

Credit Cooperatives in Early Israeli Statehood: Financial Institutions and Social Transformation

Neta Ziv*

In 1948, when the State of Israel was founded, 125,000 people (about one fifth of the Jewish population) were members of credit cooperative societies, which provided over 20 percent of all market financing. For several years this number continued to rise, reaching a total of 250,000 members in more than 100 credit cooperative societies. Credit associations — part of the thriving cooperative movement of early Zionism — symbolized the attempt to create a new and just Jewish society by fusing socialist and capitalist ideals. From the mid-1950s, however, in a rapid process of centralization of Israel's capital market and financial institutions, almost all credit associations were absorbed into Israel's commercial banks and dissolved. Today, Israel's two largest banks (Leumi and Hapoalim) control over 63 percent of credit provision, and 90 percent of credit is provided to less than 1 percent of borrowers. The official policy of the Bank of Israel is to rule out the establishment of credit associations, credit unions or other non-bank financial institutions. In the light of current renewed interest in "social businesses," i.e., innovative business models designed to achieve desired social outcomes, this Article traces the waning of credit associations in Israel, and the role law has played

* Senior Lecturer and Director, Clinical Law Programs, The Buchmann Faculty of Law, Tel Aviv University. I want to thank Profs. Ron Harris and Assaf Likhovski for early comments on the Article, as well as the students in the Law and Political Thought Workshop at Tel Aviv Faculty of Law, and members of TIL editorial board for excellent work bringing the Article to publication. Special thanks to Tali Margalit, who provided insightful comments on the Article, and to Hadar Yuhas, my research assistant, who accompanied me from the early stages of my work, for her dedication and significant contribution to this Article.

in that process. Their disappearance from the capital market marked not only a change in economic policy, but also the final abandonment of the ideals which underlay the provision of cooperative financial services: mutuality, partnership and solidarity.

"Social business will be a new kind of business introduced in the market place with the objective of making a difference in the world."

— Muhamad Yunus, Nobel Lecture, Oslo, Dec. 10, 2006.

INTRODUCTION

What can banks and financial institutions tell us about a particular society: its values, historical struggles, social arrangements, power relations, and systems of belief? Financial institutions may be viewed as neutral intermediaries providing goods and products in the form of deposits, loans and other financial devices that facilitate economic transactions.¹ On that view, economic and monetary transactions themselves are the substantive activities that tell us something about a society, apart from the financial institutions which enable or facilitate them. An alternative view considers financial institutions as elements that are internal to the social and economic fabric. Just as money is understood to be not just a "thing" that represents material value, but a social construct that both reveals and constitutes choices, priorities, commitments, and a set of relations between a collective and its members — financial institutions too are reflective and constitutive of the conditions and places in which they exist.²

Banks and other financial institutions are part of an economic order which has lately attracted the scrutiny of law and society scholars.³ This scholarship is interested in the way social, cultural and economic forces, both

1 MEIR HETH, *THE BANKING INSTITUTIONS IN ISRAEL* 32 (2d ed. 1966).

2 This is the approach underlying most essays in this issue of *Theoretical Inquiries in Law*. See, e.g., Bruce G. Carruthers, *The Meanings of Money: A Sociological Perspective*, 11 *THEORETICAL INQUIRIES L.* 51 (2010); Roy Kreitner, *The Jurisprudence of Global Money*, 11 *THEORETICAL INQUIRIES L.* 177 (2010); Christine Desan, *Coin Reconsidered: The Political Alchemy of Commodity Money*, 11 *THEORETICAL INQUIRIES L.* 361 (2010); L. Randall Wray, *Alternative Approaches to Money*, 11 *THEORETICAL INQUIRIES L.* 29 (2010). See also Christine Desan, *The Market as a Matter of Money: Denaturalizing Economic Currency in American Constitutional History*, 30 *LAW & SOC. INQUIRY* 1, 15 (2005).

3 Terence Halliday, *Crossing Oceans, Spanning Continents: Exporting Edelman to Global Lawmaking and Market-Building*, 38 *LAW & SOC'Y REV.* 213 (2004).

local and global, instigate the emergence of financial institutions and bear upon their mode of operation.⁴ From that perspective, law and society scholarship examines how financial institutions work: the kind of people they serve, their relations to the state and other monetary authorities, their structure and legal form, their evolvment or diminishment over time, and the way they articulate their societal role in a particular time and place.

Historical, social and cultural factors bear upon the performance of the financial institution and delineate it as a social and cultural entity within a particular polity. In that context, the question regarding the role of the law emerges: how does the legal order governing financial organizations influence, shape and constrain their activities? Based on that perspective, in this Article I shall investigate the decline and ultimate disappearance of credit cooperatives during the first two decades of Israeli statehood.

When Israel was established in 1948 there were over 80 credit cooperatives operating in the country, serving 20 percent of the population (about 125,000 people) and providing over 20 percent of all market financing. For a few years credit cooperatives continued to expand, and by 1954 there were 95 of them and their membership had doubled. Then, rather abruptly, a period of rapid decline began. From the mid-1950s, in a continuous move to centralize Israel's capital market and financial institutions, a growing number of credit cooperatives were absorbed into Israel's commercial banks, while others were converted into companies (limited liability) and dissolved. By 1961 only 27 cooperatives were operative, and the "credit cooperative movement" — so defined by its leaders and activists — was on its last legs. In 1968 the movement suffered a major setback when the largest credit cooperative — The Jaffa-Tel Aviv Loans and Savings Cooperative — decided to reincorporate as a limited liability company and merged with the largest cooperative bank (Zrubavel Bank). This story is discussed at length in Section II.D. In the early 1970s there were still several small and medium-sized credit cooperatives with tens of thousands of members, but it was already apparent that this financial enterprise was fast vanishing from the Israeli socio-financial scene. Although the remaining leaders of the movement continued to yearn for its revival, any hopes of reinvigorating credit cooperatives eventually were dashed.⁵

4 See, e.g., Timothy W. Guinnaine, *A Failed Institutional Transplant: Raiffeisen's Credit Cooperatives in Ireland, 1894-1914*, 31 *EXPLORATIONS ECON. HIS.* 38 (1994) (describing the failed transplant of German credit cooperatives in Ireland).

5 In a series of articles published in a local newsletter (*The Credit Cooperative*), leaders of the movement expressed hope for "a renewed place for credit cooperatives, assuming that without [credit cooperatives] there will be no real guardian of the

The credit cooperatives operated as market institutions, which provided loans to their members. But, as described below, what underlay their operation was a social and public belief that *credit is a public good that ought to be accessible to all, allocated fairly, and managed democratically*. This idea differentiated credit cooperatives from commercial banks, which did not embody a similar notion of "social responsibility." Indeed, as the existential threat to credit cooperatives became more apparent, their leaders rearticulated their moral claim by distinguishing themselves from commercial banks: the banks were "Goliath," motivated solely by profit-making, while credit cooperatives were "David" — the only remaining financial institution still loyal to "the people" and "the simple person."⁶

Four different sources of influence combined to inspire the credit cooperative movement in Mandatory Palestine. The first was a strong commitment to the ideals of the worldwide cooperative movement, in particular the German credit cooperatives established by Hermann Schultze-Delitzsch and Friedrich Raiffeisen in the nineteenth century. The second was the connection to credit associations of the Jewish Diaspora and their leaders (mainly in Central and Eastern Europe), who constituted a model and form of attachment. The third was Zionism, the collective process of nation-building, and in particular the agricultural cooperatives associated with the Labor movement, whose power bore directly upon the institutional legitimacy of cooperatives unaffiliated with the Labor movement. Lastly, credit cooperatives struggled for political clout due to the makeup of their membership: merchants, traders, commercial dealers and craftsmen, i.e., the petit bourgeoisie and middle class. The habitus of this group — of a lower

credit needs of the masses." They voiced concern about the fate of the petty-client and the small business, lost in an era of "automated banking," transformed into an "anonymous number." Only credit cooperatives, they believed, which were not driven by sheer business considerations or profit-maximizing motivations, could fulfill the credit needs of their members — the true and only owners of these financial institutions. Abraham Shtacher, *Ha-Co'operatzia ha-Ashra'it — Ma Yehe Aleiha?* [*The Credit Cooperative: What Will Be Its Fate?*], 13 CREDIT COOPERATIVE 2, 4 (1969) (Hebrew); Abraham Shtacher, *Ha-Co'operatzia ha-Ashra'it — Ma Yehe Aleiha?* [*The Credit Cooperative: What Will Be Its Fate?*], 15 CREDIT COOPERATIVE 2 (1969) (Hebrew); Abraham Shtacher, *Lema'an Hit'argenu Retsuya ba-Co'operatzia ha-Ashara'it* [*For Better Organization in Credit Cooperatives*], 16 CREDIT COOPERATIVE 1 (1970) (Hebrew).

⁶ Baruch Winitzky, *1970-1971 be-Hayey ha-Agudot ha-Shitufiyot le-Ashrai* [*1970-1971 in the Lives of Credit Cooperatives*], 19 CREDIT COOPERATIVE 4, 5 (1971) (Hebrew).

social status than the ruling Labor establishment — had a crucial impact on the fate of the credit cooperative movement.

The law regulating credit cooperatives — *The Cooperative Ordinance* — was riddled with an internal tension that triggered the course of decline. The statute, which applied to all types of cooperatives, adequately embodied the basic principle underlying this type of financial institution: to serve and further the interests of its members. It mandated equal voting power of members, restricted profit distribution among them, defined the personal nature of membership, and limited its transferability. However, in the political and social context of early Israeli statehood, this structure became a "trap" hindering the sustainability of credit cooperatives. The same enabling legal frame frustrated their ability to change and compete with banks and other financial institutions, incorporated as limited liability companies.

Subsequently, during the 1950s and 1960s numerous credit cooperatives opted to "reorganize" as a limited liability company under the *Companies Ordinance*, and hence to become uninhibited by such constraints. A company, for example, could issue different types of shares to its holders (according to their investment), grant them differential voting rights, commercialize and transfer its stock, issue stock and bonds to the public, and limit the liability of shareholders. A company recognizes the division between owners and lenders: clients/customers who deposit their money in the bank do not have any proprietary rights in the company, nor managerial powers or rights.

The seemingly technical "reorganization" — from being governed by the Cooperative Ordinance to being governed by the Companies Ordinance — was no less than an ideological conversion from one worldview to another, a substantive transformation that altered not just the formal structure of credit cooperatives, but their underlying values and relations. A cooperative spirit of mutual responsibility, solidarity and care for the less privileged was incarnated in the legal regime governing the cooperative structure. In that sense, law had a deep constitutive function, forming and defining the relationship among members of the cooperatives themselves, as well as with their socio-political and economic environment.⁷ Through statutory categories such as a "cooperative" and a "limited liability company," law not only influenced the meaning of a particular form of socialization, but also set

⁷ On the constitutive nature of law in the life of organizations, see, for example, Lauren B. Edelman & Mark C. Suchman, *The Legal Environment of Organizations*, 23 ANN. REV. SOC. 479 (1997).

its boundaries.⁸ In this Article I shall trace that process, drawing attention to the role of law in its unfolding.

