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INDUSTRIAL CO-OPERATIVES IN JAPAN ^{1/}

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^{1/} The views and opinions expressed in this paper are those of the author
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Background of Co-operatives

In Japan, small enterprises (they are usually called small and medium enterprises) are defined as: (1) manufacturing or mining establishments having a paid-up capital not exceeding ¥100 million or having not more than 300 regular employees; (2) wholesale mercantile enterprises with a paid-up capital not exceeding ¥40 million or having not more than 100 regular employees; (3) mercantile or service enterprises with a paid-up capital not exceeding ¥10 million or having not more than 50 regular employees.

In 1971, small establishments accounted for over 92.4 per cent of manufacturing establishments, around 49.2 per cent of the value of shipment and 35.5 per cent of exports, and provided employment to around 68 per cent of workers engaged in manufacturing. Small establishments usually suffer from smallness of capacities, lack of modern technology and lack of creditability. Assistance measures taken are designed to improve techniques of production, rationalize business management and strengthen bargaining power. However, public efforts to assist small enterprises are apt to become spare and ineffective on account of the gigantic number of small enterprises, namely 788,619 in manufacturing in 1972. The efforts are aimed at the elevation of the structure of small enterprises according to industry to a higher level of development through business mergers or collectivization of business activities and at the promotion and elevation of the structure of small enterprises up to their optimal scale through the organization of small enterprises into co-operatives.

In line with these policies, the Law of Co-operatives Association of Small and Medium Enterprises and the Law Concerning the Organizational Structure of Small and Medium Enterprise Organizations have been in force since 1949 and 1957, respectively. The former law was enacted with the purpose of securing the economy of scale by grouping small enterprises into co-operatives and the latter law

make the basis for small businesses - in the same line of trade and operation - to promote and coordinate their activities by themselves or by joint industrial and service trade organizations.

A special administrative organization, Agency in the Ministry of International Trade and Industry, handles general matters related to small enterprises and their organizations. In specific terms, in order to promote and coordinate the economic growth of small enterprises, the Agency is conducting various activities. The Agency plans and coordinates the financial and technical support given to economic and financial support given to enterprises. It also offers subsidies for personnel and operational expenses to the National Federation of Small Business Associations which is the main organization for giving direction to the small enterprise organizations. In principle, the actual supervision of small enterprise organizations is assigned to the local branches of the Ministry and Prefectural Government which understand more exactly the real needs of small enterprises. Applications concerning licenses to establish small enterprise organizations are generally handled by them.

The institutional organizations for fostering collective activities by small enterprises are roughly classified in two groups: (1) co-operatives and (2) commercial and industrial trade associations. Co-operatives are further classified according to the differences of their objectives and structure. These co-operatives and trade associations are ruled with some exceptions by some basic principles, that is open membership, democratic control, limitation of capital return and patronage refund payments. Co-operatives and associations can be organized at the proposal of more than four persons. The number of co-operatives and trade associations in Japan at the end of March 1972 were as follows:

Common-facility co-operatives	37,794
Common-facility special co-operatives	36
Federations of common-facility co-operatives	606
Joint-enterprise co-operatives	4,998
Fire mutual-relief co-operatives	39
Credit co-operatives	524
Joint-business co-operatives	833
Commerce and industry trade associations	1,696

Common-Facility Co-operatives

Common-facility co-operatives are composed of a group of establishments engaged in the same industry or trade or service, which agree to co-operate in undertaking one or more specific functions and, except for these functions, continue to operate independently. One of a total of 37,774 common-facility co-operatives in 1972, 11,402 were in manufacturing. The coverage of these co-operatives is quite extensive. Of the small establishments engaged in manufacturing, about 40 percent were covered by these co-operatives. In over 70 percent of the co-operatives, members do not belong to the same type of industry or trade. Membership per co-operative is not large. In a little over 65 percent of the cases, membership ranged between four and fifty.

