# Study of the Multifunctional Organic Coffee Producers Union of Cooperatives (UCPCO RL)
# May 2013

## Executive Summary

A nacatamal is a typical Nicaraguan dish that comes wrapped in various plaintain leaves; it is a food that is prepared in two days based on corn meal, pork lard, potatoes, rice, and either chicken or pork, and mint. It is a typical Nicaraguan food. In this summary we are going to use this image of opening up one plaintain leaf after another to get to the nacatamal, which in this case would seem to be a rotten nacatamal. At the same time, we are giving notice that this study is still preliminary, it can have inconsistencies, it was done in the best spirit of commitment to rural families, and to their national and international allies.

**Context and reason for the study**

1. UCPCO was growing until the 2009-10 cycle, when UCPCO began its "fall." In January 2013 UCPCO was at the brink of going broke, burdened with a debt of close to $3 million dollars that the members had not caused, with a new manager imposed in November 2012, the continuity of all the staff loyal to one extended family (FE-RIV), and with a new Administrative Council that continued to include 3 members of the old Administrative Council. The fact that the family (FE-RI) had fallen into bad administrative management practices, suspected and said openly for years, was not able to be confirmed. Partly because this family is economically and politically powerful in the municipality, friends with people at the highest levels of the government, and because they were given legitimacy by coffee buyers, financial institutions, the international fair trade network and the aid agencies that were financing projects. Two external audits had been done without either of them being able to show the causes for the loss of the millions of dollars of resources, fundamentally because the audits were based on existing accounting documentation. The reality is that nearly $3 million dollars were missing! We are dealing with a more serious case than what happened in JIRPCOOP in the 90s in Jinotega; we are dealing with the case of a cooperative organization manipulated by an elite, in collusion both internally and externally to strip resources from the lives of around 400 families. The present study ilooks for openings that would allow an uncorrupted audit to be done, and that above all would allow the causes of this crisis to be understood, in order to reorganize UCPCO on the basis of solid footings, and renew that cooperativism and the fair trade organizations are instruments for reducing and erradicating poverty, not for producing it!

2. An impressive amount of papers with quantitative data was reviewed, minute books going back to 2007, receipts, audits. Administrative staff, technicians, cuppers, leaders and member families of the 5 organizations were interviewed. This is the basis for this text. Said figuratively, little by little "the nacatamal was uncovered", at least a good part of that "nacatamal", because the other part must be complemented by the buyers, by FLO, by the certifiers and by the financing institutions like Root Capital
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**The "leaves of the nacatamal"**

3. *First leaf: centralized organization loyal to the FE-RI family*. Even though the cooperative law and the statutes of UCPCO themselves indicate that a board member cannot occupy a board post for three consecutive periods, in practice everything has been permitted in UCPCO: the current

treasurer has held that post since 2006; the current at large member has been president in two previous periods. In 2004 the FE-RI family obtained the presidency of UCPCO and immediately named as general manager the son of the president, who hired and named members of his own family to key posts – brother, cousins, nephews, adopted sons, uncles. There were family members present at every position except for that of grassroots technicians, but they created a system of favors there to make the technicians dependent. Everything was controlled! In addition all the meetings that they had were started with prayers and readings from the Bible, in this way covering everything with a religious mantle.

4. *Second leaf: Conversion of clients into members to increase the amount of coffee collected*. Since 2009-10, based on FLO-CER observations made about clients of UCPCO that were appearing as "members" without being members, the management forced those clients to become members of the cooperatives, and forced the cooperatives to accept them as members, without caring whether they were outside the cooperative, and even though afterwards they did not participate in any meeting of the cooperatives. Becoming a member was a formality in order to sell ("turn in") coffee and receive credit, even though in practice they never considered themselves members, nor did the cooperatives consider them to be members. In this way the coffee that they sold to UCPCO could continue, only it would appear as if it came from members of UCPCO- because formally they were. It was the first way of increasing the coffee production to be exported.

5. *Third leaf: "Inflation" of production data in order to hide the fact that they were buying coffee off of clients*. Since the 2011-12 cycle different information sheets were managed on the quantity of coffee produced by the cooperatives, a real information sheet for the members, and another one made up (called "adjusted") to be given to the BIOLATINA certifier and for the purpose of audits. In 2011-12 the cooperatives produced 16,000 quintals parchment coffee and BIOLATINA certified 32,000 quintals parchment coffee. This "inflation" means that conventional coffee was sold as organic coffee, which implied premium payments for fair trade coffee and premiums for organic coffee. This situation was information that the grassroots cooperatives knew about, they accepted it even with certain resistance, they accepted "lying" for UCPCO to cover its operational costs and to capitalize. In other words, we are facing a "collective collusion" in a chain of actors that goes from the grassroots cooperatives up to the international organizations – the "collusion" being knowing what was happening or by supporting these practices without knowing them in great detail.