A. Existing Scholarship on Credit Cooperatives in Israel

The literature on the decline of credit cooperatives in Israel is quite limited. Heth points to the changes in Israel's emerging banking system as the background to this development. This internal explanation identifies the establishment of a central bank in Israel (The Bank of Israel) in 1954 as the major cause for the decline. The Bank of Israel took steps to assume (state) centralized control over a myriad of small banking institutions which had operated during the British Mandate under a loose and decentralized supervisory regime. It encouraged mergers and acquisitions of small banks, aligned national banking policies, and unified financing rules in order to control the provision of credit by financial institutions. Consequently, credit cooperatives encountered strong competition from the strengthened, consolidated banking system. However, claims Heth, instead of carving a niche for themselves, credit cooperatives started competing with banks under inferior conditions, and ultimately lost their relative advantage and popular basis.⁹ Karlinsky traces the sustainability problem of credit cooperatives to their "private" ideology and its alienation from the Zionist meta-narrative, which adopted a strong collective ethos and dogma.¹⁰ These cooperatives served the middle class and petit bourgeoisie, whose worldview was based on liberal individualistic ideals, on the salience of private property and accumulation of personal wealth. In contrast to the collective ideology of the Labor movement — and its own cooperative apparatus, mainly the Kibbutz and Moshav agricultural settlements — credit cooperatives did not adopt an overall "transformative vision" for Israel's nationalist revival project. Therefore their activists were marginalized and their leaders removed from political power centers; they did not gain public visibility and recognition, and remained subordinate to the mainstream polity.

8 On the mutually constitutive relationship between law and its environment, see Austin Sarat & Thomas R. Kearns, *Beyond the Great Divide: Forms of Legal Scholarship and Everyday Life*, in *LAW IN EVERYDAY LIFE* 21 (Austin Sarat & Thomas R. Kearns eds., 1993).

9 HETH, *supra* note 1, at 49-52; MEIR HETH, *BANKING IN ISRAEL, PART I: HISTORICAL OVERVIEW* (1994) [hereinafter HETH, *BANKING IN ISRAEL*].

10 Nahum Karlinsky, *The Private Cooperative in the Mandate Period: Credit and Savings*, in *ECONOMY AND SOCIETY IN THE MANDATE PERIOD: 1918-1948*, at 239, 259-60 (Avi Barel & Nahum Karlinsky eds., 2003).

While I recognize the validity of both points of view, I believe they do not capture all aspects of this chronicle. Rather, as will be explicated below, a combination of diminishing commitment from within the rank-and-file of cooperative members and external-structural circumstances led to their demise. To be sure, the centralization project of Israel's banking system and the preeminence of the Labor movement and its organizations had a compelling effect on the fate of credit societies. Yet there was also a real endeavor within the credit cooperative movement to further a *public ideal* and to instill its ethos within a particular market-economic activity — credit provision. The movement was highly committed to the core cooperative values of mutual responsibility, solidarity, and care for the less privileged. It conceived of itself as a shield against the forces of uncontrolled and ruthless capitalism. It offered a more humane alternative to an emerging propensity for profit-maximization as the reigning motivation, and it struggled to translate these commitments into valid economic and legal institutions.

Ultimately, these efforts were not successful; but they can teach us a lesson relevant to the present day, as the division between economy and society is constantly being blurred.¹¹ Market agents — businesses, corporations, financial institutions and banks — have been developing modes of social accountability and are expected to become more ethical, democratic and responsive to all of society's constituents. Credit cooperatives are an illustrative model of a fusion of this sort between financial market activities and a social common good.¹²

11 See, e.g., John M. Conley & Cynthia A. Williams, *The Corporate Social Responsibility Movement as an Ethnographic Problem* (Univ. of N.C. Legal Studies, Research Paper No. 1285631, 2008), available at <http://ssrn.com/abstract=1285631>; Ronen Shamir, *The De-Radicalization of Corporate Social Responsibility*, 30 CRITICAL SOC. 669 (2004); Robert Reich, *The Case Against Corporate Social Responsibility* (Goldman Sch. of Pub. Policy, Working Paper No. GSPP08-003, 2008), available at <http://ssrn.com/abstract=1213129>.

12 For a similar context situating cooperatives as an alternative to the "Standard Economic Model" based on profit-maximizing and competition, see RICHARD C. WILLIAMS, *THE COOPERATIVE MOVEMENT: GLOBALIZATION FROM BELOW* (2007); see also HENRY HANSMANN, *THE OWNERSHIP OF ENTERPRISE* (1996) (describing a variety of "noncapitalist firms," such as employee-owned corporations, consumer-owned companies and numerous non-profit enterprises, as alternative forms of investor-owned corporations).

I. CREDIT COOPERATIVES IN MANDATORY PALESTINE

A. The Cooperative Movement in Mandatory Palestine

The foundations of the modern cooperative movement are associated with the establishment of the first consumer cooperative by 28 pioneer weavers in Rochdale, England in 1844.¹³ The Rochdale cooperative was not the first of its kind, but its founders laid down the basic principles of the modern cooperative: open, voluntary membership in an organization whose purpose is to further the economic interests of its members, equal voting powers, democratic governance, limited interest on equity shares, mutual support, and the advancement of the common good. The philosophic foundations of the modern cooperative movement developed in the second half of the nineteenth century as a response to industrial capitalism and its harsh social consequences. The ideals of the cooperative movement took concrete shape through the establishment of hundreds of thousands of cooperatives all over the world in different areas of life.¹⁴ Consumer cooperatives, production, service and distribution cooperatives, agricultural cooperatives, housing and building cooperatives, transportation, insurance and credit cooperatives — testify to the breadth of this movement.¹⁵

In the Israeli context, the cooperative movement is closely tied to the saga of Jewish national revival and state-building. Its significance runs beyond cooperative membership rates (which were relatively high in and of themselves),¹⁶ to the movement's vital contribution to the formation of Jewish national institutions. The literature has pointed to the fundamental role played by communal agricultural settlements (the Kibbutz and the Moshav) in

13 The history of the Rochdale Pioneers is commemorated in a museum dedicated to the co-op movement in Rochdale, UK, <http://museum.co-op.ac.uk/> (last visited Aug. 10, 2009), and the Rochdale Pioneers Equitable Society website, <http://archive.co-op.ac.uk/pioneers.htm> (last visited Aug. 10, 2009).

14 The International Cooperative Association, established in 1895, continues to serve as a central organization which "unites, represents and serves co-operatives worldwide" from all sectors of the economy, in over eighty countries, with over 200 million members. See The International Co-operative Alliance, <http://www.ica.coop/al-ica/> (last visited Aug. 10, 2009).

15 On the historical and philosophical foundations of the cooperative movement, see, for example, JOHNSTON BIRCHALL, *THE INTERNATIONAL CO-OPERATIVE MOVEMENT* (1997).

16 In 1937, for example, there were 871 registered Jewish cooperatives in Mandatory Palestine; according to Karlinsky, almost every adult was a member of one or other cooperative society. In 1945 there were over 1200 Jewish cooperatives. Karlinsky, *supra* note 10, at 239.

performing the Zionist mission, as well as by the Labor movement's industrial cooperative apparatus (affiliated with the *Histadrut* Federation of Labor).¹⁷ The agricultural cooperatives incarnated the ideological transformation of the "new Jews": hardworking pioneers, people of the land, settled in communal or cooperative living arrangements, became the symbol of the collective struggle for Jewish national revival.¹⁸ Out of this enterprise grew a network of distribution and consumer cooperatives (the largest being *Hamashbir*, established in 1916), whose primary goal was to distribute the products of the agricultural cooperatives.¹⁹ Together with transportation, marketing, housing and credit cooperatives, the Labor movement and the *Histadrut* assumed an overreaching, almost monopolistic proprietorship over the economic resources of the Jewish establishment. Over time, these economic enterprises were incorporated into a centralized legal entity (The Workers' Society, which complemented the economic control of the *Histadrut* and confirmed its political supremacy.²⁰

Besides the cooperatives affiliated with the Labor movement, "private" production and service cooperatives emerged in the early 1900s. The first was a printing cooperative (*Dfus Ahdut*) established in Jerusalem in 1910 by "The Zionist Workers Party."²¹ This enterprise was followed by carpenters',

17 On the origins and significance of the cooperative movement and ideology in Jewish national revival, see AVRAHAM ZBARSKY, HA-COOPERATZIA: HA-TNU'A, EKRONOTEHA VE-HESEGEHA [THE COOPERATIVE: THE MOVEMENT, ITS PRINCIPLES AND ACHIEVEMENTS] (1942) (Hebrew) (the book itself was printed by a printing cooperative); HARRY VITELES, A HISTORY OF THE CO-OPERATIVE MOVEMENT IN ISRAEL: A SOURCE BOOK IN 7 VOLUMES (1966-1970); NOAH ORYAN (HERTZOG), THE COOPERATIVE: THEORY AND PRACTICE (1966); ABRAHAM DANIEL, THE CREDIT COOPERATIVE: SUCCESSES AND FAILURES 28-33 (1989); Avital Margalit, *Law, Organization and Corporate Structure in the Workers' Society*, 26 TEL AVIV U. L. REV. 451 (2002) (Hebrew); Danny Rabinovitz, *The Forgotten Option: Cooperative Urban Housing*, in SPACE, LAND, HOME 113 (Yehuda Shenhav ed., 2003).

18 On the agricultural cooperatives in early Zionism, see ABRAHAM DANIEL, COOPERATIVE THEORY AND COOPERATIVES IN ISRAEL 119-73 (1972).

19 On the establishment of *Hamashbir*, see *id.* at 174. Consumer cooperatives branched out of this central cooperative. *Id.* at 201.

20 Margalit, *supra* note 17, at 476-82; ITZHAK GREENBERG, ME-HEVRAT OVDIM LE-MESHEK OVDIM: HITPATHUT RA'YON HEVRAT HA-OVDIM BA-SHANIM 1920-1929 [FROM WORKERS' SOCIETY TO WORKERS' ECONOMY: EVOLUTION OF THE WORKERS' SOCIETY IDEA IN THE YEARS 1920-1929] (1987) (Hebrew).

