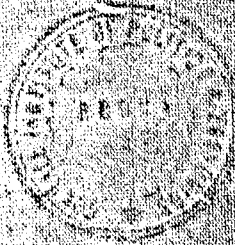


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*Economics of*  
**COOPERATIVE  
MARKETING**

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**THE ECONOMICS OF  
COOPERATIVE MARKETING**



**THE ECONOMICS**  
**OF**  
**COOPERATIVE MARKETING**

**BY**

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**McGRAW-HILL BOOK COMPANY, Inc.**  
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XIII

## PREFACE

Economic security has become the quest of millions who suffered untold hardships during the recent lean and uncertain years. The old patterns of economic and social institutions are being critically appraised to avert if possible a recurrence of the debacle that began in the autumn of 1929. The disruption of commerce and the stagnation of industry have created a great wave of renewed interest in reform movements. Cooperation is being seriously considered by many as the best possible alternative mode of organizing business to assure economic and social stability. Some leaders in the movement are apprehensive of sporadic growth. They foresee many persons being induced to exert their influence and invest their resources in organization and administrative activities without a proper understanding and appreciation of the fundamental principles involved.

The purpose of this book is to present a comprehensive statement of the basic philosophy, the decisive principles, and the practical methodology of cooperation. It is designed primarily as a college text not for the sole purpose of arousing intellectual curiosity, but as a valuable source of information for those who may teach the subject or come in contact with the broad realities of the movement through actual participation as members, directors, and employees.

The term "marketing" as it is used in the title of this book is to be construed to include both sides of the transaction, buying as well as selling. A narrower interpretation of the word is common in commercial usages connoting sales activities only. Since approximately 85 per cent of the cooperative business of the country is done by farmers' cooperative sales associations, chief consideration has been given to this phase of the business.

This book on cooperation truly exemplifies the meaning of the word. The authors have collaborated in every way in its preparation and will share all censures and commendations.

They acknowledge their indebtedness to their colleagues and to the many writers and commentators on the cooperative movement. No small share of credit for this work goes to students and assistants for their helpful analysis of the organization and technique in presentation.

HENRY H. BAKKEN,  
MARVIN A. SCHAARS.

MADISON, WISCONSIN,  
*October, 1937.*

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**PART I**  
**THE EVOLUTION OF COOPERATIVE BUYING AND  
SELLING**

## I

### *Cooperation—Its Setting in an Economic Society*

*A cooperative sales association is a voluntary business organization established for the purpose of collective marketing. Such association is owned and operated by member patrons for their direct benefit. Its immediate purpose is to obtain for its members the highest farm price; its ultimate aim is to elevate the plane of living on farms. Cooperation in marketing is a business undertaking amenable to the economic forces but not to all the traditions, codes, and practices which affect private commercial enterprises.*

*Many reasons cause farmers to set up their own marketing agencies, such as, low returns for their products, wide marketing margins, inadequate services, and, in some instances, unfair treatment by middlemen. A basic reason, however, is the small-scale production on most farms. These conditions furnish the underlying motives for the organization of cooperative sales associations which provide mass distribution for the nonintegrated, small production units such as are common to American agriculture. As business institutions these associations must succeed or fail on their own merits.*

*The cooperative association resembles the private business corporation in its methods of operation. It differs from the capitalistic system, as typified by the modern commercial corporation, chiefly in its motives and internal organization. Cooperatives in the United States do not seek paternalism but the same fair treatment accorded other American business concerns by the government. The ideals of cooperativism, however, are unlike those of socialism, communism, or fascism. Cooperativism is a synthesis of elements of several economic systems. It eliminates many weaknesses of other systems and prevents the extremes to which they go. Cooperativism is the "via media, via amicabile."*





**CHAPTER I**  
**COOPERATION—ITS SETTING IN AN**  
**ECONOMIC SOCIETY**

Private, governmental, and cooperative agencies are engaged in marketing farm products. A private agency is the usual proprietary, partnership, or corporate business that conducts its operations in the hope of accumulating profits. The local livestock buyer, wholesale butter dealer, potato jobber, and independent grocer are examples of private agencies. Approximately 90 per cent of all tradesmen in the wholesale, jobbing, and retail markets in America are private business agencies. A governmental agency is any division of government, such as the municipal, town, county, state or national government, engaged in marketing. In America the governmental agency is practically unknown as a marketing institution, but in foreign countries it is not uncommon for the government to operate certain types of commercial businesses. The third agency is the cooperative which has risen to a place of importance in commercial life by introducing novel features, methods of organization, operating policies, and principles. It is attracting the attention of all classes in society the world over as a superior method of acquiring commodities, providing services, and selling farm products.

**COOPERATIVE MARKETING DEFINED**

A cooperative sales association is a voluntary business organization established by its member patrons to market farm products collectively for their direct benefit. It is governed according to democratic principles and the savings are apportioned to the members on the basis of their patronage. Members, as owners, operators, and contributors of the commodities handled, are the direct beneficiaries of the savings that may accrue. No intermediary stands to profit (or lose) at the expense of the members. It should be noted that according to this definition the commercial

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aspects of the organization are emphasized. The cooperative marketing association is a business institution; its economic motives and its economic character distinguish it from such associations as trade unions, political parties, and purely social institutions. It is organized to conduct business according to sound business principles. The cooperative marketing agencies, in organization, are distinctly different from those of governmental and private commercial enterprises. Their methods of conducting marketing operations, however, may be radically different or vary only slightly from those of private tradesmen. Instead of selling independently and in competition with one another, farmers through their cooperative companies consolidate their selling force, improve their bargaining position, and pool their resources. Under this plan they no longer sell *to* a private middleman, but rather *through* their cooperative. The voluntary aspects of the membership are important for the association is truly American in principle in that the individual's wishes and property rights are recognized. No one is forced to join a cooperative; it stands or falls on its own merits.

Legal definitions pertaining to the cooperative are found in the federal and state statutes. The Capper-Volstead Act, the federal law, defines a company as cooperative if it operates for the mutual benefit of its members, and if each member has one vote regardless of the number of shares of stock he may own, or in lieu thereof, if dividends on capital stock or membership capital are not in excess of 8 per cent per annum; it is further stated "that the association shall not deal in the products of nonmembers to an amount greater in value than such as are handled by it for members." Such associations are also restricted under the act to agricultural producers. In most of the state laws the "cooperative basis" of organization is defined as follows: each member is entitled to one and only one vote; dividends on capital stock are limited to 8 per cent per annum; and net proceeds of the business must be apportioned among the patrons in proportion to the volume of business transacted with the association. These represent the prevailing legal concepts of cooperative associations.

Since the terminology referring to the types of cooperatives is by no means uniform or even correctly applied by all writers and speakers, the authors wish to indicate here the meaning of the

terms that will be used in this text. In a later chapter, Types of Cooperatives, a fuller description of the terms will be given.

Cooperative sales associations, also used synonymously with cooperative marketing associations, refer to farmers' cooperative associations which sell farm products which were produced individually on the farms of the members. Processing, packing, storing, financing, bargaining, and other marketing functions are carried on by such associations.

Cooperative purchasing associations pool the buying power of members and ordinarily sell to both members and nonmembers. Two subclasses are distinguished within this large group of associations:

1. Agricultural purchasing associations whose members are farmers and handle or bargain primarily for goods used in farm production.
2. Consumers' cooperatives whose members are either farmers or city people and handle or bargain for commodities needed in the home.

Cooperative service associations provide services such as financing, insurance, housing, and utility services for their members who may be either farmers or city dwellers. The services fall under two broad classifications, consumption and production.

Workers' cooperative associations are organizations that pool the labor of their members for joint action.

1. Laborers may bargain through labor unions with employers respecting wages and working conditions.
2. Farmers may organize threshing rings, spray rings, and other associations to do certain farming tasks collectively, or, as in Russia, they may run farms collectively.
3. Industrial workers may also own and operate their own factories in which they pool their labor and share equitably in the profits. The workers' self-help cooperatives, organized by unemployed workers during the years of the depression, illustrate the latter type of industrial workers' cooperative associations.