Among the functions of these co-operatives, joint purchases and joint selling are most important. Next in importance is the provision of loans or the assistance in securing loans. The provision of joint welfare services and information, agency services for members and joint production or processing activities are also important functions of common-facility co-operatives.

Even goods are sold individually, arrangements may be made jointly for inspection and stamping of approved products and a common trademark. The agency services performed by a co-operative, include dealing with business, accounting and tax affairs of members and collecting insurance premiums, electric charges, etc. from members.

Common-Facility Small Co-operatives

The common-facility small co-operatives are similar to the common-facility co-operatives referred to above, with the exception, that these are organized by small establishments with fewer than five employees (fewer than two in the case of commercial or service establishments).

Industrial Co-operatives

These are co-operatives that deal with the manufacture, manufacturing or other activities, especially jointly. The owners of such co-operatives are members of the co-operative, take part in the management by means of their assets and labour force and share the profits (or losses) equally among them. The function of such co-operatives is to serve the needs of a community, but not to make a profit for the co-operative. According to the Industrial Co-operative Act, 1912, the members of the co-operative are to be employed in the business and to elect the directors and employees and to control their work. These co-operatives are very common in wholesale and retail trade, also in manufacturing. The main motive for the formation of these co-operatives is the need to expand or to provide scale of business by merger of small enterprises and to create the opportunity of working for them.

Joint Business Co-operatives

This type of co-operative was recently introduced to promote the joint business among small enterprises with insufficient capacities. The number of joint-business co-operatives is still small, but increases steadily in these years. By expanding the scale of business to the appropriate level, members can attain the improvement of productivity and enjoy the increase of common interest. This type of co-operative is generally observed in the field of production, selling and other business activities which require a scale-work. Though, formally ruled by the co-operative principles, this co-operative is in fact a type of a corporation and it effectively pursues economic interests. Each member is involved more intensively in the collective management in joint-business co-operatives and is forbidden to run other joint-business which would compete with the co-operative. The participation voting rights can be created to the extent that it does not exceed the total voting rights equally granted to members. A dividend is usually paid in proportion to the amount of shares held. The number of shares which can be held by one member must be less than fifty percent of the total shares.

Trade Associations

The trade associations were organized in accordance with the Law concerning the Organizational Structure of Small and Medium Enterprise Organizations, originally for the purpose of overcoming excess competition among small enterprises. At present, the improvement and development of handicrafts is more important role. The associations can be formed by more than one-unit of small enterprises within the prefecture and they can operate on behalf of all of the small enterprises within the prefecture. Duplication of the territories between the associations of the same trade is not permitted.

The general functions of the trade associations are the promotion of activities, such as dissemination of necessary information, formation of mutual friendship, study of new products and technology and provision of guidance to members. The associations can make a cartel with the sanction of the concerned ministry, in the case of economic depression, or when they grapple with the rationalization by means of restricting or regulating the methods of production, kinds of products, purchasing, selling and others. The concerned ministry, if necessary, dispatches orders to outsiders to join the associations or to restrict the installation of new production facilities and other business activities to all enterprises of the same trade. If the associations are equipped with the investment capital, they can also run collective businesses as common-facility co-operatives.

Federations of Small Business Associations

To improve the business management of co-operatives (and trade associations), there is a Prefectural Federation of Small Business Associations in each prefecture, which maintains a number of workers on its staff to guide and assist co-operatives and their members. A Prefectural Federation comprises co-operatives (and trade associations) located in a prefecture. For their activities Prefectural Federations receive subsidies from the Central and Prefectural Governments mainly for personnel expenses. At the end of 1973, 557 instructors and 115 office clerks played an intensive role in the Prefectural Federations. The major functions of the Prefectural Federations are

to assist in the identification, development, dissemination and coordination of co-operatives, to provide information necessary to co-operatives, to organize lectures to directors of co-operatives and to give general and special technical advice.