6. *Fourth leaf: The gap between member coffee and client coffee contributes to the management of an organization being less responsive to its members.* Already in the 2009-10 cycle the gap between the quantity of coffee from the members and the coffee bought from clients was impressive: out of a total of 18,972 quintals of export quality coffee, 14,197 was bought from clients, in other words 75% of the total coffee came from clients that were not members. This opens the door to the question: who was UCPCO and fair trade working for? How could the member families have control over their organization if it was working more and more for other "third parties" (clients), something that was given legitimacy by the certifiers, the buyers, the audits and was done in the name of God?

7. *Fifth leaf: the management of the premiums [payments]*. In the specific case of the 2009-10 cycle, the total income was $3,917,259, of which 10% was FLO and organic premium payments. Using these numbers means that US$19.30 was paid out per quintal of export coffee as FLO and organic premiums – which means that almost all the coffee, including the conventional from clients that were not members - passed as "fair trade" and almost all passed as "organic". Since that cycle the financial reports on UCPCO were no longer sent to the cooperatives.

8. *Sixth leaf: the disappearance of the profits*. In the 2009-10 cycle in the financial reports it appears that UCPCO obtained profits of US$910,672.30, nearly a million dollars. Later in the following cycles, in spite of having collected a larger volume of coffee and of having sold the coffee at better prices, profits no longer appear. How is an organization with these profits going to turn into an organization with balances in the red?

9. *Seventh leaf: as the scale of their operations increased, their per quintal costs increased.* The logic of an economy of scale is that the costs go down with larger volume; in the case of UCPCO it was the reverse; the greater the volume, the greater the cost. In the 2009-10 cycle for the sale of 18,000 quintals of gold export quality coffee, US$3.9 million dollars were obtained, of which a little more than US$3 million were expenses, and 16.1% of that amount were operational costs (US$22.50 per quintal gold). In the 2010-11 cycle more than 22,000 quintals of gold export quality coffee was exported, obtaining US$6.8 million, of which more than US$7 million were expenses, and 14.1% were operational costs (US$44.80/quintal gold). In the 2011-12 cycle from the 27,000 quintals of gold export quality coffee sold, US$5.2 million dollars were obtained, the expenses of which were more than US$8.1 million dollars, 13.9% of which were operational costs (US$40.90/gold quintal).

*10. Eighth leaf: Agreement between UCPCO and the EIRSA company where the same FE-RIV family is in both places at the same time*. EIRSA (Rivas and Associates Exports and Imports, Inc.) was founded in 2010, with its manager and legal representative the same person, who was also the manager of UCPCO – who also had administrative power to sign contracts, grant loans, execute and collect debts, and general power of attorney to represent UCPCO for transfering ownership, selling, mortgaging, negotiating projects and loans (Meeting minutes No. 44, 2007), powers that were renewable year after year, but whose renovation did not appear ever again in the minutes. In that same year, that manager, wearing two hats (the management of UCPCO and of EIRSA), was able to get the administrative council to approve a commercial agreement between UCPCO and EIRSA, where the President of UCPCO and Ms. Erica Argentina Rodríguez for EIRSA are the people who sign the agreement. The agreement consisted in that UCPCO would transfer resources from banks, Alfinsa, Root Capital and others to EIRSA, the company that would buy coffee for UCPCO. In other words, the manager of UCPCO transferred it to the manager of EIRSA, who was the same person; the FE-RIV family led and took over both organizations.

In that same year, UCPCO signed an agreement with FENIAGRO–ALBALINISA to sell them coffee. UCPCO is provided $2.7 million dollars (Meeting Minutes No. 90, Jan 13, 2011) for 14 containers of export coffee. All of that money was transferred to EIRSA for the purchase of coffee, but not from members, rather from third parties. EIRSA collected the coffee, but given that the prices were now getting beyond US$300/quintal, decided to sell what they had collected and tried to return the money to ALBALINISA. A conflict ensued between ALBALINISA and UCPCO over this situation, where the dry mill was taken over by the Police. This conflict was resolved through negotiations where UCPCO as the signatory with ALBALINISA assumed commitments, while the FE-RIV family hid behind UCPCO. Did the earnings from this game of buying and selling coffee stay in the treasury of UCPCO? No (see point No. 14 below, the twelfth leaf).