21 Interestingly, 1910 was also the year in which Dganya, the first cooperative kibbutz, was established under socialist ideology and on the collectivist model. The establishment of Dganya is considered the constitutive moment of the cooperative movement in Israel. Daniel states: "As for the date of birth of the cooperative movement in Israel there can be no controversy . . . in 1910 . . . with the establishment

welders' and metalworkers' cooperatives, cooperatives of shoemakers, builders, bakers, farmers (unaffiliated with the Labor movement), small industries and crafts. Contrary to the cooperatives affiliated with the Labor movement, these cooperatives emerged through a "bottom-up" process. Lacking the organizational and political support of the Labor movement, they were formed voluntarily by their members' rank and file. This difference is crucial to understanding their trajectory in the Israeli polity and economy.²²

B. Credit Cooperatives — Scope and Legal Framework

Among the private cooperatives (those unaffiliated with the Labor movement) in Mandatory Palestine, credit cooperatives constituted the largest sector, with the highest value of financial and other assets, geographical scope of activities and membership rates.²³ In 1922, for example, they constituted 30 percent of all private cooperatives, with 50 percent of their membership. In 1930, 25 percent of all private cooperatives were credit cooperatives, constituting around 40 percent of membership.²⁴

The first credit cooperatives in Mandatory Palestine were established in the early 1900s, both as a means of avoiding the humiliating practice of *Haluka*, a form of patronizing support by philanthropists, and to instigate economic independence and self-sufficiency.²⁵ From the early 1920s, credit cooperatives grew steadily. In 1922 there were 10 registered credit cooperatives with a total of 3500 members; by 1928 the number had risen to 48 with 22,000 members; in 1934 there were already 96 cooperatives with a membership of around 55,000, and almost 87,000 members in 113 cooperatives in 1937.²⁶ At that

of the communal settlement of Dganya, the basis of cooperatives in Israel was laid." DANIEL, *supra* note 18, at 80.

22 Karlinsky, *supra* note 10, at 248-49; Margalit, *supra* note 17, at 503.

23 Credit cooperatives operated within the Labor movement as well, but were a relatively minor branch within this cooperative sector.

24 Karlinsky, *supra* note 10, at 244-45. In 1920 there were 10 credit cooperatives out of 33; in 1932, 21 out of 80; and in 1937, 113 out of 871.

25 B. ZIV, *KESSEF VE-ASHRAI BE-ERETZ YISREAL* [MONEY AND CREDIT IN ERETZ ISRAEL] 128 (1932) (Hebrew); HAIM MILKOV, *OSSEY KOL MELACHA: SHIV'IM SHANA LE-HIT' AHDUT BA'ALEY HA-MELACHA VE-TA'SIYA ZE'IRA BE-YERUSHALAYIM* [DOERS OF ALL TRADES: SEVENTY YEARS TO THE ESTABLISHMENT OF MERCHANTS AND SMALL INDUSTRIES UNION IN JERUSALEM] 36 (1989) (Hebrew).

26 Karlinsky, *supra* note 10, at 244. There is some discrepancy between the numbers of credit cooperatives reported by Karlinsky and Heth. According to HETH, *supra* note 1, in 1934 there were 50 credit cooperatives (compared to 96 reported by Karlinsky), and 91 in 1944 (Karlinsky reports 113 in 1937). Karlinsky relies on the reports from the registrar as his source, while Heth's source is the Banking

time, 17.3 percent of all public deposits were held by credit cooperatives, and they issued 24 percent of all loans.²⁷ During World War II they suffered a temporary decline, but toward the end of the 1940s and into the early years of Israeli statehood, the scope of activities of credit cooperatives was again on the rise. In 1947, a year before the state of Israel was founded, credit cooperatives provided about 15 percent of all credit, held over 10 percent of banking deposits, and there were about 100 of them, with over 125,000 members.²⁸

An important step in the development of the cooperative movement was the establishment of "*Merkaz* [The Center] — Audit Union of the Cooperative Societies for Loans and Savings in Palestine" in 1924.²⁹ The audit union became the collective entity that carried out the professional supervisory role of auditing and financial oversight of credit cooperatives, as well as representing them vis-à-vis external bodies (such as the Registrar and other banking institutions).³⁰ It was also the main agent in constituting "the credit cooperative movement" in Mandatory Palestine, and later in Israel. The *Merkaz* maintained connections with international credit cooperatives

Supervision Department at the Bank of Israel. Both report a linear rise in numbers and membership.

27 DANIEL, *supra* note 17, at 249.

28 *Id.*

29 On the establishment of *Merkaz*, see Karlinsky, *supra* note 10, at 267. The private credit cooperatives preferred to establish their own alliance and not to affiliate with the Central Bank for Cooperative Institutions in Palestine, established by the American Jewish Joint Distribution Committee (the Joint) and the Jewish Colonization Association established by Baron Hirsch in Germany (JCA) in 1920. This cooperative bank was largely affiliated with Labor's agricultural cooperative organizations and was viewed with great suspicion by the urban cooperatives. *Id.* at 265-66.

30 A number of examples: the Registrar viewed *Merkaz* as the address to inquire about cooperatives whose finances were problematic and which were accumulating losses, see Letter of the Deputy Coop. Registrar to *Merkaz* (Mar. 15, 1939) (on file with author) (discussing the Ramataim Credit Cooperative, which was not developing adequately); *Merkaz* informed the Registrar about policies that it was implementing to guide cooperatives on the maximum amount of credit to be issued to members, see letter from *Merkaz* to the Coop. Registrar (Nov. 11, 1940) (on file with author); it counseled the cooperatives about legal and accounting procedures that needed to be followed, e.g., Protocol of the General Assembly of *Merkaz*, the Audit Union of Credit Cooperatives (July 30, 1939) (on file with author) (dealing with the status of agricultural/farming cooperatives and setting new fees for membership in *Merkaz*); and was involved in decisions of dissolution, reincorporation as a limited liability company, etc. (see the case of the Jaffa-Tel Aviv Loans and Savings Mutual Fund, discussed *infra* Section II. D.).

around the world, held annual meetings and events, established a newsletter, and served as a platform for discussions, debates and updates on the local and international credit cooperative movement. It drew links between the present work of credit cooperatives in Mandatory Palestine and the historical achievements of cooperatives worldwide as well as of Jewish credit cooperatives in the Diaspora; it spread the fame of the movement's international visionaries and leaders, identified its local "heroes," and served as a constant reminder of the movement's ideals and missions.

The Labor movement too established credit cooperatives ("funds") that provided loans to workers, mainly in the *Histadrut's* institutions and affiliated cooperatives.³¹ Contrary to the private credit cooperatives, the *Histadrut* funds were established top-down, many with the assistance of Bank Hapoalim.³² Despite a common commitment to the cooperative mission, the culture, worldview and political inclination of the private cooperatives differed significantly from those associated with the Labor movement. Consequently, they preferred to set up an independent union — the "*Merkaz*" — which eventually turned into the main vehicle for building the cooperatives as a social subgroup and movement.³³

The law governing credit cooperatives left ample room for the development of a state-independent socioeconomic arrangement. Under the Cooperative Ordinance of 1920, the official Cooperative Registrar had only a minor and passive role overseeing registered cooperatives.³⁴ In 1933 the Cooperative Ordinance was amended, somewhat expanding the supervisory role of the Registrar (cooperatives were required to undergo a yearly audit and financial/accounting assessment).³⁵ Altogether, however,

31 These cooperatives were called "The Workers' Loans and Savings Funds." On the Labor credit cooperatives, see NAHUM T. GROSS & YITZHAK GREENBERG, *BANK HAPOALIM, HAMISHIM HA-SHANIM HA-RISHONOT, 1971-1921 [BANK HAPOALIM, THE FIRST FIFTY YEARS, 1921-1971]* 237-76 (1994) (Hebrew).

32 Karlinsky, *supra* note 10, at 245. According to Gross and Greenberg, Bank Hapoalim was often the operative body behind funds of this sort. GROSS & GREENBERG, *supra* note 31, at 6.

33 Karlinsky, *supra* note 10, at 268-73.

34 Cooperative Ordinance, 1920, Legislation of Palestine 102, §§ 3, 8, 9, 12, 43-48A, 64 (1918-1921). Cooperatives were required to fulfill only minimal reporting duties, and were largely self-regulated with little state supervision. See ABRAHAM FELLMAN, *THE LAW AND PRACTICE OF COOPERATIVE SOCIETIES IN ISRAEL* 17-19 (1951); Margalit, *supra* note 17, at 465-66.

35 Cooperative Ordinance, 1933, 1 Hukei Eretz Yisrael 330. The main changes in the amended legislation were: 1. Appointment of an official Registrar as part of the new department, with broader authority to inquire into the financial operations of a cooperative, including the power to appoint an accountant and to dissolve

the interface between the Registrar and the cooperatives remained relatively limited, and in fact was largely of a bureaucratic nature.³⁶ The Registrar rarely intervened in the extra-financial doings of the credit cooperatives, and the government's general policy was to allow a broad spectrum of self-regulation and autonomy.³⁷ Although the 1937 Banking Ordinance tightened the requirements for institutions requesting to provide banking services (banks and credit cooperatives needed a license from the government), this instruction was for the most part not enforced upon credit cooperatives, which continued to provide their services as before.³⁸

In general, and somewhat contrary to the collective-socialist mission of the Zionist institutions, Mandatory law stood in favor of the underlying tenets of the private credit cooperatives.³⁹ Mandatory law was a bourgeois law: it protected private property, and was based on a liberal and individualistic worldview. In that sense, it was not in tension with the ideals of the cooperative movement and left sufficient autonomy and space for internal organizational work and the movement's continued development.⁴⁰

In sum, during the British Mandate period the credit cooperatives were transformed into a social subgroup, developing their own ideological leadership. Its activists articulated a distinct perception of their identity and

a cooperative. 2. Vesting administrative powers with the High Commissioner to issue regulations and hear appeals on decisions of the Registrar. 3. Authorizing cooperatives to include certain powers in their articles of association, mainly to collect members' debts and impose sanctions. 4. Equalizing the voting powers of members in cooperatives, through the principle of "one member — one vote," and limiting the capital each member could hold in the cooperative. 5. Imposing a duty of accounting supervision, either through an accountant or a credit alliance.

36 It entailed official registration, inspection of balance sheets, and oversight of loan rates compared to equity, of paid up capital and obligations, payment of dues by members, mergers and dissolution of cooperatives, etc.

37 Margalit explains that the Cooperative Ordinance was amended in order to vest the Registrar with more active authority in order to facilitate the creation of Arab agricultural and credit cooperatives, as a means of assisting the Arab population in a time of economic crisis. The policy regarding the Jewish cooperatives was to allow them to operate with little intervention, due to their know-how and accumulated experience in running cooperatives. Margalit, *supra* note 17, at 467-68.

38 HETH, BANKING IN ISRAEL *supra* note 9, at 48-49.

39 The multidimensional relationship between Jewish national institutions and the British Mandate Government has been the subject of expansive research in the last decade. See ASSAF LIKHOVSKI, LAW AND IDENTITY IN MANDATORY PALESTINE (2006); RONEN SHAMIR, THE COLONIES OF LAW: COLONIALISM, ZIONISM AND LAW IN EARLY MANDATE PALESTINE (2000); Margalit, *supra* note 17.

40 Cf. Margalit, *supra* note 17, at 470-75.

social mission, fusing firm bourgeois-individualistic ideological grounds, the basics of cooperative ideology, with formalized organizational structures, institutions and publications. In the following sections I shall describe the various forces that shaped the formation of the Jewish credit cooperative movement in Mandatory Palestine.