At the national level, there is the National Federation of Small Business Associations. This organization consists of 400 local associations in 30 States and the District of Columbia. The major functions of this organization are: to provide guidebooks and textbooks for co-operatives, to provide courses for the instructors of prefectural federations, to conduct research on the management of the Prefectural Federations, to investigate the conditions of co-operatives, to make recommendations to the Government for protection of rights and interests of members of co-operatives and to research and study the development of co-operatives. The National Federation maintains an instructor and 12 office workers for these functions. The National Federation receives subsidies mainly for personnel expenses from the Federal Government. They fully make use of printed literature on industrial co-operatives and leaflets on the subsidies available for small enterprises made by the Small and Medium Enterprise Agency. This Agency also organizes one-month lectures for the instructors in these Federations.

Assistance on Problems of Management and Technology

Business management of industrial co-operatives involve arrangements for credit, purchase of supplies, manufacture or processing, sales, inventory control, cost accounting, etc. Some other experienced experts besides the ones who deal with the problems peculiar to co-operatives are needed to solve these problems. Small co-operatives with a limited number of products and services, cannot afford many full-time qualified employees. Advisory services in the field of business management and economic guidance to make up insufficiently qualified personnel are offered free of charge by the guidance centers for small businesses founded by the prefectural governments and some big municipal governments. When co-operatives or

Individual small enterprises need all-round investigation in management, advisers composed of managerial and technical experts give advice, free of charge, on the basis of on-the-spot investigation. Around 400 co-operatives receive this service from the guidance centers every year. The co-operatives which utilized, or are going to utilize, the special low-interest loans extended by Central and Prefectural Governments for industrial estates or joint facilities for co-operatives are under an obligation to have this all-round investigation.

Advice and assistance on technical problems is of great importance to secure the steady growth of modern industrial co-operatives. Advice on technical problems regarding feasibility surveys, scale of production, selection of machinery and production methods, development of new products etc., can be given by the guidance centers. The prefectural technical laboratories in various technical fields of which more than 150 were set up in the nation, provide assistance in solving technically sophisticated problems of small enterprises. Co-operatives and small enterprises can receive technical assistance in close co-ordination with the guidance centers and can use testing apparatus, machine tools and other equipment in the laboratories at actual expense. The laboratories make an effort to have close links with small enterprises, so that the results of research can soon be put into use and the problems in industries requiring technical knowledge may be brought to the due attention of the laboratories.

Government Support

The problems of business management of industrial co-operatives and associations are very wide and complex. The possible range of co-operative activities is quite wide and may include many functions. The shortage of funds and the lack of adequate knowledge in management and technology may hamper their growth. It is not easy to keep co-operatives active only by self-help efforts. The members do not

always show equal interest and sometimes become hostile to each other. The problems are most serious in the co-operatives and associations which cannot afford experienced full-time paid employees.

Economic and financial support on a very large scale is provided to conquer these difficulties and to promote the organization of small enterprises. On the whole, all types of co-operatives and associations enjoy preferential treatment. Through advice and guidance on economic and technical problems are offered by the prefectural governments and the Federations of Small Business Associations.

Financial Support

One important function undertaken by common-facility co-operatives is to help members meet their credit needs. To this end, they either borrow from financing institutions and provide loans to their members, or they stand security for loans borrowed by members from financing institutions.

Through standing security, the co-operatives facilitate taking up loans by small enterprises from commercial financing institutions. The loans provided by the co-operatives may be for working capital or equipment and may take many forms, e.g., loans on goods, or discounting of notes and bills, or loans on mortgage. The most common method for the provision of credit is through discounting of notes and bills.

The co-operative trade associations' own funds are usually small, the supplies of commercial credit for working capital and investment are often inadequate, business turnover per co-operative is often not sufficient for economic stability and for prosperity and co-operatives especially in the field of traditional industry are apt to become inactive.

The financing structure evolved for looking after the needs of these co-operatives and their members is very elaborate. In addition to commercial financing institutions, the Government also provides loans. The funds available through the Government or government financing institutions are for medium- and long-term loans.