#### PURPOSE AND SCOPE OF COOPERATIVE SALES ASSOCIATIONS

People offer many different reasons for becoming members of cooperative sales associations. The most common one is the desire for pecuniary gain. Producers and consumers do not organize or belong to cooperatives merely for the pleasure of association. There must be some tangible consideration, which is generally economic betterment. The *immediate* purpose of a farmers' cooperative sales association is to obtain the highest farm price, *i.e.*, the largest price payable to the farmer for the products which he has to sell. The *ultimate* purpose is to elevate the plane of living on farms. The primary aim of a farmers'

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purchasing association is to obtain high quality farm or household supplies at the lowest possible cost.

The purpose is, therefore, defined in economic terms; all social considerations are secondary. A cooperative must succeed as a business institution; it cannot prosper long on any other basis. Regardless of any individual social ambitions of its members, it must excel its competitors in collective marketing or be doomed to failure.

The four main concepts of cooperatives may be delineated as follows:

1. **The Social.** Cooperation is often considered as a means of social reform. Owen and Fourier sponsored communal societies with cooperative production, living, and government. Their plans embodied complete changes in living and working habits of the members. Owing to the inclusiveness of their programs, many difficulties were evoked by their attempted social regeneration and practically all of these societies failed.

2. **The Sociopolitical.** The sociopolitical concept considers cooperation as an effective political means of improving the social life of the cooperators. Sponsors of such cooperation believe that social reforms are dependent upon political partisanship. Consequently in some countries political groups such as the Socialist and the Cooperative parties have been promoted to gain the ends sought by the cooperators. In America, however, the movement has remained relatively free from political alliances.

3. **The Legalistic.** Some think of the cooperative organization as a legalistic creation. An association in their minds is simply a form of corporate organization in which the legal rights and duties, powers and exposures are carefully enumerated. Such conditions of cooperative procedure are recorded as: binding contracts, membership agreements, specific limitations on transfers of shares of stock, and the listing of members' property rights. The legal concept considers the cooperative's success as contingent upon the expertness with which its legal instruments are drawn and upon how minutely the cooperative's organization and operating policies are defined.

4. **The Economic.** For many others, the economic concept expresses the scope and the purpose of cooperative marketing associations. It considers the organization and operation of cooperatives as a means to a richer life and a higher plane of living. Efficiency in conducting the business of marketing is the chief aim of this concept, and social improvement in agricultural life is its ultimate goal.

There are three ways in which the cooperative can achieve this goal: (1) obtain a better price than could be obtained by private agencies, (2) obtain the same price but have a lower marketing margin so that the net price received by the producer

**COOPERATION—ITS SETTING IN AN ECONOMIC SOCIETY 7**

will still be higher than that paid by private middlemen, and (3) a combination of these two. To illustrate, let us assume that a private middleman sells a product for \$1, takes out a margin of 25 cents, and pays the farmer 75 cents. A cooperative may increase the returns to the farmer as follows:

Methods of increasing returns	Sale price	Gross* margin	Net to producer
Higher price.....	\$1.05	\$0.25	\$0.80
Lower margin.....	1.00	0.20	0.80
Combination.....	1.02	0.22	0.80

\* Gross margin or gross profit consists of operating costs plus net profit. It is the difference between the selling price of the product and the amount received by the producer.

Cooperative associations are based upon the fact that agricultural production is essentially a small unit business. If there were in agriculture, enterprises as large as the major industrial concerns, it is also doubtful whether cooperatives would be developed for marketing their products. Large industrialists are in a position to integrate their production and marketing functions, and many find it more economical to distribute their own products than to have private middlemen do it for them. Small independent operators do not have sufficient goods to market them economically. Likewise few farmers have a single carload of livestock, wheat, cotton, potatoes, or other products. Hence, they are dependent upon a middleman system which will assemble, grade, pack, store, and perform all other services of marketing. Whether these services are to be performed by private or cooperative agencies is determined by the farmers themselves.

The ostensible purpose of a cooperative is not to eliminate private middlemen as some persons believe. The purpose of cooperative action is to lower the costs of distribution, improve production, integrate marketing and production operations, eliminate wastes, prevent expensive duplication of agencies, and distribute products in a systematic manner. With these reforms in operation some private middlemen may not be able to compete successfully—others may. Marketing services, however, must be performed irrespective of whether the middleman is a private

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or cooperative agency. The need for the middleman's services is not eliminated with a cooperative; the individual performing the functions may be.

Local and regional associations are an outgrowth of many causes, such as the unfair or dishonest treatment by private buyers, wide margins between prices received by farmers and prices quoted in the market papers, a desire to secure for themselves the profits taken by private businessmen, a faith in the hypothesis that in union there is strength, and the success of cooperatives established elsewhere. When farmers learn that they receive but 25 to 50 cents of the consumer's dollar, they conclude that the existing middleman system is at fault and that improvement can be best secured through cooperation rather than through government regulation or reorganization of the existing middleman system. There is no doubt that the practices and ethics of some private operators have forced farmers into cooperative associations.

Unorganized farmers have often become the victims of shrewd and well-informed market operators. The upper level which prices may reach in the market place and still move a given supply into consumption is determined by the purchasing power of consumers and the demand for the particular products. Tradesmen attempt at all times to realize this maximum price. The price level is usually established by the representative firms. Therefore, there are always those who could charge less due to their efficiency and those who would like to charge more due to their inefficiency. Competition keeps their prices uniform, but competition is not the easy-working, price-lowering force for consumers or price-raising force for producers that classical economics postulates. Tradesmen long ago learned that price cutting (in the commercial sense) is ruinous and that a far better policy is to "live and let live." Even though no formal agreements are reached in regard to the prices to be charged, they, nevertheless, assume a high degree of similarity in a given market. As a result of this leveling out of retail prices and the necessity of conforming to the prices of the representative firms, every effort is made to widen the marketing margin by lowering the prices paid to producers. In the country market where uninformed producers are on one side of the transaction and well-informed buyers on the other, it is little wonder that farmers

have become the victims of many buyers. That on the same day and in the same market there should be a price variance of \$5 to \$12 a bale for the identical grade of cotton or of \$1 to \$2 a hundredweight for the same grade of hogs, is a disparity that farmers will not tolerate. The fact that the competition was shifted to the farmers where they unknowingly undersold each other has been an efficacious factor in causing collective action. The general practice of selling farm products on an ungraded basis has caused farmers to lose millions of dollars. It is not surprising that farmers reconstructed the marketing system to escape the results of the defects in the older system.

One of the chief objectives of a cooperative association is to influence but not arbitrarily control prices which farm products sell for in the markets. Yet, many farmers believe that through organization arbitrary price-fixing power is gained. The cooperative that receives a large percentage of a crop and is supported by excellent market information and a national distributing system commands a position that enables it to obtain the most favorable selling prices. The futility of attempting to dictate market prices without possessing monopoly power is shown in a survey of the defunct Tobacco Growers Cooperative Association in which investigators reported that:

The attitude of some of the leaders of the association became one not of rendering efficient marketing services to its grower members but rather that of monopolistic control of the market and the setting of a price without full consideration of the factors of demand and supply. . . . The impossibility of the success of such a policy should have been obvious; the harmful effect upon the membership was inevitable.<sup>1</sup>

A number of excellent studies have been made to determine why farmers join cooperative associations. The reasons given by farmers are not necessarily the same as those given by the management, but they show the objectives, impracticable though some may be, that farmers have in mind and what they hope to accomplish by organization. Out of 462 cotton and tobacco producers, 236 joined to get better prices, 75 "thought it a good thing," 44 were dissatisfied with the existing system, 23 were disappointed with low prices at time of organization, and the

<sup>1</sup> SCANLAN, JOHN J., and J. M. TINLEY, *Business Analysis of the Tobacco Growers Cooperative Association*, U. S. Dept. Agr. Circ. 199, pp. 16-17, 1929.

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remainder expressed other reasons.<sup>2</sup> In a study conducted among cotton farmers alone, 141 out of a total of 594 farmers joined to obtain more money for cotton, 130 "believed in the idea of cooperation," 113 thought the cooperative would improve agricultural conditions, 111 wished to secure better marketing services, and the others gave sundry reasons for joining.<sup>3</sup> Other studies, it is believed, would show similar reasons for joining and supporting the cooperative movement in America.