C. The International Credit Cooperative Movement

Credit cooperatives were first introduced in Germany in the mid-1800s, by people who needed loans for their business operations. Such individuals formed a membership cooperative, and each member deposited a certain amount of money, which constituted the basis for loan provision. The loan was to be secured not by the borrower's property but through the promise of mutual support of members' labor.⁴¹ There were two major models for credit cooperatives, reflecting the activities of their founders — Hermann Schultze-Delitzsch and Friedrich Raffeisen. The Schultze model was established mainly for the urban low- and middle-class workers and businesses, while the Raffeisen cooperatives were established mainly in rural areas and served farmers and other agricultural workers. Although differing in some basic aspects,⁴² both types expanded beyond Germany in the early twentieth century, becoming the prevailing models for credit cooperatives in Western countries, East European countries, and some British colonies (including India).⁴³

The Schultze and Raffeisen models of credit cooperatives were introduced

41 ZBARSKY, *supra* note 17, at 90.

42 The main differences were: the Schultze model accepted the principle of limited liability of its membership (retaining the notion of the separation between membership and control, a feature that distinguishes limited liability companies and limited liability cooperatives), and allowed persons to be members of more than one credit cooperative. The Raffeisen model was usually implemented in a designated geographical area, did not allow membership in more than one credit cooperative, and rejected the idea of limited liability of members in the cooperative. On this point, see Timothy Guinnane, *Cooperatives as Information Machines: German Rural Credit Cooperatives 1883-1914*, 61 J. ECON. HIST. 366 (2001); Karlinsky, *supra* note 10, at 248; ZBARSKY, *supra* note 17, at 90-92.

43 On the history, structure and current status of cooperative banking, see Wim Fonteyne, *Cooperative Banks in Europe — Policy Issues* (Int'l Monetary Fund, Working Paper No. 07/159, 2007), available at <http://www.imf.org/external/pubs/ft/wp/2007/wp07159.pdf>; Heiko Hesse & Martin Čihák, *Cooperative Banks and Financial Stability* (Int'l Monetary Fund, Working Paper No. 07/02, 2007), available at <http://www.imf.org/external/pubs/ft/wp/2007/wp0702.pdf>.

in Palestine around 1910 by the Anglo Palestine Company (APC, the Central Bank established by the Zionist Organization).⁴⁴ According to B. Ziv, by 1912 there were 45 "loan societies" in Palestine, operating according to the Schultze model, all supported by APC.⁴⁵ Interestingly, initial support for the first credit cooperatives in Palestine came from the early Jewish Zionist movement in Russia. The Odessa branch of "*Hovevei Zion*" (a late nineteenth-century Zionist movement established in Eastern Europe that supported immigration to Israel) provided an initial sum of 50,000 francs to these cooperatives, through APC. As I shall discuss in Section D, this support illustrates the second strong link between the credit cooperative movement in Mandatory Palestine and the Jewish Diaspora credit societies of the nineteenth and early twentieth centuries.

The bond between credit cooperatives in Mandatory Palestine and the worldwide credit cooperative movement strengthened over time. As credit cooperatives became more established and professionalized during the 1930s and 1940s and into the 1950s, they energized their movement and built its social identity by affiliation with the broader international cooperative establishment. Orderly reports from meetings of the International Cooperative Association (ICA, established in 1895),⁴⁶ discussions about cooperative education, constant reminders of its underlying values, reports about the development of cooperatives in different parts of the world, the celebration of international and local leaders and heroes⁴⁷ —

⁴⁴ See *infra* note 64 and accompanying text.

⁴⁵ ZIV, *supra* note 25, at 130-31.

⁴⁶ The International Cooperative Association currently claims that over 800 million people are members of cooperatives, with a significant economic impact on production, employment, financial deposits and GDP in various countries. See International Co-operative Alliance, *supra* note 14 (from the introduction: "ICA is an independent, non-governmental association which unites, represents and serves co-operatives worldwide. Founded in 1895, ICA has 221 member organisations from 85 countries active in all sectors of the economy. Together these co-operatives represent more than 800 million individuals worldwide.").

⁴⁷ See — as a typical example — the October 1968 newsletter of *Merkaz* — The Israeli Audit Union of the Credit Cooperatives, which includes in its international section the following articles: a report on cooperative education in the world, its rationale, schooling and training opportunities, government involvement, etc., Y. Ben Dror, *Hinuch Cooperativi be-Tnu'at ha-Cooperatzia ba-Olam* [Cooperative Education in the Cooperative Movement in the World], 11 CREDIT COOPERATIVE 26 (1968) (Hebrew); a report on the celebration of the 46th International Cooperative Day (which at the time encompassed 61 countries and over 60,000 cooperatives with over 220 million members), *Yom ha-Cooperatzia ha-Beinleumi ha-46* [The 46th International Cooperative Day], 11 CREDIT COOPERATIVE 30 (1968) (Hebrew);

all illustrate this establishment's inspiration to the Jewish credit cooperative movement in Mandatory Palestine. The leaders of the latter saw themselves — first and foremost — as being affiliated with other organizations working for a common cause, sharing the ideals of the worldwide cooperative movement. Special focus was put on the credit cooperatives' international movement and its commitment to the democratic provision of credit to the working class and the "masses," to values of mutual support and solidarity — underscoring these principles as distinguished from those applied by commercial banks in their usual operations.⁴⁸

D. Jewish Credit Cooperatives in the Diaspora

Alongside their connection to the international movement, credit cooperatives in Mandatory Palestine maintained a strong connection to the Jewish credit cooperatives that flourished in Eastern Europe between the two World Wars. Though other types of cooperatives were not prevalent among the Jewish communities in the Diaspora, credit cooperatives played a vital role in Jewish social life, beyond their direct financial function. Jewish credit cooperatives (and Jewish cooperative banks) — each incorporating tens of thousands of members — thrived in Bulgaria, Romania, Poland, Russia, Czechoslovakia, Lithuania, Bessarabia, and Latvia. In Poland alone, out of three million Jews who lived there before World War II, 500,000 were members of credit cooperatives.⁴⁹ Polish Jewish credit cooperatives, claims Oron, were a central pillar of Jewish life: they disseminated the ideas and principles of the cooperative movement and,

a report on the cooperative movement in India and Gandhi's heritage. David Gruman, *Ha-Cooperatzia be-Hodu — Halacha le-Ma'ase [The Cooperative in India — In Practice]*, 11 CREDIT COOPERATIVE 31 (1968) (Hebrew); and an article about Jewish credit cooperatives in Eastern Europe before the Holocaust. S. Oron, *Ha-Coopertatzia ha-Asharait be-Kerev Yehudey Mizrah Eropa Al Saf ha-Shoa 1938-39 [The Credit Cooperative Among Eastern European Jews on the Verge of the Holocaust, 1938-39]*, 11 CREDIT COOPERATIVE 36 (1968) (Hebrew).

⁴⁸ See, for example, a report on the state of credit cooperatives in Europe at that time: Walter Preus, *Credit Cooperatives in the World: 150th Anniversary of Raffeisen's Birth*, 15 CREDIT COOPERATIVE 22 (1969) (reporting on the existence of 500,000 credit cooperatives in 152 countries built on the Raffeisen model, incorporating 80 million members; and stating that credit cooperatives are relatively strong in Germany, Austria and Switzerland, but in most countries they do not reach more than 10 percent of the population, are quite weak in the Scandinavian countries, and hardly exist in Britain).

⁴⁹ Oron, *supra* note 47, at 37.

enjoying a semi-autonomous status, functioned at the same time as inter-communal, self-supporting institutions around which Jewish economic and social life revolved.⁵⁰

Further to this notable tradition, the Jewish cooperative movement in Mandatory Palestine drew a direct link between Eastern European cooperatives and those established in Palestine.⁵¹ The notion of renouncing the Diaspora and its Jewish institutions — so prominent within the Zionist Labor movement — was absent from this cognition. One explanation for this position was the similar social makeup of Diaspora credit cooperatives and of those in Palestine. Both were urban financial organizations, serving the middle class and the (petit) bourgeoisie: merchants, small businesses and traders. Karlinsky demonstrates the direct personal connection between the two continents, as leaders from Jewish cooperatives in Russia and Poland came to Palestine and worked in the newly established credit cooperatives in Palestine, teaching the novices the principles of being a cooperator and laying the ground for the professionalization of this occupation.⁵²

In sum, the continuity and connection between the Jewish Diaspora credit cooperatives and those established in Mandatory Palestine determined the status of the latter and, consequently, their political and economic power. Their refusal to reinvent themselves as new Jews by disconnecting from the Diaspora enhanced the marginalization of credit cooperatives and distanced them from the mainstream Zionist ethos and its economic and political apparatus.

E. Social Makeup — the Bourgeoisie: Trade and Small Business

Karlinsky attributes the relative weakness of the credit cooperative movement to the private, bourgeois makeup of its membership.⁵³ A growing body of research in the last two decades has documented the relative exclusion and marginalization of the bourgeoisie from political power in Mandatory Palestine, and later in Israel. Ben Porat, in his comprehensive review of the urban bourgeoisie — *Where Are All Those Bourgeoisies? The History of the Israeli Bourgeoisie* — points to the gap between the size of the private

50 The first Jewish cooperatives were established by the JCA. The first Jewish cooperative is said to have been established in Vilnius (under the Lithuanian regime) in 1897 by Jewish small traders and craftsmen. See ZBARSKY, *supra* note 17, at 108-10.

51 Karlinsky, *supra* note 10, at 251-52.

52 *Id.* at 254-55.

53 *Id.* at 246-47.

sector and its political influence.⁵⁴ In 1922, 82 percent of the population in Mandatory Palestine lived in urban centers, and the source of most capital was private.⁵⁵ Nonetheless, claims Ben Porat, since the urban bourgeoisie were only weakly affiliated with the Zionist movement's ideals, *as defined by the Labor party and establishment* — i.e., reinvigorating Jewish life and delineating the profile of the new Jew — their status remained subordinate.⁵⁶

The bourgeoisie came to Israel with the aim of preserving their old lifestyle and culture, and remained faithful to ideals of private property and wealth accumulation. Their interests centered on economic self-interest rather than the collective Zionist project. The bourgeoisie renounced political aspirations to become a ruling class, as long as there was no real threat to their interests. Despite not being part of this establishment, they depended on the resources and support of the Labor movement.⁵⁷

Bettelheim, who has explored the topic of trade associations in Jerusalem and Tel Aviv, also describes feelings of inferiority and weakness among tradesmen, craftsmen and other occupations embodying the ideas and practices of a free market economy, competition, and private entrepreneurship. They encountered massive bureaucratic hurdles in getting licenses and permits, discrimination in government tenders, and selective law enforcement — barriers apparently not imposed upon those connected with the Labor movement and party.⁵⁸

Thus, the *lack of a sound, Labor-inspired, Zionist ideological basis* was a real disadvantage to the credit cooperative membership and, consequently, to the movement: largely advocating self-interest, they did not share the collective ethos of the agricultural Labor establishment.

54 AMIR BEN PORAT, HEICHAN HEM HA-BURGANIM HA-HEM? TOLDOT HA-BURGANOT HA-YISRAELIT [WHERE ARE ALL THOSE BOURGEOISIES? THE HISTORY OF THE ISRAELI BOURGEOISIE] 88-89 (1999) (Hebrew).