The Central Bank for Commercial and Industrial Co-operatives (CBCIC)

As a separate special quasi-official institution focusing on co-operatives (co-operatives and trade associations except joint enterprise co-operatives) and their members, there is the Central Bank for Commercial and Industrial Co-operatives. Almost all active co-operatives are affiliated with it. Nearly one-half of its capital has been subscribed by them and the residual part by the Government. Its resources are composed of securities, deposits, share capital and special loans from the Government. Deposits are provided by the members of co-operatives, although about ten per cent are derived from prefectural governments. The CBCIC was originally intended to deal only with co-operatives themselves. However, because of the weakness of some co-operatives, it was authorized to finance members directly. Its loans outstanding by the end of December 1972, amounted to ¥1,326 billion. This amount accounts for only 4 to 5 per cent of the total institutional financing of small manufacturers, but it plays an important role in the promotion of co-operatives. About one third of CBCIC's total loans were extended directly through its 76 offices, and two thirds were extended through the 347 credit co-operatives serving as CBCIC agencies. The CBCIC extends loans principally for working capital purposes, which is equivalent to 70 per cent of its loans outstanding to small manufacturers in 1972. Interest rates are moderate. They were 7.9 per cent for short-term loans and 8.4 per cent for long-term loans in 1973. The upper limits for loans are ¥ 300 million to co-operatives and ¥ 80 million to the members of co-operatives.

Small Business Finance Corporation (SBFC)

Another official institution accessible by co-operatives (and trade associations) is the Small Business Finance Corporation, which was established as a wholly government-owned corporation in 1953. Long-term loans are available to small enterprises and co-operatives from the SBFC. Its total resources in 1972 amounted

to Y 1,457 billion, of which 8 per cent consist of share capital and the remainder primarily of loans from the Government Trust Fund system. It operates smoothly, using a staff of about 1,700 personnel in 47 offices, and is headed by 19 lending institutions with around 7,000 offices which serve on the assets of the SHSG. It receives deposits from the public, banks, companies, or through the courts. At the end of December 1972, loans outstanding had risen to Y 1,440 billion. The SHSG extends only term loans for periods from 12 months to 10 years, although in some cases a shorter period may be agreed. It does not usually provide readily available credit for the conversion of small enterprises. Though the main purpose of its loans is the financing of plants and equipment, working capital loans are given when term working capital loans are essential for this purpose. The SHSG provides small enterprises with a less expensive source of term financing. The interest rate is 8 per cent per annum. Though the upper limit of normal loans to co-operatives is Y 50 million, the same as to individual small enterprises.

Special Financing Program for Collective Projects

In addition to these financial institutions, the Government extends through prefectural governments very favourable loans to co-operatives (and trade associations) for setting up joint facilities and common factories, for establishing industrial estates and for other joint projects by co-operatives. The conditions of loans are at an interest rate of 2.7 per cent, repayable within 12 years, with the first installment due at the end of the second year. In each prefecture, a special account is set up for this purpose with funds provided by the prefectural and Central Governments and loans are extended to co-operatives and to their members through co-operatives, in accordance with the standards laid down by the Small and Medium Business Agency. The maximum ratio of loans to total requirements is 65 per cent, but there is no limitation of the amount of loans. In the case of industrial estates, it is required that more than twenty small enterprises be located in an estate and carry out some joint activities.

From 1961 to 1973, loans were extended to the following projects in the field of manufacturing industries:

industrial estates	171	common factories	140
joint facilities	3,811	joint facilities for pollution control	56

Credit Guarantee System

With the view to facilitate financing to small enterprises, a system of credit guarantee is in operation through the fifty-two official credit guarantee associations (fourty-six at the prefectural level and five at the municipal level). More than 90 per cent of their capital funds have been provided by prefectural and municipal governments. The associations guarantee loans, not only from commercial, but also from governmental financing institutions to small enterprises and co-operatives at a small premium (around 1.07 - 1.38 per cent per annum). The maximum amounts of loans to be guaranteed vary from association to association and are Y 38 to 53 million per enterprise and Y 71 to 83 million per co-operative.