### COOPERATIVE MARKETING AND ECONOMIC PRINCIPLES

No cooperative association or private enterprise has ever succeeded for a long period of time by ignoring economic laws and principles. There is nothing in the cooperative plan of organization that gives it any privileges, any special economic rights or powers, or any extra liberties that a private business does not enjoy. A cooperative cannot secure high prices if the volume of products to be marketed is greatly in excess of consumption requirements; it cannot force people to buy if they are not inclined to do so, nor can it hope to have low costs of operation with small volume, inefficient management and overcapitalization. Successful cooperatives have realized success not because they controverted the laws of economics, but because they skillfully governed their activities to conform to these laws. Thus, they have been able to meet competition. They have won trade confidence through efficient and businesslike methods of operation. Some large-scale regional associations in the second decade of this century attempted arbitrary price fixing. Failing in this, they changed their policies to conform with good business procedure. Today they are rewarded by success rather than the failure with which they were formerly threatened.

Efficient managers of large-scale regional associations are conscious of the importance of economic laws. Some have established economic research departments within their organizations to advise the manager, directors, and the members of economic trends and price movements. The American Cotton Cooperative Association and the National Livestock Marketing

<sup>2</sup> JONES, J. W., and O. B. JESNESS, *Membership Relations of Cooperative Associations*, *U. S. Dept. Agr. Circ.* 407, p. 5, 1927.

<sup>3</sup> MANNY, T. B., *Farmers' Experiences and Opinions As Factors Influencing Their Cotton Marketing Methods*, *U. S. Dept. Agr. Circ.* 144, p. 27, 1931.



Association, to name only two organizations, have research departments to perform these services. Through their own publications, such data are made available to the cotton and livestock industries.

The reader may question why the *cooperative* method was chosen by farmers as the effective means for improving marketing. To answer this, one must consider the various methods for reducing the cost of products purchased and increasing the price of farm products sold. There are five choices: (1) competition, (2) monopoly, (3) government regulation, (4) governmental distribution, and (5) cooperation.

Competition as a force to lower costs of marketing and to increase prices paid to farmers has not proved itself a dependable medium of improvement. The good neighbor policy of "live and let live" and collusion among buyers of farm produce, as well as the concentration of economic power by huge corporations in the primary markets, have made competition in the purchase of farm products an unreliable and impotent force. If the operation of monopolies in the distribution of farm products should result in distinct economies of operation, there is still no assurance that such gains would be passed on to the farmers in the form of higher prices or to consumers in the form of lower retail prices. There is just cause to fear monopolies as the experience of farmers in country communities where only one dealer handles the producers' products has repeatedly shown.

Governmental regulation of business as a safeguard for both producer and consumer has also been shown incapable of being completely effective under a democratic form of government. Most regulatory legislation passed by Congress or state legislatures has been bitterly fought by private enterprises. Examples of such opposition are the fight against revision of the Food and Drug Act, the Packers' and Stockyards' Act, the Commodity Exchange Act, the government's labeling program, and other measures too numerous to mention. Legislation is usually a compromise measure, much weakened and emasculated by its opponents during its passage through the legislative mill. Moreover, the enforcement of such legislation is often negated by passive commissions and unfriendly courts. Often on the merest technicality, prosecution of offenders is prevented, and the spirit of the law is violated. Thus, although governmental regulation

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is desirable, the actual facts do not lead the farmers and consumers to believe their interests are fully protected and advanced by this method.

There is little indication at present that the government will become a distributing agency of farm products. In our democratic government the slogan has been, "Less government in business but more business in government." There is no assurance whatsoever that government-operated business would best promote the interests of the farmers. Owing to the fact that the government has an obligation to all groups in society, the farmers would have no assurance that those entrusted with the management of a government enterprise would be any more "rural minded" than "urban minded."

None of these methods already discussed has resulted in maximum long time benefits to producers and consumers. The reason may be that, except under government distribution, a profit always constituted a part of the distribution margin. The cooperative agency has proved to be the only sound medium which eliminates the profit motive. Under this plan the profits (and losses) of the middlemen revert to producers in the form of higher (and lower) prices or to consumers in the form of lower prices. The cooperative method is better suited to farmers since it is based on what the farmer has to sell, *i.e.*, farm products, and not on what many farmers lack, namely, capital. This can be shown in the following illustration. Let us assume that Farmer *A* has 20 acres of apple trees and only \$50 to invest in a cooperative company. With this he can buy 5 shares of stock. Farmer *B* has only 5 acres of apple trees but \$200 with which to buy 20 shares of stock. *A* has four times as many apples as *B*, but *B* has four times as much money as *A*. *A* has far greater interest in the affairs of the company than *B*. *A*'s products from 20 acres contribute more to cost reduction than *B*'s from only 5 acres. In a private corporation *B* would gain four times as much from cost reduction as *A*, but in a cooperative *A* would get four times as much of the savings as *B*. Hence, an organization in which *A* with his greater volume of produce can have as much voice in the management as *B* with his larger capital investment suits *A*'s purpose better than an organization in which his voting is restricted to his investment. As long as the success of a business is more dependent upon patronage than upon capital invest-

ments, it is apparent that the cooperative form of business is better suited to the business of selling farm products than the usual corporate form of organization. Capital, to be sure, is needed in a cooperative company, but it is not so important as patronage which can of itself become the basis of capital loans. Many cooperatives have begun without capital investments, have borrowed upon the patrons' products, and have succeeded. However, no amount of capital without patronage can make a business succeed.

#### COOPERATION AND CAPITALISM

Since competition as an internal corrective force and governmental authority as an outside controlling agency have both been unsatisfactory and incapable of assuring both producers and consumers of a "square deal," some enthusiasts for cooperation advocate the overthrow of the capitalistic economy, and the substitution of a cooperative commonwealth. Some feel that cooperation is a peaceful way of establishing a socialistic or communistic state and at the same time of warding off fascism. Others contend that cooperation is an effective means of preventing the encroachments of socialism and communism and that it is a brake upon the extremes of capitalism. The following discussion does not attempt to defend or condemn these economic doctrines but rather to point out their similarities and differences as compared with the philosophy of cooperation.

**Similarities.** Capitalism may be briefly defined as a system of economic organization in which capital is invested for gain by the investor. Private property rights in both producers' and consumers' goods are the basis of capitalism. Other socio-economic institutions fundamental to the system are those of inheritance, right of free enterprise, right of contract, guaranteed privileges, and personal liberty. Cooperatives possess many features found in a capitalistic enterprise—they require capital to carry on their functions and pay interest for its use; they need labor and, when forced by competitors, attempt to get it as cheaply as the capitalists do; they use land, buildings, and equipment, which they attempt to purchase as reasonably as possible; they employ managers who retain their positions on the basis of the merits of their services; they appeal to producers on the

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grounds that they will gain by being members; if business is done with nonmembers they may gain or lose in their transactions; they attempt to eliminate competition and to obtain exclusive control of the market; they depend upon business efficiency for success; and they favor the retention of the socio-economic institutions that are basic to capitalism.

**Differences.**—The differences, however, between a cooperative corporation and a private corporation are much more striking than the similarities. The most important difference lies in the aims. A capitalist invests capital with the primary hope of *profit* for himself; a cooperative member uses capital as a *means* to provide marketing services at cost. In the former, the basis of organization is *money*; in the latter, it is the *individual* or the *user* of capital. In the former, operations are designed primarily to earn profits and secondarily to provide only those goods and services which may bring profits. The cooperative is also interested in savings or gains, but these are secondary to the performance of efficient services. The capitalist attempts to eliminate competitors and to secure monopoly advantages for himself; the cooperative attempts the same elimination and procurement of monopoly advantage, but for the benefit of the members. It, moreover, strives to liberate its members from unbridled competition among themselves and from the competitive advantage of those with whom they must deal. Whereas the capitalistic system tends to concentrate wealth among the capitalists, the cooperative system tends to decentralize it among its members. Likewise, whereas the private corporation attempts to make its capital shares valuable, the cooperative aims to make agriculture prosperous.