55 Over 70 percent of the capital in the 1930s was private. The fourth and fifth *aliyot* (waves of immigration from Europe) brought the bourgeoisie, and with them not only real capital but also the cultural dimensions of the petit bourgeois (fourth *aliya*), and the cultural assets of the German urban bourgeois (fifth *aliya*). *Id.* at 78-80.

56 As I will explain in the next Section, Ben Porat claims that the relationship to private capital was not directly suppressive, but more complex. The Labor movement and national institutions needed the private sector and indeed supported it by various direct and indirect means, thus laying the groundwork for a capitalist economy; however, at that stage the private sector was excluded from direct involvement in the political establishment, where distributive decisions were made.

57 YAEL YISHAI, INTEREST GROUPS IN ISRAEL 125 (1986).

58 AVI BETTELHEIM, THE TRADESMEN: THE STORY OF COMMERCE IN ERETZ ISRAEL, 70 YEARS TO THE BOARD OF COMMERCE 239 (1990).

F. The Zionist Mission

Even though the genealogy of credit cooperatives did not derive from the conventional overall Zionist "meta-narrative," credit cooperatives nonetheless considered themselves deeply involved in the struggle for national revival and state-building. They attempted to carve out a unique niche for themselves in the collective mission. It was not simple to transform a private-market activity into a national goal, but leaders of the credit cooperative movement tried to do so, constantly debating their societal role within the Zionist framework, beyond the immediate financial service to their members.

In 1939, for example, the general assembly of the Jerusalem Savings and Loans Cooperative began its meeting with a commemoration of the Jews killed that year (by Arab insurgents). It went on to denounce the British "*White Book*," which restricted Jewish immigration to Palestine and the purchase of land by Jews. The business affairs of the cooperative were part of the nationalist struggle: the growth of the Jerusalem credit cooperative, announced the chair, from 40 members in 1919 to over 5,000 members in 1939, was the answer that "Jerusalem" was sending to "London." It was proof that the Jews would continue to "live and build through self-created institutions of savings and loans societies."⁵⁹ Similarly, the general assembly of the Ekron (a small agricultural town near Rehovot) credit cooperative also mixed private and public affairs. In 1945 it began its annual meeting by acknowledging the 100th anniversary celebrations of the worldwide cooperative movement. Immediately associating this international event with the Zionist mission of building the country, the chair exclaimed: "[T]he land of Israel is being built for the most part by means of cooperatives."⁶⁰

During 1943-1946, *Kupat Milve Vehisachon Hamizrah* (the Savings and Loans Cooperative of the Yemenite Community in Tel Aviv) debated the question of its commitment to relieving the plight of the immigrants and refugees arriving in Palestine from Yemen and Aden. Some members supported a proposal to obligate each of the 600 cooperative members to contribute 1 *Lira* to assist the immigrants; others objected, claiming the money would be better used to build an office for the cooperative and hire

59 Protocol of the Annual General Assembly of the Savings and Loans Cooperative Society, Ltd., (May 17, 1939) (on file with author).

60 Protocol of the Annual General Assembly of the Savings and Loans Society Ekron (Feb. 7, 1945) (on file with author).

more staff, and stating that the cooperative "is an institution that provides credit, not philanthropy."⁶¹

National and public events, then, frequently percolated into the official meetings and debates of the credit cooperatives. The latter argued about their role in the absorption of new immigrants, viewed themselves as part and parcel of the Zionist mission of "building the country," commemorated Jewish victims of the struggle, and in general emphasized their connection to the prevailing Zionist mission and narrative, and all this in addition to what they considered their most unique contribution — furthering the ideals and practices of the international credit cooperative movement and of equal access to credit and loans.

G. A Public Mission Within the Private Sphere

Beyond considering themselves part of the Zionist undertaking, the credit cooperatives also insisted they were fulfilling an additional *public* mission. They were taking part in an effort to promote the values of the international credit cooperative movement, to restrain capitalism and its callous operation, by offering credit democratically and with regard to the values of social solidarity. To substantiate this claim, it is necessary to describe the credit cooperatives' relationship with the banking system in Mandatory Palestine.

Credit cooperatives need larger banking institutions, especially in times of crisis,⁶² and in Mandatory Palestine they relied on the emerging banking system for this purpose. Gross explains that a central goal of the Zionist movement was to establish a banking system to help create the basic conditions for economic development in Palestine.⁶³ The largest financial institution at the time, APC (subsequently named Leumi Bank of Israel), was founded in 1902 by the World Zionist Organization, and owned by the Jewish Colonial

61 Protocol of the Annual General Assembly of the Savings and Loans Cooperative Hamizrah (Aug. 25, 1943) (on file with author); Protocol of the Annual General Assembly of the Savings and Loans Cooperative Hamizrah (Dec. 10, 1946) (on file with author).

62 Credit cooperatives need the backup of the state financial system. In order to survive, they must be supported by financial institutions (most commonly these are cooperative banks) and other financial support systems (such as cooperative alliances). On the vital importance of cooperative banks, see ZBARSKY, *supra* note 17, at 100-04.

63 Nahum Gross, *Jewish Banking and Market Growth in the Mandate Period*, in *ECONOMY AND SOCIETY IN THE MANDATE PERIOD: 1918-1948*, *supra* note 10, at 217, 219-36.

Trust.⁶⁴ Though registered in London, APC operated only in Palestine and was considered the main bank of the Zionist movement. APC and later on Bank Hapoalim operated "ideologically" — they aspired to further nationalist as well as sectarian interests, alongside their goal of profit-making.⁶⁵

During the 1920s and 1930s, numerous local and foreign commercial banks were established alongside APC. The rapid growth of these small banks (their number peaked at 80 in 1935) resulted from the absence of a central monitoring bank and the loose regulatory framework supervising their operation.⁶⁶

Within this financial system, a unique niche was reserved to the credit cooperatives; they continued to expand and played a vital role in the banking industry.⁶⁷ Credit cooperatives offered banking services in locations and to clients not well served by the commercial banks, who were hardly interested in banking for small businesses, merchants, craftsmen, and other small industries and urban service providers. The commercial banks had no branches in the peripheries, were closed to the public in the afternoons (when small businesses often conduct their banking activities), did not encourage households to open savings accounts, and in general were less oriented towards clients who needed small, short-term loans.⁶⁸ The banks preferred to serve larger companies: the Electric Company, institutions of the *Histadrut*, and other profitable entities and individuals.⁶⁹ Even though the banking system vouched for the credit

64 On the Anglo Palestine Company and the early stages of banking in Israel, see HETH, *BANKING IN ISRAEL*, *supra* note 9, at 20-30; NISSAN LEVITHAN & HAIM BARKAI, *THE BANK OF ISRAEL, FIFTY YEARS OF STRIVING FOR MONETARY CONTROL* (2004); ISRAEL BAR YOSSEF, *THE BANK OF ISRAEL IN THEORY AND PRACTICE* 6 (1985); Gross, *supra* note 63; ZIV, *supra* note 25, at 74-127. On the Jewish Colonial Trust, see Jewish Colonial Trust, <http://www.jct.co.il/index.html> (last visited Aug. 10, 2009).

65 Gross, *supra* note 63, at 234; ZIV, *supra* note 25, at 67.

66 In 1948 there were 24 registered banks in Israel, a sharp decline from the peak of 80 registered banks in 1935. The decline in the number of banks resulted from the combination of an economic boom during the 1940s and a tighter regulatory regime introduced in 1936 by the British Mandate Government. HETH, *BANKING IN ISRAEL*, *supra* note 9, at 22-23; Gross, *supra* note 63, at 217.

67 In 1928 credit cooperatives held more financial assets than the five private Jewish banks that operated in Mandatory Palestine (not including APC). HETH, *supra* note 1, at 21.

68 Gross, *supra* note 63, at 219; Karlinsky, *supra* note 10, at 241; HETH, *supra* note 1, at 48.

69 This attitude is exhibited in the publication celebrating the fiftieth anniversary of the establishment of Bank Leumi (formerly APC): "When the bank was the only source of credit, anyone who needed a loan turned to it . . . harsh criticism was voiced at [the bank] for providing larger credit to big and wealthy borrowers than to

cooperatives in times of crisis,⁷⁰ its everyday business was driven by a strong corporate-profit motive, and it paid little attention to populations and groups who could not obtain credit, or to other social or egalitarian concerns. As Ben Porat explains, the capitalist infrastructure of the banking system was laid by the socialist and nationalist apparatus of the Labor movement.⁷¹

Oddly enough, the small merchant or tradesperson — whose only concern was the accumulation of personal wealth and the retention of private property, and who never claimed to share any of the socialist ideology of the Zionist Labor movement — encountered the downside of capitalism through the evolving banking system in Mandatory Palestine. Zbarsky — a strong supporter of the private Jewish cooperative movement — described the fate of the small (micro) businessman: crushed by the mighty forces of capitalism, he could compete with neither the factory owner equipped with expensive machinery, who can produce complicated and cheap goods, nor the "middle man" who controls the market and appropriates a lion's share of his income. At that point, he "is succored by the credit cooperative, which has developed to the highest form of economic life, [operating] in areas where the capitalist banks, masters of the material order alone, had assumed unlimited control."⁷²

Credit cooperatives thus took upon themselves a public mission within the private sphere. They stepped in with a firm worldview, the values and the know-how of cooperative banking to address the failures and inadequacies of the emerging banking system towards the needs of the less privileged.

H. Summary

During the Mandate period, credit cooperatives constituted important financial institutions within the Jewish population. Their emergence was a partial and limited form of institutional transplantation of the German credit cooperatives, which served as models for other countries to follow.⁷³

low-income borrowers . . . all this ended, in fact, when personal loans were provided by the credit cooperatives." HETH, *supra* note 1, at 48 n.4; *see also* Gross, *supra* note 63, at 234.

70 During World War II and the Italian-Ethiopian War of 1936, a period of acute financial crisis in the region, credit cooperatives received crucial assistance (a line of credit) from APC, enabling them to avoid a financial breakdown due to massive withdrawal of deposits by the public. Karlinsky, *supra* note 10, at 276.

71 BEN PORAT, *supra* note 54, at 88-89.

72 ZBARSKY, *supra* note 17, at 14.

73 *See* Guinnaine, *supra* note 4.

Partial, because credit cooperatives in Palestine were shaped and formed by the interplay of a variety of political, social and economic forces during this period in the region. As such, they provided loans and credit to groups and individuals who were not well served by commercial banks, operated in the periphery, and saw themselves as providing not only important financial services, but also an alternative socioeconomic worldview, set between socialism and capitalism. Despite their relative distance from the mainstream Labor establishment, credit cooperatives managed to articulate their national role, fusing private interests with a "public calling." The legal framework regulating banking institutions enabled credit cooperatives to maneuver in a sphere of autonomous self-regulation, with minimal accountability to the official Registrar in the Mandatory state regime. This sphere narrowed dramatically after the establishment of the state, changing the playing field for the credit cooperatives.