At the apex, there is the government-owned Small Business Credit Insurance Corporation, with a capital of around Y 99.6 billion as of the end of March 1972. Of this capital, around Y. 80.5 billion form a special fund for loans to the credit guarantee associations. The long-term loans carry an interest of 3.0 per cent per annum. These loans are deposited at commercial banks as a security to ensure repayment of debts. The difference of interests between borrowing and term-deposits becomes the basic income of the credit guarantee associations. The maximum amounts to be insured by the Corporation are Y 70 million for a co-operative and Y 45 million for an enterprise. The rate of compensation is 70 - 80 per cent and premium rates vary from 0.35 to 0.7 per cent with the types and amounts of loans (e.g., for less than Y 1 million, the premium is 0.35 per cent). The outstanding amount insured by the Corporation was Y 1,497 at the end of March 1973.

Investment

Small enterprises are subject to favourable taxation. Small corporations with a fixed capital of less than 500 million, pay the corporation tax at a lower rate: 20 per cent for an income of less than 50 million, and additional depreciation of one-fifth of the value of investments and equipment is allowed in the first year, in the case, that they are required for the installation of small enterprises. Co-operatives (and trade associations) receive some of the beneficial treatment and in some cases complete exemption. Co-operative, except joint enterprises and joint ventures are co-operatives and a preferential rate of depreciation is allowed for their investments. The same preferential procedure is followed in their tax assessment. For encouraging the establishment of industrial estates, the income obtained from selling old factory sites in order to have to new industrial estates, is exempt from taxation. Members of co-operatives who take part in the restructuring programmes designed by the co-operatives, are allowed to depreciate fifty per cent more than usually of the value of machines, equipment and other fixed assets for five years. Moreover, a co-operative can have half of its income exempted from corporation taxes until its reserves reach 25 per cent of the amount invested. Generally, the surpluses distributed as a patronage dividend are exempt from taxation. Co-operatives are exempted from fixed assets tax for their hospitals, clinics, offices and warehouses, other local taxes and stamp duty.

The Restructuring Programme

This programme aims at the modernization of all small enterprises in the same line of trade at the same time, following the concerted and voluntary plan made by a trade association (or a common-facility co-operative) with membership of more than one-half of the small enterprises of the same trade. The associations are required to be reliable in management and represent the whole trade, not only members, but also outsiders, so as to successfully make a plan and carry it out. This five-year plan contains objectives and measures which may include