The private corporation is an outgrowth of the joint stock company and serves a most important function in that it provides for the amassing of larger sums of capital than could be supplied by one person or a workable partnership. Persons who invest their funds in a corporation obtain shares of stock. They wish to secure dividends upon their investment without having to work for the corporation, supply it with raw materials, or purchase its services or commodities. Their relationship to the corporation is highly impersonal. In a cooperative corporation, on the other hand, there is a personal relationship between the member and his organization. The member does not invest in

**COOPERATION—ITS SETTING IN AN ECONOMIC SOCIETY 15**

the cooperative as a lucrative investment medium but rather for the purpose of establishing a company which will market his products. Any savings over and above actual costs of operations are returnable to the members on the basis of patronage contributed and not on the basis of the amount of financial investment. Such differences as these are shown in the following tabulary series.

	Cooperative corporation	Private corporation
<b>Purpose</b>	Secure increased returns, better marketing services, marketing services at cost, and improve plane of living of members	To profit upon investment and perform marketing services for the benefit of shareholders
<b>Basis of organisation</b>	Farmers producing the products to be marketed	Money—only persons with wealth can invest
<b>Incorporation</b>	Under cooperative laws	Under general corporation laws
<b>Membership</b>	Usually unrestricted—bona fide producers eligible. Selective membership policy based on willingness of members to cooperate. Membership not transferable or assignable in a non-stock association. Restriction on sale of shares of stock by stockholders. Stock not sold on public exchanges	Often restricted—many corporations are "closed" corporations in which stock cannot be purchased. No restrictions on sale of stock by shareholders. In "open" corporations stock available to anyone having funds. Stock sold "on the open market"
<b>Government</b>	On a democratic basis; usually on a one-man one-vote basis, or on a patronage basis. Voting by proxy not allowed. Number of shares that one person may own often limited. No concentration of control by an "inside" group	On the basis of shares of stock owned—ordinarily one vote for each share of common stock held. Proxy voting permitted. No limit on shares of stock any individual may own. Control often concentrated in a small minority of "insiders"
<b>Operations</b>	In the interest of producer-members. Pooling of resources, expenses, products, and sales receipts. Sales at best prices obtainable	In the interest of shareholders. Purchases at lowest price possible and resale at highest price obtainable.
<b>Prices and margins</b>	Operations at cost. Interested in narrow margins and in as high a price level as long time marketing operations can reasonably secure*	Chief concern to widen margins to most profitable amount. Less concern over the height of price level
<b>Patronage</b>	Secured from members and in many associations also from non-members	Seldom patronised by stockholders, but by anyone whose business can be solicited
<b>Savings</b>	Returned to members on patronage basis. Limited interest payment on shares of stock. No speculation in stocks. Wealth is widely distributed among patrons	Profits distributed to shareholders on basis of shares owned. No limit to dividends on capital. Aim of members in buying stock is often to profit from its resale. Tendency to concentrate wealth among shareholders

\* For example, a cooperative is much concerned whether the price of hogs is \$10 per hundredweight or \$4. It aims to obtain the highest price possible for farmers. A private corporation is much less concerned about the particular level of hog prices. It is more deeply interested in the margin it may obtain for handling hogs, i.e., if this margin is 50 cents or \$2 a hundredweight.

## COOPERATION VERSUS SOCIALISM

Professor William H. Kiekhofer states that "the term 'socialism' is properly used to designate any one of three things: (1) a proposed organization of economic society; (2) a political movement aiming at the attainment of the socialistic state; and (3) a certain body of economic principles or theories set forth by socialists as a philosophical basis of the social movement."<sup>4</sup> There are several types of socialism which have been termed Marxian, Fabian, Guild, Christian, and Utopian. These different sects grew out of disagreements among the socialists as to the method of establishing a socialistic state, as to how property should be held in common, or as to how distribution of goods and services should be carried out. All socialists, however, have certain principles in common, even though there may be disagreement as to the precise methods of attaining their objectives.

Socialism requires that the process of production and distribution should be regulated, not by competition, with self-interest for its moving principle, but by society as a whole, for the good of society. The term "collectivism" more accurately connotes its aims and methods. This implies that the individuals who make up society should, in their collective capacity, possess all the instruments of production, and thus prevent the evils arising from the present industrial system. It implies the subordination of the individual to the community, and puts public utility above private interest. Under the new socialistic regime, it is assumed that all will receive their due, according to the measure of their capacity and willingness to perform the social duties assigned to each by public authority.<sup>5</sup>

These principles will be delineated and contrasted with those of cooperation. It will be seen that the economic philosophies are dissimilar and that the few likenesses that do exist are more superficial than real.

Socialists wish to abolish private property rights in all instruments of production which may be used to exploit labor, and in the place of competition, the regulative force in production today, the socialistic state would exercise supreme control. Since capital would be collectively owned by the state, the capitalists as a

<sup>4</sup> KIEKHOFFER, WILLIAM H., "Economic Principles, Problems, and Policies," p. 913, D. Appleton-Century Company, Inc., New York, 1936.

<sup>5</sup> PALGRAVE, INGLES R. H., "Dictionary of Political Economy," The Macmillan Company, New York,

class would be eliminated. Wages, rather than interest, rent, or profits, would be the chief monetary income under socialism, and these would be distributed according to some system mutually agreed upon, presumably according to the needs of the workers. Since no private receipt of interest payments on production goods would be possible, it is also doubtful if private accumulations of capital would be encouraged.

Let us contrast these doctrines with those of cooperatives. The fundamental difference lies in the fact that cooperatives do not advocate collective ownership of production goods by the state. Carried to its logical conclusion socialism would require state ownership and control of farm land. Such a procedure is entirely remote to the philosophy of cooperative marketing which American farmers have endorsed. Cooperatives distribute savings according to patronage and not according to the needs of farmers. Moreover, savings are encouraged, since cooperatives pay nominal rates of interest upon capital investments. It has been said that if the present capitalistic order were overthrown in America, the agrarian class would most bitterly oppose the change and would put up the last defense against encroachments upon the institutions of private property. Also the source of income to members in cooperative associations is not wages alone but a combination of wages, interest, and unearned increment. Politics is a vital part of socialism but is singularly absent in the cooperative.

It is apparent from these basic differences that cooperation and socialism differ on several important points. Cooperativism is therefore preferred by farmers to socialism, since it provides them with a system of safeguarding their private property rights, while socialism would confiscate property for the state, in which case, control would be in remote hands rather than in that of the individual farmer as it is today.

#### **COOPERATION VERSUS COMMUNISM**

It has been seen how the underlying philosophy of cooperative marketing institutions differs from that of socialism. A still greater difference, however, exists between this philosophy and the economic doctrines of communism. Under communism, consumption goods as well as production goods are to be owned collectively by the state. During the nineteenth century many

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communal societies were formed in America in accordance with several current doctrines for social, economic, and religious reform. In these communities production was regimented and articles of consumption rationed out to each member according to his needs. Farmers in America, however, do not consider communal life as an end in their cooperative enterprises. Although they have not, on the whole, successfully employed their real property as a capitalistic instrument of exploitation against other classes in society but rather in many instances have become victims of its possession, they, nevertheless, tenaciously hold to their property as the only thing which, they believe, can give them any assurance of security in a capitalistic society.

Farmers desire to initiate reforms which will result in their economic betterment; they do not wish to make radical changes in their mode of living or to break with the desirable traditions of the past. Through economic and social improvements, they hope to enable their members to lead a richer and more natural life. Moreover, leaders in the cooperative movement have not followed a militant, radical program to achieve their ends as the communists have but, on the contrary, have learned that cooperation succeeds better as an evolutionary development rather than as a revolutionary outburst. Although in Russia communism of several different forms has been in existence, nevertheless, cooperative selling and purchasing have been tolerated only under certain restrictions.