II. CREDIT COOPERATIVES IN EARLY ISRAELI STATEHOOD

A. Changes in Banking Policy and Their Effect on Credit Cooperatives

In 1969 a lively debate took place in *The Credit Cooperative*, the newsletter of the *Merkaz*. In a series of essays entitled *The Credit Cooperative: What Will Be Its Fate?* Abraham Shtacher, a prominent member of the *Merkaz*, voiced hope that the government would change its attitude towards "the guardians of the credit cooperative," who "to this day watch over the ember of the credit cooperative so it will not die. . . ." Hopefully, he stated, the Bank of Israel, the Israeli economic leadership and the public would realize "the value and importance of credit cooperatives in Israeli economy and society."⁷⁴

Shtacher's essays were published against the background of a growing comprehension within the credit cooperative establishment of its fate. Contrary to developments in the West during the 1960s, with credit cooperatives expanding their social and financial role, the situation in Israel was clearly moving in the opposite direction.⁷⁵ The number of

⁷⁴ Shtacher, *supra* note 5, at 2-4.

⁷⁵ The 1970 ICA meeting documented the expansion of credit cooperatives in Europe and in other developing countries. Although the number of credit cooperatives was declining, this was due to mergers and not to lower membership rates. The affluence of credit cooperatives was largely attributed to governmental policies that supported their activities and provided an accommodating legal and financial environment that enabled the cooperatives to develop while maintaining their cooperative principles.

credit cooperatives and their membership rates declined continuously, while many cooperatives changed their legal structure and reincorporated as limited liability companies. The concern was that credit cooperatives were on the verge of extinction, and that "the cooperative spirit" was dying.

Both external and internal factors accounted for this decline. Externally, the Bank of Israel and the government took steps to centralize the banking system through mergers and standardization, a policy disadvantageous to credit cooperatives. From within, the movement was losing its rank and file. Credit cooperatives, both large and small, were "crossing the lines" and becoming profitable "capitalist" banking institutions. Some cooperative directors had become bank directors — a complete abandonment of the cooperative worldview and mission. The crux of the problem, lamented Shtacher, lay within the weakening "spirit" of the credit cooperative movement.⁷⁶

B. Centralization and Standardization — A Disparate Impact on Credit Cooperatives

During the British Mandate there was no central bank supervising banks, and the regulatory framework in this area was relatively loose. This situation changed significantly following the founding of the state and the establishment of the Bank of Israel in 1954 as its central monetary institution.⁷⁷ The Bank of Israel took immediate steps to tighten supervision over the banks, largely in order to avoid inflation, in recognition of the banks' extensive powers to influence the supply and distribution of money and credit.

The most immediate change introduced by the Bank of Israel was the determination of liquidity reserves. Liquidity reserves are an important monetary tool to control the amount of money in the market (as a means of avoiding inflation), in addition to being a safeguard for the protection of clients' deposits. Until 1950 the level of fractional reserves was set at 45 percent — for banks and credit cooperatives alike. This rate was raised significantly for banks in the early 1950s, to levels varying between 70-100 percent, depending on the type of deposits held by financial institutions.⁷⁸ Until 1958 credit cooperatives enjoyed a lower level of reserve requirements

See Natan Braude, CPA, *The Second International Conference of Savings and Credit Cooperatives*, 18 CREDIT COOPERATIVE 26 (1970).

⁷⁶ Protocol of the General Assembly of *Merkaz*, the Audit Union of Credit Cooperatives 1, 5 (July 27, 1963) (on file with author).

⁷⁷ HETH, *supra* note 1, at 87; Gross, *supra* note 63.

⁷⁸ HETH, BANKING IN ISRAEL, *supra* note 9, at 91-93.

(60 percent on deposits), but thereafter this benefit was eliminated and their status was equated with that of commercial banks.

This regulatory-policy change was not easily enforced upon the banks. Levithan and Barkai describe how, despite formal limits on credit level and liquidity requirements, banks often disregarded these regulations and monetary instructions.⁷⁹ The Bank of Israel therefore found it necessary to standardize its regulation and apply unified procedures for all financial institutions — including credit cooperatives — to enhance enforcement of the new rules.

Equalizing liquidity requirements for commercial banks and credit cooperatives was detrimental to the latter, and imposed a tremendous burden upon them. The difficulty stemmed from the fact that cooperatives' equity was low — comprised almost exclusively of members' deposits. Credit cooperatives could not increase their equity in order to meet capital adequacy requirements by issuing securities, stock or bonds. As for banks — the capital they raised through the securities market did not increase their capital adequacy requirements, and was thus fully available for expanding the banks' business, and increasing their profits. Due to the fractional reserve requirements, the cooperatives felt they were being "choked." They lacked operating capital, either for reinvestment in the cooperative or to provide additional loans to their members.⁸⁰

It is hard to overestimate the importance of this factor. During the annual meetings of the credit cooperatives in the 1950s and 1960s, they recurrently complained that the Bank of Israel was not accommodating their special needs. On the one hand, the Bank of Israel treated cooperatives in the same way as banks; but on the other hand, their structure and financial opportunities together with the Bank of Israel's "indifference" put them at a disadvantage and lowered their chances of financial sustainability.⁸¹ Credit cooperatives were also denied licenses to conduct transactions in foreign currency.⁸² This prevented them from receiving foreign deposits and investments, put them at a disadvantage compared to commercial banks, and diverted their clients to these latter institutions.

79 LEVITHAN & BARKAI, *supra* note 64, at 90-96.

80 A summary of these conditions imposing hardship on credit cooperatives can be found in Letter from Jaffa Tel Aviv Mutual Fund to A. Schweitzer, Coop. Registrar (Jan. 1, 1964) (on file with author).

81 *Id.*

82 *See, e.g.*, Protocol of the General Assembly of the Jaffa-Tel Aviv Mutual Fund 7-8 (Mar. 28, 1963) (on file with author) (address by Mr. Gordon, on behalf of the Board of Directors).

Moreover, the Bank of Israel adopted a rigorous policy intended to facilitate consolidation and mergers in order to reduce the number of small banks that continued to operate during the early days of Israeli statehood. Licenses for new banks were difficult to obtain, and the Bank of Israel encouraged banks to open branches in different locations.⁸³ The policy of consolidation and centralization had a powerful effect on credit cooperatives. During the years 1950-1954 the number of credit cooperatives rose somewhat, to 95 associations, but soon thereafter the trend shifted and credit cooperatives began to fold their operations: some were bought by banks, while others were transformed into limited liability companies or consolidated with other cooperatives. In 1961 only 27 cooperatives remained active, and their number continued to drop persistently.

The credit cooperatives had begun to encounter competition from commercial banks. Contrary to the situation during the British Mandate, commercial banks started taking an interest in catering to the needs of small businesses, individuals with modest means, and the petit bourgeoisie. They expanded to the periphery, advertised their operations, and offered a bundle of financial services to their clients in a "one-stop" deal. Being significantly more profit-driven than the cooperatives, the banks increased their earnings. This gap troubled the cooperative managers, and they constantly debated the issue of profitability.

The need to compete with the profitability of commercial banks brought to the surface a difficult dilemma for the cooperative establishment: organizational success was measured solely by profit rates. The relatively low profits of some cooperatives clearly prompted them to question their sustainability within the cooperative form. In others, though, members objected to this move, arguing that cooperatives need not be assessed by profit rates alone, since they contributed distinctive added value: equitable access to credit, democratic governance of financial institutions, mutual responsibility among members, reinvestment in the cooperative in preference to dividend distribution, and, in general, a shared commitment to further "the common good" — a basic principle of the cooperative movement.⁸⁴

Additional factors contributed to this decline. Beside the Bank of Israel's disregard for their fate in its implementation of standardization and

83 HETH, *BANKING IN ISRAEL*, *supra* note 9, at 48-49. In 1950 there were 23 commercial banks in operation, and 26 in 1961, but according to Heth there were structural changes in the ownership of banks which reflected centralization, although initially this trend was not reflected in the number of banks.

84 For opposing views on the topic, see *infra* text accompanying notes 106-15, during the debate of the Jaffa-Tel Aviv Mutual Fund.

centralization measures, governmental policy was unfavorable towards the credit cooperatives. During the Mandate period credit cooperatives had been granted special privileges, including exemptions from certain taxes and fees; all of these were cancelled in the 1950s as part of the standardization process. Credit cooperatives experienced direct discrimination against them by the government. Despite the cooperatives' ability and willingness to provide various financial services, it favored commercial banks in channeling public funds, subsidies, loans and other governmental payments. Representatives of credit cooperatives asked for a fair share of these banking activities, but were ignored; the government relied exclusively on commercial banks for its banking activities. Arguably, the cooperatives' relative distance from the Labor Party establishment, discussed in Part I, continued to set them at a disadvantage.

In addition to the external factors stemming from the monetary and banking systems, which were adversely affecting credit cooperatives, a problem emerged from within: the dwindling commitment among members to the cooperative mission. The conversion of cooperatives to limited liability companies, a widespread phenomenon during this period, shows how profound the problem was.

C. From Cooperatives to Limited Liability Companies — Law, Structure and Values

Haim Avni, CPA, identified the source of the credit cooperatives' decline in *the law* governing their operation. The Cooperative Ordinance, he explained — unlike the Companies Ordinance — prohibits cooperatives from issuing stocks and bonds to raise capital. Combined with the standardized requirements regarding fractional reserves, that put credit cooperatives at a significant disadvantage compared to banks.⁸⁵ The solution, Avni suggested, was to change the law and allow cooperatives to raise capital in the market. Yair Yakir, who served as the Cooperative Registrar in the 1950s, also believed that if cooperatives would be allowed to sell their (membership) stock in the stock market, the problem of capital could be alleviated, without compromising the cooperative principles.⁸⁶ Continuing the discussion a few months later, Shtacher — who strongly believed in the prospects of credit cooperatives due to their invaluable social role — also identified *law* as a constraining factor

⁸⁵ Haim Avni, *In Merkaz and the Cooperatives: Strengthening Credit Cooperatives — How?*, 15 CREDIT COOPERATIVE 32 (1969).

⁸⁶ Yair Yakir, *Three Points for a Wake-up Journey*, 13 CREDIT COOPERATIVE 8 (1969).

in relation to the equity problem. Law limited the range of services credit cooperatives could offer the public, he stated; it was the "mere [bad] luck" of the credit cooperatives that the Cooperative Ordinance did not permit them to issue stock and bonds or provide a range of financial services to their members.⁸⁷

To be sure, the legal structure governing credit cooperatives was restrictive: it prohibited the raising of capital beyond members' deposits, as it constrained the conveyance of membership stock, reception of foreign investments, and issuance of different types of stock. Dividend distribution was proscribed. Compared to commercial banks, not confined to such conditions, credit cooperatives were indeed disadvantaged.

These constraints, however, were not "mere luck," as Shtacher suggested. The cooperative framework was not just a neutral or technical legal scheme, which had to be converted to accommodate a new fiscal and political order. The ordinance structured and reflected a set of vital connections and relations among cooperative members, and between the members and the outside world. Changing the legal framework meant changing these commitments and values, incorporated through and embodied within the legal doctrine that regulated cooperatives.