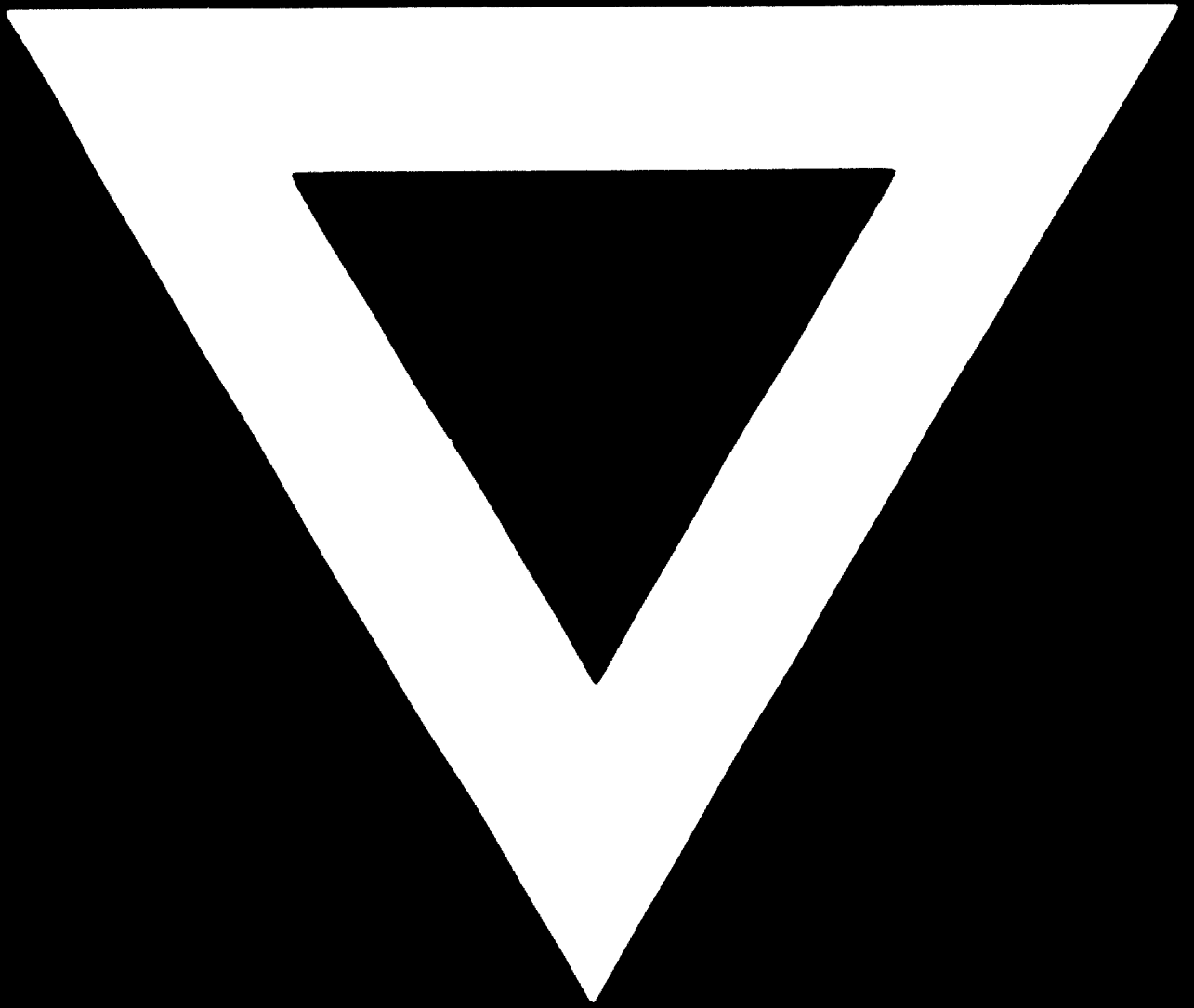
replacement of machinery, cultivation of new markets, development of design and products, promotion of collective undertakings, etc. Participating small enterprises in the restructuring programme are privileged to low interest loans and tax exemptions. The Small Business Financing Corporation offers besides normal loans, long-term fixed capital loans for machinery, equipment, land, and construction up to a period of ten years and working capital up to a period of five years at an interest rate of 7.0 per cent per annum. The maximum amount of fixed capital loans are 1,000 million to a small enterprise, Y 300 million to a trade-association and Y 50 million as working capital loans to both, small enterprises and trade associations. Participants of the restructuring programme can apply additional depreciation of the value of the production facilities and build up a reserved fund (up to 1.5 per cent of turnover) for restructuring.

Public Purchase

To increase the flow of orders to small enterprises and co-operatives (and trade associations), the information regarding orders by the central and local governments and public corporations are circulated through the Federation of Small Business Associations. Public purchases are prohibited to designate the brands of goods in advance, are urged to divide a big order into small parts and to name small enterprises and co-operatives as specified bidders, so that these can avail themselves of given opportunities. With the recognition of the importance of joint sales of small enterprise co-operatives, private contracts with these are exceptionally authorized by public offices and public corporations.

As the importance of joint sales by small enterprise co-operatives is recognized, public offices and public corporations are exceptionally authorized to issue private contracts with such co-operatives.





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