### COOPERATION AND FASCISM

Beginning as a movement of armed, marching, and sometimes fighting bands (the *fasci di combattimento*, from which the name "fascism" is derived), without clear-cut economic objectives or program, the fascist movement in Italy has gradually developed a distinctive program of action and philosophy, political, economic, and social. In its economic aspects fascism may be described as a plan which retains private property in production goods but makes the investment and management of capital subject to state control. The capitalistic organization of economic life, according to fascism, is thoroughly defensible, but inefficiency and waste are intolerable.<sup>6</sup>

Dictatorial control of all industrial and commercial life supersedes democratic control. Fascism, like socialism and communism, is as much a political as an economic doctrine. In Italy

<sup>6</sup> Клекингов, *op. cit.*, p. 930.



the cooperative movement has been brought under the control of the fascist regime, but those cooperatives that were not operated in conformity with the fascist party principles were either reorganized or dissolved. The cooperative marketing movement in the United States both resembles and differs from economic fascism. If the sentence in the above quotation were paraphrased to read as follows: "In its economic aspects cooperation may be described as a plan which retains private property in production *and consumption* goods but makes the investment and management of capital subject to the *democratic* control of the membership," the striking difference between cooperation and fascism becomes apparent. A cooperative is fundamentally a democratic institution controlled by its members to promote their interests. A fascist corporation is autocratically controlled by the state and operated in the interest of the state.

From this brief analysis, it is apparent that cooperativism is not socialism, communism, fascism, or capitalism. Cooperativism can be described as a synthesis of several plans of economic organization. In some ways it resembles laissez-faire capitalism and to some extent socialism, but it differs from both of these sufficiently to make it a distinct and independent system. It is distinguished from these other systems by its objectives and principles rather than by its operating methods. It is not "just another business." Like the capitalistic organizations in America, it operates under the principles of *laissez faire* in which competition and government regulation are relied upon; and, like the socialistic organizations, it abolishes the profit motive and aspires to give to the members a larger share of the consumers' price. The changes it makes in the ordinary types of corporate organization are in conformity with its economic objectives. Cooperativism modifies the extremes of capitalism, fascism, and socialism. It occupies in many respects a middle course and is neither conservative nor radical. It is a liberal movement, practical in application and idealistic in purpose.

#### COOPERATIVE MARKETING AND THE STATE

There are no special privileges or concessions not accorded to other commercial organizations which farmers ask of the state for their cooperative associations. Legislation legalizing the cooperative associations did not involve special concessions.

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Neither do cooperatives seek paternalism; all they ask is the same fair treatment granted to others. As Mr. Babcock states,

All that I would ask from any administration for the protection and furtherance of the agricultural cooperative movement in these United States would be two things: (1) A guarantee that cooperatives enjoy a free and unobstructed channel to the investment market for the purpose of selling their securities. Such a guarantee has been most effectively given to cooperatives through the agency of the present Farm Credit Administration. (2) Provision that cooperatives be exempt from corporation and income taxes on that portion of their earnings which they pass back to their members in the form of patronage dividends.<sup>7</sup>

Only in a limited way during the period of the operations of the Federal Farm Board have cooperative marketing organizations been the special beneficiaries of federal or state subsidies, but in this respect they have not received so many gratuities as the railroads, the aviation industry, the merchant marine, and other major industries. Cooperative sales and purchasing associations pay taxes like all other corporations. They are, however, exempt from paying capital stock, excess profits, and income taxes, provided they qualify for exemption. For the past two decades cooperatives in general have received favorable treatment and open endorsement of state and federal governments, recognition by the courts, and encouragement by practically every commission that has investigated agricultural conditions.<sup>8</sup> The approval of the cooperative system of marketing farm products is based upon its economic soundness and upon its demonstrated ability to ameliorate conditions in the distributive system for agricultural products. Our government grants and protects

<sup>7</sup> BABCOCK, H. E., *Cooperatives as a Means for Doing Business Practically*, p. 41, "American Cooperation, 1935," American Institute of Cooperation, Washington, D. C.

<sup>8</sup> The Joint Commission of Agricultural Inquiry in House of Representatives, 67th Congress, 1st Session, *Report 408*, Part IV, p. 9, "recommends that the agricultural producers of the United States be encouraged to develop cooperative associations to hasten the standardization of agricultural production, improve the distributive processes, and reduce their costs."

See also "The Condition of Agriculture in the United States and Measures for Its Improvement," a report by the Business Men's Commission on Agriculture, National Industrial Conference Board, Inc., New York, and Chamber of Commerce of the United States, Washington, D. C., 1927.

property rights in patents, copyrights, and trade-marks of private corporations and individuals; it has a Department of Commerce to promote and foster domestic and foreign commerce for the direct benefit of private businesses and for the indirect benefit of the general populace. In similar manner the Department of Agriculture and Farm Credit Administration through research and service functions may benefit cooperative associations and individual farmers directly and the entire nation indirectly. Such aid should be encouraged rather than discouraged.

#### COOPERATION AND PRIVATE MIDDLEMEN

Private middlemen usually question the advance of the cooperative movement and frequently take active steps to retard its growth and curb its activities. Slush funds, passage of resolutions condemning farmers' selling and buying associations, and other similar means have been used to defeat the farmers' efforts. Such concerted action is prima-facie evidence in itself that private tradesmen recognize in the cooperative a powerful competitor. There is no doubt that cooperatives exert a different competitive force in the marketing system from that of the usual private dealer. This difference may be summed up in the concept that a cooperative returns to farmers all it can while a private dealer pays only as much as competition forces him to. As a result many private operators have been forced to narrow their margins or abandon their business. Cooperatives have also been forced out of business by more efficient private dealers.

But, cooperatives are not competitors of all private businesses—for many they are the most dependable sources of raw materials. Thousands of local associations regularly supply jobbers and auction companies with high quality products, and many a processing plant obtains its products from farmers' companies. It is, no doubt, for this reason that some terminal market dealers who are dependent upon the cooperatives assert that *local* cooperation is sound but cooperation beyond that point is unsound. There is, of course, no validity for such statement. Cooperative marketing companies need private retailers and often other private marketing agencies to get the widest distribution for their products. Mr. Charles Teague, President of the California Fruit Growers Exchange and of the California Walnut Growers Association, makes this clear in the following statement:

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We believe in the established channels of distribution. In the organizations with which I am connected, we do not attempt to short-cut to the consumer. In the fruit business someone must perform the [jobbing] function and someone the retail function; we do not believe that the cooperative marketing organization could itself perform either one as well, or as cheaply, as it is now being done by the 4,000 odd jobbers and 500,000 retailers who handle our commodities. We work with the trade constantly in cooperative merchandising endeavors and desire that every trade factor handling our goods and performing a service shall make a fair profit in so doing, for otherwise he will not long handle it. As a consequence we are regarded by our trade as allies rather than as competitors, a most important trade relationship to maintain, in my opinion.<sup>9</sup>

### COOPERATIVE MARKETING AND CONSUMERS

If cooperative sales associations achieve their goal of returning higher prices to their members, is not this at the expense of consumers, and, therefore, a movement to be feared by them? A brief examination of the facts will show such fear largely unfounded. The retail price of oranges in 1936 was less per dozen than in the first years following the turn of the century. Oranges were once a luxury. They have been marketed by cooperatives for more than 40 years, but retail prices instead of increasing have been decreasing. There is every reason to believe, however, that producers are receiving a higher proportion of the retail price from their cooperative than they received from middlemen before the cooperative was organized. This is only one of many illustrations that can be cited. The reason is that higher net returns received by farmers lead to larger production, and larger production in turn to lower prices, until the market demand is again broadened to absorb such increased production at higher prices. In most manufacturing industries, production is adjusted to market demands at a certain administered price, but in agriculture production responds to competitive prices and is not regulated. Thus, consumers as a class have more to gain from successful cooperatives than from a continuation of any inefficient system of marketing.

Other advantages inure to consumers which are the result of careful grading, packaging, and orderly market distribution by

<sup>9</sup> TEAGUE, C. C., *Management Relationships*, p. 115, "American Cooperation, 1935," American Institute of Cooperation, Washington, D. C.

the cooperative. Moreover, cooperatives eliminate speculation in food products, waste and spoilage, high costs of distribution resulting from failure to coordinate and integrate marketing operations, and monopoly influences that prevent farm prices from properly reflecting retail prices. The beneficial effects to society as well as some of the limitations of the cooperative form of business will be noted under the various headings throughout the succeeding chapters.