Converting a cooperative into a limited liability company entailed minute and standardized technical work (conducted by commercial and corporate lawyers). Section 256 of the Companies Ordinance of 1937 laid out the process and requirements for "reorganization" as a limited liability company.⁸⁸ Nothing in this technicality, however, gave any clue regarding the profound changes that accompanied this legal transformation, underlying the different values of these two legal entities.

In mainstream corporate law, the limited liability company is a strong manifestation of the principles and the value of private property. For many years the consensual mainstream view within legal scholarship has been that corporate law is based on *shareholder primacy* and *the maximization of shareholder value*. The theoretical basis of this supremacy lies, first

⁸⁷ See sources cited *supra* note 5.

⁸⁸ Companies Ordinance, 1929, 1 Hukei Eretz Yisrael 155, as amended 1937, Iton Rishmi (Official Gazette of the Government of Palestine) add. A 660, § 256. The plan had to be confirmed by the Cooperative Registrar and to ensure the interests of the cooperative's creditors. Following the Registrar's approval, the general assembly of the cooperative's membership had to approve the reorganization plan. The plan itself was to allocate the type of equity (shares) of the company, the manner of share distribution (between the cooperative members and outside investors), the rights of each type of shareholder, and the articles of association of the company.

and foremost, in the preeminence of the shareholders' property rights. They own the corporation, and have a right to enjoy their possession to its largest possible extent. Shareholder interests prevail over those of clients/customers, employees or the public at large. The separation between ownership and control — one of the basic foundations of the company — is a second basic principle of the shareholder supremacy model and serves to ensure the supremacy of shareholder rights. Due to the risk that the company's managers might run the corporation in their own interests instead of shareholders', corporate legal doctrine requires managers to owe their highest fiduciary duties to the shareholders and to maximizing their interests, i.e., their profits.⁸⁹

Accordingly, in commercial banks the interests of shareholders take preference over those of the customers/clients who receive financial services. They also precede the interests of other "stakeholders" (as this term has been coined by critics of the mainstream approach⁹⁰) such as the bank's workers or the general public (stakeholders of "the common good"). The company can issue different types of stock to its holders according to their investment, and grant differential voting rights and privileges (such as the right to appoint directors) according to the quantity and type of shares they hold.⁹¹ The company is registered with initial nominal capital, which can be changed following a certain procedure, and it can issue stock and bonds to the public.⁹² Shares, bonds and options are transferable, unless restricted by the company's regulations,⁹³ and shareholders' liability for the company's

89 On the principles of mainstream corporate law, see ADOLF A. BERLE & GARDINER C. MEANS, *THE MODERN CORPORATION AND PRIVATE PROPERTY* (1932); D. Gordon Smith, *The Shareholder Primacy Norm*, 23 J. CORP. L. 227 (1998); Steven M.H. Wallman, *Understanding the Purpose of a Corporation: An Introduction*, 24 J. CORP. L. 27 (1999); William T. Allen, *Our Schizophrenic Conception of the Business Corporation*, 14 CARDOZO L. REV. 261 (1992). In Israeli law this principle has been incorporated in the new Companies Law, 1999, S.H. 189, as amended. Section 11 of the Companies Law states: "The purpose of a company is to maximize its profits through business considerations, and it may take into account among these considerations . . . the interests of its creditors, employees and the public."

90 On the critique of the mainstream view and development of alternative corporate approaches such as "social responsibility," "social accountability," and "stakeholder theory," see Kelley Y. Testey, *Linking Progressive Corporate Law with Progressive Social Movements*, 76 TUL. L. REV. 1227 (2002).

91 Companies Law § 183.

92 Originally this authority was granted in sections 95-98 of the Companies Ordinance, currently in sections 288-292 of the Companies Law.

93 Companies Ordinance, §§ 17, 31-33; Section 293 of the Companies Law creates a presumption that stocks, bonds or options to purchase them are transferable.

debts and other financial obligations is limited, unless otherwise specified in its regulations.⁹⁴ Clients/customers who deposit their money in the bank do not have any proprietary rights in the company, nor managerial powers. The advancement of the "common good" is secondary, if it exists at all, to the bank's routine operation.⁹⁵

Clearly, credit cooperatives are based on a different rationale. Cooperatives in general and credit cooperatives in particular were formed as an alternative to the "capitalist" model embodied in the corporate company. Their structure — embodied in the legal entity of a cooperative — incarnates a set of institutional relations both within the organization and with external parties, which differs substantially from the limited liability company.

Whereas in a banking corporation there is no necessary correlation between ownership (shareholders) and clientele (loan seekers), members of the cooperative are its owners and its clients. The cooperative uses membership fees — considered a deposit rather than an investment — to issue loans to other members in times of need.⁹⁶ Section 36 of the Cooperative Ordinance states that "[t]he cooperative is prohibited from lending money to anyone who is not a member," and section 37 prohibits the cooperative from borrowing or accepting deposits from non-members. Additional restrictions disclose that profit-maximizing is not the cooperative's central goal in its ordinary course of business.⁹⁷ Each member has one vote, regardless of the size of his/her deposit,⁹⁸ and there is a limit on capital concentration among

94 Companies Ordinance § 4; Companies Law § 34.

95 This of course has been a matter of debate from the early days of the corporation. See Allen, *supra* note 89 (describing the "social entity concept" of the corporation). It has also been the basis of the critique under the "progressive corporate law" approach. See Testey, *supra* note 90; David L. Engel, *An Approach to Corporate Social Responsibility*, 32 STAN. L. REV. 1 (1979); Kent Greenfield, *Corporate Social Responsibility: There's a Forest in Those Trees: Teaching About Corporate Social Responsibility*, 34 GA. L. REV. 1011 (2000); Ronen Shamir, *Corporate Responsibility and the South African Drug Wars: Outline of a New Frontier for Cause Lawyers*, in THE WORLD CAUSE LAWYERS MAKE: STRUCTURE AND AGENCY IN LEGAL PRACTICE 37 (Austin Sarat & Stuart Scheingold eds., 2002).

96 Section 4 of the Cooperative Ordinance, 1933, 1 Hukei Eretz Yisrael 330, states that the purpose of the cooperative is to act in order to assist in the self-help, mutual help and savings of people with common economic interests in order to improve their lives, businesses and means of production.

97 For example, section 38 of the Cooperative Ordinance restricts business transactions with non-members unless allowed by the cooperative's regulations.

98 *Id.* § 16(1).

members.⁹⁹ Members cannot transfer their membership-share to others,¹⁰⁰ and do not have a right to receive profits (dividends) if the cooperative is profitable. Profits of the cooperative are usually reinvested in the cooperative or set aside for reserves.¹⁰¹ The cooperative is allowed to donate a part of its profits to charity or to a public cause.¹⁰²

It is therefore apparent that converting a cooperative into a company entails more than just submitting a "reorganization plan," as required by law. It is a substantive transformation that alters the values and relations embodied in the structure of a cooperative. Therefore, the widespread conversion of credit cooperatives into banks, which took place during the 1960s, reflects an ideological shattering of the spirit underlying this financial institution. The case of the Jaffa-Tel Aviv Loans and Savings Mutual Fund in 1965, described in the next Section, illustrates the magnitude of this breakdown.

D. The Jaffa-Tel Aviv Loans and Savings Mutual Fund

The Jaffa-Tel Aviv Loans and Savings Mutual Fund (TAMF) was established in 1918. In 1922 it began providing banking services and over time became the largest credit cooperative in Mandatory Palestine, and then in Israel. In 1924, 36 percent of all credit cooperative members belonged to TAMF, and in 1945 the rate was about 14 percent.¹⁰³ Karlinsky explains that the overall policy of TAMF was conservative and cautious. Its directors were well versed in the theoretical and professional know-how of credit cooperative management. They believed that TAMF was "a 'classic' credit cooperative whose role was to secure the monies of the urban middle-class person."¹⁰⁴ TAMF was careful to maintain adequate liquidity rates and constantly expanded its reserves.

TAMF continued to grow after World War II and entered the era of Israeli statehood as the strongest among the credit cooperatives. Located in Tel

99 Section 5 of the Cooperative Ordinance restricts each member to a maximum of one fifth (1/5) of capital in the cooperative.

100 *Id.* § 17.

101 *Id.* §§ 39(1), 39(2).

102 *Id.* § 42. As for companies, the authorization to take into account the public interest (beyond the shareholder interest) was added in 1999 to the new Companies Law of 1999, but did not exist in the Mandatory Companies Ordinance that preceded that law. The authority of the cooperative to do so was included in the ordinance originally, illustrating the connection between the cooperative and the "common good."

103 Karlinsky, *supra* note 10, at 281-82.

104 *Id.* at 283.

Aviv, Israel's growing financial and commercial center, and well run by professional cooperators, TAMF's membership and capital grew during the 1950s and early 1960s. However, already by 1963 the atmosphere within the cooperative had changed: its relatively low profitability became the central topic of debate. Despite constant growth in membership and capital, stated its then-director Matityahu Gordon, TAMF was lagging behind the banks in profits: "[A] lot has been said about the banks' profits, which are high," he stated. "Unfortunately, we cannot pride ourselves with easy profits; it is with great labor that we are able to accumulate profit."¹⁰⁵ Gordon laid out the reasons for this difficulty: TAMF had been refused a license to trade in the foreign currency market, liquidity requirements were raised (from 64 to 67 percent), and there were other limitations on interest rates which affected profitability. Other factors were of a more general nature — the rise of the cost of living index, and TAMF's operational inefficiency compared to banks.¹⁰⁶ Responding to this grievance, Molcho (a member participating in the meeting) voiced a different opinion, stating that "a credit cooperative like our own need not aspire to gain profits, and profits do not determine its progress."¹⁰⁷

Throughout the discussions during this period, the cooperators identified "the cooperative framework" as a major aspect of the problem, claiming that its legal structure was impeding the cooperative's development. The cooperative structure, they reported, restricted TAMF's ability to raise capital in the stock market, whereas a company "issues securities one day and collects a fortune the next." "[O]ur institution cannot do that," they explained, "our membership fees are not accounted as equity by the financial institutions . . . we could pay dividends like other banks if we had stock that together with our deposits would show large capital . . . [b]ut our hands are tied as we are a cooperative."¹⁰⁸

A few months later, in the General Assembly of the *Merkez*, a member of TAMF (Dr. Heller) explained why the large cooperative had no choice but to convert into a company and become a commercial bank. The debate over the topic was heated, touching upon the core mission of credit cooperatives and its relation to their legal structure. The atmosphere during the meeting was highly critical of "reorganization"; opponents rejected the position that it was necessary to change the legal form of the cooperative to overcome the difficulties faced by TAMF. Shtacher exclaimed:

105 Protocol of the General Assembly of the Jaffa-Tel Aviv Mutual Fund, *supra* note 82, at 8.

106 *Id.* at 10.

107 *Id.* at 11.

108 *Id.* at 8.