Nevertheless, in this situation it became clear what was happening, and this is how the Prosecutor expressed it to the staff of UCPCO´s dry mill: "*they have gotten involved with the government, tell …. to turn over the money quickly or the coffee, because you cannot play with the government; the violation of the agreement is unacceptable, Feniagro-Albalinisa did not given them money from ALBA for the purchase and sale of coffee for personal profit, that manipulation of the ALBA money is unacceptable.*"

11. *Ninth leaf: The theft of coffee from the members themselves through camouflaging low output*. In the 2009-10 cycle the output for the cooperatives varied between 2.10 and 2.16[1], and for the clients 2.18; but for the 2010-11 cycle a surprising change happens with the entry of EIRSA. For that 2010-11 cycle there are two reports, one that was presented to the cooperatives, and another that was confidential. The one presented to the cooperatives, and the one used for calculating their payments, reported that the coffee ouput of the cooperatives varied between 2.07 and 2.10, while the output of coffee bought by EIRSA was 2.0. In other words the coffee output of the cooperatives was less, they needed between 207 and 210 pounds to get 100 lbs of export coffee, while the coffee bought by EIRSA has an incredible output, 200 lbs to get 100 lbs of export coffee. But in the confidential report, the EIRSA output appears to be 2.2. In this cycle UCPCO collected a total of 16,282 quintals export coffee, of which 10.9% came from the cooperatives and 88% from EIRSA that bought it from third parties. Because of the importance of this data, we copied the following table, where just by the output factor for EIRSA there is a difference of 1,445 quintals of export coffee in their favor (15,904 – 14,459 = 1,445).

| **Financial results reported to the cooperatives** | | | | |
|---|---|---|---|---|
| **Cooperative/Clients** | **Qq parchment collected** | **Output** | **QQ of Export coffee** | **%** |
| Cooperatives | 7,660.9 | 2.07 | 3,692.7 | 18.32 |
| Clients | 1,184.91 | 2.10 | 563.2 | 2.79 |
| EIRSA | 31,809.76 | 2.00 | 15,904.9 | 78.89 |
| **Total** | **40,655.57** | **2.02** | **20,160.8** | **100** |
| **Results not presented (confidential)** | | | | |
| **Cooperative/Clients** | **Qq parchment collected** | **Output** | **QQ of Export coffee** | **%** |
| Cooperativs | 3,682.3 | 2.07 | 1,775.0 | 10.90 |
| Clients | 103.58 | 2.14 | 48.3 | 0.30 |
| EIRSA | 31,809.76 | 2.20 | 14,459.0 | 88.80 |
| **Total** | **35,595.64** | **2.19** | **16,282.3** | **100** |
| **Variation** | **5,059.93** | | **3,878.5** | |
| Total | **40,655.57** | | **20,160.8** | |

12. *Tenth leaf: the profits from the previous cycles change to losses starting in the 2010-11 cycle*. The financial data show that even though there was an increase in the amount exported and the coffee was sold at better prices, with FLO, organic, quality and differential premium prices that added up to 14.1% of the total of $6,819,451.66 of income, UCPCO had losses of US$221,966.16. Compared to with the previous cycle, that had a smaller volume of coffee exported and sold at a lower price, but had nearly $1 million dollars in profits, now in this 2010-11 cycle they started having losses.

13. *Eleventh leaf: Root Capital provides capital WITHOUT collateral*. For the 2011-12 cycle, due to the situation with ALBALINISA they did not have capital to buy coffee, so the manager with his "UCPCO hat" negotiated resources in financial institutions: Shared Interest ($271,000, collateral was export contracts for organic, fair trade coffee); Root Capital ($2,522,00, WITHOUT

[1] Ouput in this context refers to how much parchment coffee it takes to end up with 1 quintal of export coffee.

collateral[2]); Rabobank – 20th of April Cooperative ($23,000, lien on harvest); Oikocredit ($400,000, mortgage on cooperative assets); BANPRO ($2,104,083, first mortgage on the dry mill and lien on coffee in warehouse, revolving line of credit). These resources that UCPCO got were transferred to EIRSA to buy coffee. Note: in a context of financial losses in UCPCO, of a national scandal linked to ALBALINISA where the role of EIRSA and the FE-RIV family became public, the financial institutions (some institutions connected to coffee buyers) still provided it with credit, and in addition ROOT CAPITAL provided it resources WITHOUT asking for collateral, and in addition ROOT CAPITAL provided resources WITHOUT asking for collateral.