#### Questions

1. How does the cooperative law in your state define a cooperative association? How would you define a cooperative association in your own words?
2. What is the purpose, objective, or goal of a cooperative sales association? Why are associations organized?
3. What alternatives are open to farmers to improve their economic status? Why was cooperation chosen as the most hopeful means for alleviating their condition?
4. Show how a private corporation resembles and differs from a cooperative enterprise.
5. "The cooperative movement is simply a type of socialistic procedure designed to overthrow capitalism in this country." Critically appraise this assertion.
6. "Cooperative marketing could not succeed were it not for the constant nursing by an altruistic government. It is a clear case of paternalism gone wild." How would you reply to such an attack?
7. Give four concepts of cooperation and show how they differ from one another.
8. Look up in your library reports upon the state of agriculture made by various commissions and note the statements made to the effect that cooperative marketing and purchasing are a relief measure.
9. Do consumers have to fear the organization of farmers' cooperative sales associations?
10. In what sense is a cooperative association more democratic than a private corporation?

## II

### *The Forerunners of the Cooperative Movement*

*A historical account of the development of cooperative enterprises reveals how versatile successive generations have been in adapting their organizations to their needs from the earliest known instances to the great cooperative institutions of today. Often men wish to escape the realities of life, and when they do, they dream of Utopias. During these brief imaginative moments of escape from things as they are, they visualize things as they would have them in a new society unrestrained by either natural or superficial barriers. This propensity to plan for the future provides the basic architectural designs for a new order replacing the economic and social institutions that have become obsolete.*

*The more soundly these plans are conceived the more certain will be the progress of man, especially during periods of rapid changes in the social and economic systems. The phenomenal achievements which certain European nations have attained through cooperation are due in no small measure to the foresight and indomitable courage of their leading thinkers. Alfred Marshall, the British economist, evaluated collective action as a vital force. To him cooperation is distinguished from all other movements by its calm and wise business practices and by its strong and fervent faith.*



## CHAPTER II

### THE FORERUNNERS OF THE COOPERATIVE MOVEMENT

#### THE ANTIQUITY OF COOPERATION

Cooperation is as ancient as mankind itself. In one manner or another, humans have not only found it advantageous, but congenial to work together. Man ceaselessly discovers new ways and means of uniting his powers and his resources with others for mutual benefit. During various periods in the development of civilization, the predominating motivations for concerted action have been quite different in character. Eons before the dawn of history, the species *Homo sapiens* associated for protection against enemies and for the procurement of food. Although the extent of association among our pristine ancestors is largely a matter of conjecture, there are some curious instances of cooperative effort in early civilization periods.

In China, a religious custom made it essential for men to undertake a journey to a sacred mountain at least once during a lifetime. The devout souls who lived near the borderline of dire necessity found it difficult to save enough money to defray the expenses of their pilgrimage. Impelled by this pious motive, the Chinese organized the first credit and savings societies.<sup>1</sup> Other events in the lives of the Orientals created a congenial environment for these mutual savings societies; until this day the weddings and the funerals of the Far East are ceremonies so freighted with expenses that it takes the average citizen the greater part of his lifetime to accumulate enough to meet them. "Crop watching" was another incentive for cooperative organization in China. To guard against vandalism and theft by wandering bands of robbers, those engaged in cultivating crops were forced to keep watch over their fields day and night.<sup>2</sup>

<sup>1</sup> SMITH, ARTHUR H., "Village Life in China," 4th ed., pp. 141-142, Fleming H. Revell Company, New York, 1899.

<sup>2</sup> *Ibid.*, pp. 161-168.

Some irrigation systems of medieval times were constructed and managed cooperatively. In arid regions where the Mediterranean type of climate prevails, such as the southwestern part of the United States, Egypt, and the Levant, crops could not be cultivated successfully without supplementing the natural rainfall. Cultivators residing in the same ravine or valley united their forces in building a system of flumes to direct the flow of water from field to field and from farm to farm. The successful distribution of water required the full cooperation of every individual participant, especially where the supply of water was limited; otherwise the fields at the lower end of the flume might easily be parched. Each member of the irrigation system was expected to keep his section of the flume clean, unobstructed, and in good repair, and the quantity of water which he could shunt at any time was contingent upon the requirements of neighbors living below him.

About a century before the Trojan war, Minos, mythical son of Zeus, conquered several islands, chief of which was Crete. Here he established a communal society which for several hundred years was governed by laws exemplifying unusual justice and virtue. Fellowship was fostered by rearing and educating the children in common at the expense of the state, and rich and poor alike were fed in the dining rooms of his dominion. A moral code, the object of which was to banish idleness and vice, decreed a kind of equality for all citizens. While slavery existed in the Cretan state, the Cretans distinguished themselves by their humane treatment of their vassals; accounts describe the feasts of Hermes when free citizens and masters served their slaves and paid them the same honors received of them during other days of the year.<sup>3</sup>

Before assuming the leadership of the Spartans, Lycurgus visited several countries in Asia and Africa where the customs and institutions had attracted notable attention, but he was most favorably impressed by the laws and institutions of Crete, a neighboring island state, and he established the senate in imitation of the Cretan council. This body functioned as a kind of counterpoise to the monarch. Lands in Sparta were divided

<sup>3</sup> ROLLIN, CHARLES, "The Ancient History of The Egyptians, Carthaginians, Assyrians, Babylonians, Medes and Persians, Grecians, and Macedonians," vol. 1, pp. 370-372, George Dearborn, New York, 1836.



fairly and equally, and all the people were required to eat together in public places at the expense of the individuals comprising the groups.

The tables consisted of about fifteen persons each. . . . Each person furnished every month a bushel of flour, eight measures of wine, five pounds of cheese, two and one-half pounds of figs, and a small sum of money for preparing and cooking the victuals. Everyone without exception . . . was obliged to be at the common meal.<sup>4</sup>

The empire of the Incas in South America is an illustration of a communal society which arose without the philosophical assistance of the Aryan world. It thrived for three hundred years or more until the conquest of the Spaniards in 1529.<sup>5</sup>

There is some basis for believing that our modern industrial and social cooperative schemes have been influenced by the heritage of social thought as recorded in such works as Plato's "Republic" (430 B.C.), the teachings of Christ, Sir Thomas More's "Utopia," "The New Atlanta" by Lord Bacon, Campanella's "City of the Sun," and Harrington's "Oceana." Collective effort in the peaceful pursuits of life among ancient peoples was a spontaneous reaction to immediate needs; one might call it "subconscious cooperation."

The cooperative movement has passed through successive stages of development, but only within the last century has emphasis been given to economic associationism. This phase of its development was incidental to the industrial revolution but by no means without precedent before the nineteenth century.

#### THE MEDIEVAL GUILDS

The guilds probably represented the first great conscious movement toward formal organization designed to promote the welfare of selected groups in society. As early as 300 B.C. the Greeks formed associations known as *Eranot*, which possessed many of the characteristics common to the guilds that were formed in Teutonic Europe between the seventh and fifteenth centuries. If their financial circumstances permitted, members were expected to make an annual contribution to a general fund. Each guild carried on certain kinds of business, gave protection to members

<sup>4</sup> *Ibid.*, pp. 173-175.

<sup>5</sup> GIDE, CHARLES, "Communist and Cooperative Societies," p. 42, Geo. C. Harrap & Co., Ltd., London, 1930.

during periods of illness, arranged for funerals, provided feasts, and aided and comforted those in distress.

There is some historical evidence to support the belief that the guilds of the Saxons and the Franks were patterned after the Roman *Collegia* which were contemporary with the Greek *Eranoi*. Plutarch, the Greek moralist, listed nine craft guilds purported to have been instigated by Numa, the Roman. Early Greek associations manifested a tendency toward specialization at their inception and were either religious, political, or commercial in origin.