The illusion that our legal status is a hindrance is misleading. It only reveals the depression within the cooperative community . . . there is no reason to leave the cooperative because we cannot do all [banking] activities. The credit cooperative theory did not negate such activities. On the contrary, they gave us the possibility of taking care of the weak person. Now capital has appeared . . . we will not bow down and say that because our capital is low and we cannot issue stocks, we will do nothing. We will neither rest nor stay silent and we will give it thought and also consult with lawyers. The cooperative law is not something that cannot be changed and adapted to life.¹⁰⁹

Freiman, another devoted member of the *Merkaz*, interjected: "How painful it is for me to hear the words of Heller! The last Mohican at TAMF . . . we knew that in the last few years [he] has been fighting against those ideas that began to 'cook' . . . at TAMF against escaping from the cooperative and changing the legal status."¹¹⁰ Referring to the trend of converting credit cooperatives into banks, Shtacher concluded:

I believe [those] who have behind them a full history of cooperation should not hastily throw into the ocean their '*talis* and *tefilin*' [Jewish religious articles], mistakenly thinking that by doing so they will save the ship from sinking. On the contrary, the ship might go down with those holding the '*talis* and *tefilin*' together with their defeatist spirit.¹¹¹

Echoes of the dramatic meeting reached TAMF, which was quick to rebut the accusations of betrayal. The directors of TAMF assured the *Merkaz* that whether as a cooperative or a bank they would be committed to the values of democratic, popular banking, serving all segments of society and remaining loyal to the values of solidarity, fraternity and mutual help.¹¹²

On January 1, 1964 the directors of TAMF approached the Cooperatives Registrar and officially notified him of their decision to reorganize as a limited liability company. At the time, TAMF had 75,000 members and the size of its equity did not lag far behind the three large commercial banks. The directors gave all the reasons for this move, and mentioned another significant problem: government discrimination between the banks

109 Protocol of the General Assembly of *Merkaz*, the Audit Union of Credit Cooperatives 5 (July 29, 1963) (on file with author).

110 *Id.* at 7.

111 *Id.* at 9.

112 Letter from Board Members of TAMF to A. Schweitzer, Coop. Registrar (Nov. 20, 1963) (on file with author).

and credit cooperatives: "Banks that are significantly smaller than our institutions and with less financial assets are being allowed to act in the foreign currency market," they complained. Government loans, they added, were being channeled through a small number of banks, while TAMF was being ignored. TAMF "has not paid dividends to its members for years, in order to reinvest in the cooperative and strengthen its equity, but this deters members from staying with the cooperative."¹¹³ The cooperative therefore asked to begin the formal process of reorganization as a limited liability company.

There was no consensus in TAMF over this move, and shortly thereafter another member sent a letter challenging the request. He contested the assertion that TAMF was "constrained by the cooperative framework and law," claiming that problems stemmed from engagement in activities unbefitting "the spirit and purpose of the cooperative" (for example, getting involved in large financial transactions from which its members did not benefit, abandoning the cooperative mission). He disputed the moral right of TAMF's directors to forsake the cooperative framework, a matter "so crucial to the cooperative and its members."¹¹⁴

Objections from within TAMF and the *Merkaz* notwithstanding, reorganization moved ahead, but it entailed a strenuous administrative and legal struggle. In May 1965 TAMF notified the Cooperative Registrar of its decision to leave the *Merkaz*; the *Merkaz* claimed the decision was invalid (because its representative was absent from the meeting discussing the secession); the Registrar accepted this argument and refused to approve the request; and TAMF appealed to the Minister of Labor. The Minister, Yigal Alon, conducted hearings on the appeal and on March 30, 1965 the appeal was rejected (based on a deficiency in the hearing process). In a special meeting, however, this procedural flaw was corrected, and TAMF left the *Merkaz*.¹¹⁵

The reorganization process took place between the latter half of 1965 and the beginning of 1966. The *Merkaz* tried to protect the interests of the original cooperative members, by creating an effective "block" of public shareholders (the Jewish Agency and other national institutes) in the corporate structure. On June 5, 1966 the General Assembly of TAMF approved the transformation of the cooperative into a company, a bank

113 Letter from Jaffa-Tel Aviv Mutual Fund to A. Schweitzer, Coop. Registrar *supra* note 80.

114 Letter to A. Schweitzer, Coop. Registrar (Jan. 25, 1964) (on file with author). The letter is handwritten and the name of the writer cannot be determined.

115 All documents on file with author.

named *The Savings and Loans Bank of Israel Ltd.*¹¹⁶ Each member of the cooperative could choose between reclaiming his/her deposit or receiving shares in the new bank. It took additional time to register the bank with the Banking Supervision Unit at the Bank of Israel and the Companies Registrar, but in 1969 the largest credit cooperative in Israel ceased to exist.

In its articles of association, the new bank included the objective of retaining its "popular" nature as a "peoples' bank"; it is not clear, though, whether this objective was ever achieved. The Savings and Loans Bank of Israel Ltd. ceased to exist in the 1970s, when it was bought by one of Israel's commercial banks. Even though smaller credit cooperatives continued to operate following TAMF's transformation, that event signaled the death of the movement, together with the hopes for democratic and popular banking in Israel.

CONCLUSION

The case of the Jaffa-Tel Aviv Loans and Savings Mutual Fund is a fine illustration of the dynamics that led to the demise of the credit cooperative movement in Israel. After the establishment of the state there was a strong propensity to reorganize the relations between the state and the financial sector. The Bank of Israel was established as a central supervisory body over a previously decentralized banking system, and enforced a unified monetary policy. The commercial banks were less than enthusiastic about the new order, and therefore stringent unified norms were applied and enforced by the central bank to ensure their compliance. Due to their unique structure and mode of operation, credit cooperatives were placed at a disadvantage by this new "one size fits all" banking and monetary policy. To continue operating within an emerging competitive financial system, they required adaptations to suit their relative disadvantage: different fractional reserves rates, exemptions from fees and taxes, and other rules enabling them to survive in a changing polity and economy.

Within the financial establishment there was hardly any recognition, let alone appreciation, of the unique financial and social role credit cooperatives could play in the modern Israeli economy. On the contrary, not only were no special arrangements made to assist credit cooperatives, but they suffered indifference and discrimination by the government, which preferred to use

¹¹⁶ This process also included the merger of Bank Zrubavel, a cooperative bank, with the newly established bank.

commercial banks for its economic activity. The Bank of Israel wanted to consolidate small banks and centralize the financial sector, and the steady diminishment of credit cooperatives clearly suited this policy.

Credit cooperatives were not close to the Labor establishment apparatus and therefore unable to influence monetary or banking policy to further their own interests. As in the British Mandate period, they represented a sector set apart from the corridors of power. In the first decades of Israeli statehood, the agricultural (and security) sectors preserved their hegemonic ruling status, and the bourgeoisie continued to be excluded from newly established institutions. All they could do was approach the Bank of Israel and other state officials, lay out their needs, and hope to be heard.

Politics from above, then, had a direct impact on the weakening of the credit cooperatives. While governments in other Western countries took steps to support and encourage credit societies (by establishing cooperative banks or adjusting requirements of fractional reserves), the State of Israel adopted policies that were to their detriment.

During that period, every issue of *The Credit Cooperative* reported about credit cooperatives in some part of the world — South America, Scandinavia and Europe, Turkey and India — which managed to sustain their social and financial role. The members of the *Merkaz* participated in meetings and conferences of the international credit cooperative association, returning disheartened by the growing differences between the worldwide trend and the Israeli reality.

Distanced from the Zionist meta-narrative of state-building, the Israeli credit cooperative movement could not advocate for this cause. The *Merkaz* leadership tried to articulate their mission as protectors of the weak, the masses, and the "small person" — underscoring the essentiality of popular banking against the forces of brute capitalism. This stance, however, was hardly effective in procuring the support of the state apparatus. The constituency of private credit cooperatives — the urban petit bourgeoisie, with their continued attachment to the international cooperative movement and to the Jewish credit cooperative tradition — left the leadership excluded from the mainstream bases of power.

Weakened as it was, the credit cooperative movement was directed from above: the *Merkaz*, the established, professionalized audit union, acted as the bearer of the credit cooperative ideals. But the *Merkaz* operated in isolation. From below, the "masses," the people on behalf of which it endeavored, did not join the struggle. With only a weak attachment to the hegemonic ideology of the newly established state and confronted with a competitive banking environment — the rank and file of the credit cooperative establishment fell apart. Members of credit cooperatives failed to forge a strong enough bond

of cohesion and commitment to the cooperative ideals that could lead to "collective action" within civil society. To be sure, within the cooperatives there were people who believed they were furthering an ideological and value-based enterprise. But at the end of the day, most members were not committed enough to constitute a social force willing to fight "from below" to save this financial institution.

Perhaps a consciousness of and commitment to the cooperative principles had never really developed among the bourgeoisie; after all, this class relies on the essence of capitalist structure itself for its subsistence.

Consequently, credit cooperatives continuously opted out of the cooperative regime. Law struck the death knell of the Israeli credit cooperative enterprise and its attempt to offer an alternative banking and credit regime, based on values of solidarity and mutual support. The Banking Law (Licensing) of 1981 sealed any prospect of reviving the credit cooperative movement in Israel in the foreseeable future.¹¹⁷ Section 4 of the Law authorizes the Bank of Israel to issue a license to a financial institution, providing it is incorporated under the Companies Law.¹¹⁸ Hence, under current Israeli law a banking institution cannot be a cooperative. Just as the legal transformation from a cooperative to a limited liability company crystallized the breakdown and demise of the credit cooperative movement during the 1960s, the 1981 law symbolizes the current perception of the social role of banks in Israel.

EPILOGUE: CAN THIS PERCEPTION BE CHALLENGED?

Yes — if we are willing to rethink the goals of banks and reintroduce notions of social responsibility into the financial system. In his lecture delivered at the ceremony awarding him the 2006 Nobel Peace Prize for establishing *Grameen Bank* — the bank for the poor — Muhamad Yunus said: "Social business will be a new kind of business introduced in the market place." Social businesses, under this definition, are driven by social objectives; they are not interested in profit-maximization, but are "committed to make a difference to the world. . . . They want to give better chance in life to other people. . . . They create a new class of business which we may

117 Banking Law (Licensing), 1981, S.H. 232.

118 Section 41 authorizes issuing a banking license to an institution that provided banking services at a date prior to the coming into force of the Banking Law (Licensing) — March 31, 1982, thereby recognizing existing credit cooperatives, but not allowing the establishment of new ones.

describe as ‘non-loss’ business.”¹¹⁹ Without labeling themselves as such, credit cooperatives in Israel were in fact a kind of social business. Nowadays, with the emergence of a discourse and praxis on the social responsibility of market entities in general, and of financial institutions in particular, the story of credit cooperatives can teach us much about the weaknesses and promises of such a fusion.

119 Muhamad Yunus, Nobel Lecture, Oslo (Dec. 10, 2006), *available at* http://nobelprize.org/nobel_prizes/peace/laureates/2006/yunus-lecture.html.