy is somehow transformed in a more social and equal direction. Generally speaking, this is not the case. If cooperatives attain a comparative advantage in their specific field of action, competition may well intensify. Many examples can be cited, one being the intense competition between Japanese companies, which are inside themselves "cooperatively" structured to a degree not found anywhere else in the economic world.
15) According to article 33 of the Indonesian Constitution of 1945, "Economic affairs are to be organized as a joint effort (usaha bersama) based on family principles (asas kekeluargaan)", what generally is equated in Indonesia with cooperatives (for a discussion see Röpke 1984).
16) See Wibisono 1990b.
17) See Röpke 1990b.
18) For an extensive discussion of the consequences of primarily external help instead of cooperative self-help see Röpke 1990c.
19) See **Kompas**, 21.03.1990, p.2.
20) We are always assuming, of course, that the contractual relations are those of a cooperative, of which the individual is a member. Our question therefore is: What is the comparative advantage of cooperative membership?
21) To what extent employees contribute to wealth creation at the firm level is an open theoretical and empirical question. Following Schumpeters theory of economic development, new wealth is ultimately created neither by the owners (capitalist) nor by the workers, but by the entrepreneur/innovator. Since entrepreneurs are the driving force of development, denying them a substantial part of the new wealth created by them may reduce their incentive to innovate. This has happened in all known systems of bureaucratic socialism and cannot be ruled out if employee ownership is pushed too far. How to provide incentives for innovators is the main and unsolved problem of workers cooperatives. A trade-off between economic development and a more egalitarian distribution of wealth surely exists. But about its magnitude we know little. Connected with this difficulty, and a possible solution to it, are cooperative patterns of venture capital financing.
22) See Becker 1989; Weitzman 1984.
23) West German companies have recently ventured into this field providing their employees - in addition to Belegschaftsaktien - company tailored investment funds (Hülsmeier 1990).
24) For a good discussion, see Grubel 1987; Aoki 1988; Barney 1990.
25) A bonus plan is any compensation plan, where employees are paid a sum of money in addition to base (core) salary. The size of bonuses vary as a function of either the performance of an entire firm and/or as a function of the performance of a particular employee.
26) A good demonstration for the beneficial working of a bonus system is provided by Japanese firms. Up to 50% of an employee's income can consist of bonus payments. Because of these "flexible" wages, Japanese firms can guarantee a high level of job security (permanent employment), which again increases the incentives of employees and firms to invest in human capital, resulting in a higher level of competitiveness, and so on.
27) A case in point is the Kopkar of P.T. Indocement, the biggest Indonesian cement producer, with around 2000 members and assets of 500 mill. Rupiah (for a report on this cooperative see **Buletin BK 3**, 1990, p.7).
28) There are exceptions to this conclusion for firms where the employees have many possiblities to damage the owners by making careless use of the assets provided to them (transport firms are good examples). Not astonishingly, the most successful ESOPs have been in this field; by making the users of the asset (for example a taxi, a bus) also its owner, a careless use of the asset will damage the user (the driver) in his role of owner.