The first guilds of Northern Europe undoubtedly were formed as a defense against invasions and served to maintain peace and order within the communities, which were later the nuclei of many towns and local governments. The guild laws, with some modifications, were generally adopted as the laws of the local governments. Landowners and leaders who had been the most aggressive in organizing peace guilds and in forming their local governments usually monopolized trade in their communities. When town governments were established as units of a dukedom or a kingdom, the landowners and leaders obtained charters granting them the exclusive rights to trade and to protect their interests through the guilds which they had formed. While trade in the Middle Ages was largely restricted to the manor or town, there was always some importation of goods from other districts or regions, and exchange was effected greatly to the profit of those holding vested interests in the markets. In the course of time, traders bearing goods from the "outside" were more frequently admitted into the community until their visitations became a regular annual or semi-annual event. Some lords and leaders who controlled the local markets did much to encourage trade, especially in those towns situated on important rivers and along the sea coast. When the number of foreign traders increased and different markets vied with each other for supremacy, those in charge arranged a system of fairs which were held for periods of a few days to several months. Conflicting dates were avoided insofar as it was possible, so that each market might attract the maximum number of traders who made it a business of traveling from fair to fair throughout the season. Specialization in handicraft production in different areas tended to minimize intermarket competition and to place commerce on a mutually

profitable basis. Incidental to this system of exchange there evolved a body of laws governing transactions which, through the influence of traveling traders, became more or less common to many markets. Each market had its own judicial organization known as the "piepowder fair court" in which disputes were summarily settled. During the period from the eleventh to the fourteenth centuries there was a rapid growth of trade guilds and craft guilds, particularly in the centers where protection and peace were assured. The widespread adoption of Christianity in Northern Europe during this same period gave impetus to the organization of social guilds.

The social guilds were the antecedents of the Friendly Societies, and the Friendly Societies were the forerunners of the numerous charitable, fraternal, and social organizations of today.<sup>4</sup>

#### A PERIOD OF INSTITUTIONAL CHANGES

For ages feudalistic Europe with all its accoutrements of the nobility, lords, estates, manors, and restrictive laws had frozen the lower classes to the land from which there was no escape. A series of events, beginning with the bubonic plague in the middle of the fourteenth century, resulted in the freeing of the land-bound masses from serfdom and the villenages. Home industries began to develop. The era following the rediscovery of America by Columbus was one of exploration conducive to expansion in commercial activities. Trade, when once wrested from the powerful commercial monopoly of the Hanseatic league of the Baltic region, fell by favor of the king to English merchant adventurers. International trade grew and the advantages of transporting articles of commerce in a country's own bottoms brought about a long struggle for supremacy on the high seas. Changes in the channels of commerce lessened the importance of local markets and consequently diminished the influence of trade guilds.

During this period of great institutional changes, religious organizations were being reformed; the church was subordinated to the state and removed from the jurisdiction of the papacy.

<sup>4</sup> For an illuminating discussion refer to Joshua Toulmin Smith, "English Guilds," preliminary essay by Lujo Bretano, *On the History and Development of Guilds and the Origin of Trade Unions*, Truebner & Co., London, 1870.

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† Their close relationship to the church involved the social guilds in the changes that were to come.

Henry VIII, King of England, confiscated the financial reserves and the landed property of the guilds and the monasteries, and Edward VI dissolved the chantries.<sup>7</sup> With the abolition of the monasteries and the social guilds, the state undertook the duty of providing charity and schools; alms and learning had been assumed responsibilities of the guilds and the monks. However, the inclosure movement<sup>8</sup> which resulted in the wholesale eviction of tenants and villeins placed more of a burden on the king's exchequer than was anticipated, and, instead of alleviating poverty or pauperism, it precipitated disaster for many. Parliament sought to solve this social upheaval by passing a series of "poor laws" that placed the responsibility of supporting the poor upon local communities,<sup>9</sup> but the mere enactment of laws cannot do away with vital institutions which are an inherent part of society. Like gnarled oaks on windswept highlands, organizations of natural growth may be bent and twisted by the whims of a king or the momentary caprices of a legislature but cannot be uprooted by either rulers or parliamentarians.

#### THE FRIENDLY SOCIETIES

In passing the sequestration acts, Parliament tempered its language to make the greed of the Tudors seem less rapacious. The king's commissioner was instructed to suppress the institutions cultivating religious superstitions and corrupt practices. This official naturally found evidence on every hand of abuses, corruption, and general decay among the business, social, and religious foundations of the day. Only a few of the guilds were spared from the confiscation of their property by the crown.

<sup>7</sup> CHENEY, EDWARD P., "A Short History of England," Chap. XI, p. 272, Ginn and Company, Boston, 1904:

"A chantry was an endowment to pay the expense of keeping up a shrine in a church and supporting one or more priests to perform service at it in memory of the founder."

Refer to Parliamentary Acts 27, 31, and 37 of Henry VIII and Act 1 of Edward VI.

<sup>8</sup> The inclosure movement was a transition from strip farming to a type of large-scale enterprise in agriculture. Extensive tracts of fields and commons were enclosed with hedges to make easier the herding of sheep.

<sup>9</sup> CHENEY, *op. cit.*, Chap. XII.

The robbing of the guilds and the monasteries immediately plunged the poor classes into greater depths of misery. The English nation was undergoing a transition from a period of self-sufficing agriculture to that of a commercial commonwealth.

From the last quarter of the sixteenth century to the beginning of the eighteenth century, there were small scattered groups of individuals who clung resolutely to the principle of self-help in preference to charity from the state under the conditions of its administration. The conciliatory attitude of the trade guilds made it possible for them to readily adapt themselves to the new conditions; and their tenets and ties of brotherhood, which had formerly been reserved for a select number of patrons, were now made accessible to large numbers by virtue of the newly acquired democratic ideals. The rapid increase in the number of trade guilds paved the way for an amalgamation of local units into social orders, as well as the reorganization of aid societies patterned after the old religious-social guilds. In this period of readjustment and change the aid societies resorted to secrecy as a mode of protection and a means of transmitting through time the glorious traditions of the past. In his essays, such as "Giving Alms No Charity," Daniel Defoe, the father of the English novel, took up his pen in protest against the deplorable conditions of the working classes. He advocated compulsory societies and the policy of giving the able bodied no relief without work. Those in substantial agreement with Defoe revived the old brotherhoods in protest to the Poor Law Acts of Queen Elizabeth and William III.

At the beginning of the eighteenth century, the guild of the craft of masonry, by introducing mystic rites and observances, transformed its organization into a social order called Freemasons. The order proved to be eminently successful, and men of all ranks in society became members. Other guilds in this period quickly formed fraternal orders, imitating the Freemasons in design and purpose, such as the Odd Fellows, the Druids, the Free Gardeners, the Foresters, and a great number of others less well-known because of their short existence.<sup>10</sup>

On the first day of summer in 1793 the British Parliament passed an act which assured the people the right to form voluntary

<sup>10</sup> HARDY, GEORGE F., "Messenger Prize Essay on Friendly Societies," Charles and Edwin Layton, London, 1887.

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associations for the purpose of aiding one another during times of sickness, need, and bereavement. Prior to this act, these associations had no legal status under which they might safeguard themselves against exploitation and fraud. The act of 1793 was amended five times before 1820 and rewritten as many times during the nineteenth century, not to mention the number of amendments each act engendered. This legislative activity is, in part, evidence of the extent to which the English preoccupied themselves with reform of social conditions.

It is estimated that in the year 1800, there were in the British Kingdom 7,200 societies with a membership of 600,000. It is believed that in London more than 70,000 people belonged to 600 lodges. The friendly society movement was more tardy in its development in other European nations, and nowhere did its roots penetrate so deeply as in English soil.

The benevolent and provident societies were born out of groups assembling periodically in the spirit of fellowship and mutual understanding. In the barren years when poverty and want stalked the homes of the common people, it was quite natural that they should exert themselves in discovering new ways and means of escaping degradation and misery, and, impelled by this objective, the laborers of English industrial towns launched upon new and untried social and economic experiments.

#### THE PENNY CAPITALISTS

One of the earliest attempts to conduct business on a cooperative basis in Britain is generally conceded to the small group of weavers in the village of Fenwick in Ayrshire, Scotland, who in 1769 formed an association to purchase for domestic production such handicraft supplies as weavers' reeds and for home consumption such items as oatmeal and staples. Because they set up their own business enterprises and endeavored to make all possible savings, they were scornfully called "penny capitalists" by the multifarious shopkeepers of that period.