14. *Twelfth leaf: the losses for UCPCO increased and the coffee of their members "got lost."* In the 2011-12 cycle the losses for UCPCO were not thousands but millions: US$2,892,421. In addition to the many reasons already mentioned, a new one is added. The desire for quick enrichment on the part of the FE-RI family made the manager "with two hats" order the collection of coffee of EIRSA in amounts beyond the capacity of the dry mill to store, which, when the sale of the coffee got delayed, made between 5,000 and 7,000 quintals lose quality- it got full of mold. Nevertheless, the cost of that loss of quality that happened in the dry mill got charged to the members of UCPCO; according to the staff-personnel of the dry mill, to justify this "charge on the producers," they ordered the staff of the dry mill to lie, to say that the loss of quality was due to the fact that the producers turned in poor quality coffee. So they brought dozens of members in to the dry mill, showing them the damaged coffee and telling them that they the producers had turned in poor quality coffee. Many producers did not accept this explanation and they defended the quality of their coffee, showing each step followed, from the farm, to the wet mill and to the dry mill, passing through weight and quality control, but they did not receive support, even from their leaders (see Meeting Notes from that date).

15. *Root Capital pressured for payment*. Given that they did not receive payment within the established term, Root Capital ordered an audit be done in August 2012. In that audit EIRSA appeared as "Rodríguez and Associates", an incorrect surname, but that surely contributed to the fact that the audit was not able to detect EIRSA represented in the management itself of UCPCO. Shortly after the results of this audit, Root Capital asked for collateral, including co-signing on the part of the Assembly of Delegates. This is the moment at which the Delegates realized that they did not receive that money. Root Capital pressured them and agreed with UCPCO to export the coffee through ECOM (Atlantic) to Green Mountain, and that Green Mountain would transfer the payment for this coffee purchased. So the members refused to turn in their coffee, so their organic coffee ends up going to the informal market as conventional coffee.

**Information and explanations that are still needed**

16. The buyers (e.g. Green Mountain, Sustainable Harvest, Mitka..) need to send us information from the last four cycles on the amount of coffee purchased from UCPCO, the price that they paid and the premiums they provided (price differential, fair trade premium and organic premium). The FLO organization and the Biolatina certifier need to inform us about the exact amount of coffee certified in each cycle of the last four cycles, and explain to us the type of audits that they have done of UCPCO in the last 4 cycles. Organizations like Root Capital need to clarify why they gave resources to UCPCO when they knew about the EIRSA-UCPCO situation, and what had happened with ALBALINISA, and how, knowing that these resources did not benefit the member families of UCPCO, they then pressured these families to take responsibility for something that they never received. This requested information is fundamental for revising and completing the assessment –

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[2] Oscar Mauricio Hernández Medina, Public Accountant and Consultant. Report of Audit and Financial Statements on June 30, 2012, October 8, 2012. Audit ordered by Root Capital.

we say revising because this study can also have inconsistencies that can be clarified with the support of the different organizations.

17. Having the requested information, FLO and the historic coffee buyers of UCPCO should support a new audit that would include UCPCO as well as the other organizations that have something to do with this, and then support doing a real strategic plan for UCPCO. We say "real" because Root Capital supported the preparation of a strategic plan in 2011, a plan that, like the audits, did not have real information, and therefore were plans that ended up in the files. It is important to be aware that audits and strategic plans that are not based on real data, end up contributing to the production of poverty.

**Transformation of the cooperatives and the chain of actors that work with the cooperatives**

18. On the basis of this assessment, to be completed with the requested information, a new audit and a new strategic plan be done

- UCPCO will be able to be reorganized in such a way that the Administrative Council might govern UCPCO with policies and strategies, and the management might efficiently execute these policies and strategies; that the managers might not usurp the leadership that belongs to the leaders named by the cooperative member families. That the grassroots cooperatives might become real counterbalancing powers to ensure the rotation of leadership in UCPCO, and so that the certifying organizations and FLO might weave real alliances for reducing and erradicating poverty. In this new phase UCPCO needs the buyers and the FLO organization to commit decisively to the new and emerging UCPCO.
- The international organizations and institutions will be able to review their policies and their practices, because the crisis situation of UCPCO shows that it is not only a crisis that has to do with UCPCO and its members. It is a crisis that also has to do with the businesses that buy coffee, fair trade organizations, the certifiers, the aid agencies and the financial institutions. A chain of actors is part of this problem, and a chain of actors is part of the solution.

19. The purpose of this study is not to find the "guilty parties" nor to "punish" anyone. This study seeks to know the causes of the current crisis so that later "tailor made" solutions might be designed. So far, the principal lesson that this study reveals is that the crisis of UCPCO should be considered a crisis of the cooperative movement and its international allies, and that therefore all should be part of the solution.

The nacatamal that we have can still be rescued if the chain of actors contributes their "grain of sand." We can make this nacatamal be true human nourishment for San Juan as well as for national and international actors.