Undoubtedly a number of similar societies arose and sank into oblivion from 1769 to 1794, when the records bring our attention to the next association organized at Mongewell, Oxfordshire, for the purpose of purchasing the necessities of life at the lowest possible prices. Some writers refer to this association as the first cooperative store.

In 1795 the inhabitants of Hull, England, revolted against "the invasions of covetous and merciless men" by establishing an antimill society. Through the operation of its own mill, this society provided the flour and some other common articles of consumption for about 1,400 people. The flour mill continued operations for more than one hundred years. Similar supply societies were established at Devonport and Sheerness. After the turn of the century, the tide of migration from the country into the industrial centers swelled, and the handicraft industries began to wane. Living in the new environment presented many serious problems.

In 1812 an association at Lennoxtown, Scotland, introduced the novel feature of dividing its yearly surplus among its patrons according to the amounts of their purchases. This scheme of apportioning net earnings has become basic to cooperative organization throughout the world. Fourteen years later this association incorporated under the name Friendly Society. This legal step to limit personal liability suggests modern business organization and identifies the association with the larger and more general organization movement of the time.

A number of families in London carried out their idea of a self-employing cooperative community by founding, in 1821, the Cooperative and Economical Society, the purpose of which was to unite the community in the operation of a store for the purchase and distribution of supplies at cost and in the provision of facilities for gaining a livelihood and for the education and recreation of its members. Its failure is another instance of ambition winding its steed.

#### THE BRIGHTON EXPERIMENT

Probably one of the most notable instances of early cooperation was the experiment of the working class at Brighton, England, in 1828. Holyoake gives the following description of its organization, "Its funds were raised by penny subscriptions. It had 170 members, who ultimately accumulated £5 with which they commenced their store, and their first week's sales amounted to half-a-crown." The Brighton Cooperative Society acquired a few acres of land on which its members kept gardens and grew some products to be sold through their store.

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Dr. King, editor of *The Cooperator*, wrote to Lord Brougham giving an account of the new organization in his community and asked counsel in framing laws which would aid and protect similar enterprises in other parts of England, because he believed in their principles and objectives. According to his judgment the workers could better their positions by withdrawing labor from the market and employing themselves in their own businesses. It is implied that the better wages resulting from decreasing the number of competing workers would improve the morale of the workers and increase their purchasing power. More income would create a new series of wants which would operate against pauperism and crime. Contemporary with the organization of the Brighton society other groups formed similar societies at Worthing, Darlington, and Findon.

#### THE ROCHDALE PIONEERS

The star of fame does not shine less brightly on the poor weavers of Rochdale because they were preceded by others, even in their own community, in the enterprise of purchasing cooperatively some simple household necessities. In 1830 fifty-two workmen, with a capital of £108 and a library of thirty-two volumes, formed a Friendly Society and engaged in the manufacture of flannel, employing the workers of ten members' families.<sup>11</sup>

Charles Howarth, who became the leader of the famous twenty-eight pioneers, tried to establish a cooperative store in 1833, but failed in the attempt. "It had died from the blight of the weaver's poverty." During the years 1843-1844 when unemployment was common and low wages general, some workmen were in the habit of meeting at "The Weavers Arms" and "The Socialists' Institute" to escape the despair of their homes and to banish cares in the companionship of fellow workers. Mr. Howarth's observations at these very informal social gatherings prompted him to suggest another attempt at economic emancipation. According to his plan each weaver was to save twopence a week which otherwise would be ill spent; by pooling these resources a capital fund large enough to begin a cooperative provision store could be created. After nearly a year's effort twenty-eight persons succeeded in saving £28, and on the evening

<sup>11</sup> HOLYOAKE, GEORGE J., "The History of Cooperation," rev. ed., p. 285, E. P. Dutton & Company, Inc., New York, 1906.



of December 21, 1844, they opened a store on Toad Lane in Rochdale. The twenty-eight undauntable pioneers were:<sup>12</sup>

Name	Occupation	Affiliation
James Smithies	Woolsorter and book-keeper	Socialist
Charles Howarth	Warper	Socialist
William Cooper	Weaver	Socialist
David Brooks	Block printer	Chartist
John Collier	Engineer	Socialist
Samuel Ashworth	Weaver	Chartist
Miles Ashworth	Weaver	Chartist
William Mallalien	Weaver	Chartist
George Healey	Hatter	
James Daly		
James Tweedale	Clogger	Socialist
Samuel Tweedale	Weaver	
John Kershaw	Warehouseman	Chartist
James Maden	Weaver	
John Screwcroft	Hawker	
John Hill		
John Holt		
James Standing	Weaver	Socialist
James Manock	Weaver	Chartist
Joseph Smith	Woolscrtter	Socialist
William Taylor		
Robert Taylor		
Benjamin Rudman	Weaver	Chartist
James Wilkinson	Shoemaker	
John Garside	Cabinetmaker	
John Bent	Tailor	Socialist
Ann Tweedale		Socialist
James Banford		

With their small amount of working capital, they could offer only limited supplies of butter, flour, oatmeal, and sugar. At first the store was open to the public only on Monday evenings, from seven to nine, and on Saturday evenings, from six to eleven, but after 4 months the store operated Saturday afternoons and every evening, except Tuesday. It took boundless courage, faith, and determination to sustain the Equitable Pioneers

<sup>12</sup> HOLYOAKE, GEORGE J., "The History of the Rochdale Pioneers," pp. 83-87, Swan Sonnenschein & Company, London, Charles Scribner's Sons, New York, 1893.

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through the first faltering years when the specters of poverty, indifference, and opposition mantled every move. The reward for their perseverance was great. The brilliance of their attainments can scarcely be measured by the summary figures of their yearly business transactions, but since pecuniary gains are perhaps the most commonly understood proof of success, such data are shown in Table I.

TABLE I.—GROWTH OF THE COOPERATIVE WHOLESALE SOCIETY OF ENGLAND, 1865-1935\*

Year	No. of members belonging as shareholders †	Total capital	Net sales	Sales expenses	Net surplus from sales
1865	24,005	£ 7,182	£ 120,754	£ 906	£ 1,850
1870	79,245	40,658	507,217	4,644	4,248
1875	198,608	263,282	1,964,829	28,436	20,684
1880	361,523	565,854	3,339,681	47,153	42,090
1885	507,772	841,175	4,793,151	74,305	77,630
1890	721,316	1,474,466	7,429,073	126,879	126,979
1895 ‡	930,985	2,093,578	10,141,917	199,512	192,766
1900	1,249,091	3,187,945	16,043,889	314,410	289,141
1905	1,635,527	4,398,933	20,785,469	396,767	304,568
1910	1,991,576	6,655,039	26,567,833	544,584	462,469
1915	2,535,972	11,075,199	43,101,747	715,365	1,086,962
1920	3,341,411	27,844,322	105,439,628	2,138,333	64,210‡
1925	3,778,659	45,369,050	76,585,764	1,658,465	1,053,504
1930	4,884,090	66,517,146	85,313,018	1,925,262	1,344,218
1931	5,138,124	72,366,833	81,498,234	1,929,137	1,692,157
1932 ‡	5,352,310	76,467,379	82,769,119	1,941,415	1,729,223
1933	5,488,364	84,060,875	82,120,864	1,976,166	1,473,838
1934	5,983,810	93,660,021	90,177,672	2,098,090	2,052,498
1935	6,155,964	104,098,072	98,283,975	2,102,208	2,095,481

\* Data furnished by Scottish Cooperative Wholesale Society, Ltd.

† Approximate number of consumers is four times the number of members or nearly 25 million in 1935.

‡ Period of 53 weeks.

‡ Deficit.

Not even the most optimistic of the men who called themselves the Equitable Pioneers dared dream of an industrial and mercantile empire so expansive as the one arising from the humble little cooperative store on Toad Lane. Strict adherence to sound

business principles is the usual explanation for the success of the weavers' enterprise, but devotion to principles does not fully explain the phenomenal growth of the Cooperative Wholesale Society.

It has been said that Englishmen possess a passion for federation. They perceived the advantages to be derived from integrating the local societies into large central associations with specialized functions. A decade after the act of 1852 which legalized the patronage dividend, another act was passed which permitted local organizations to federate into central exchanges. This enabling legislation made possible the formation of the English Cooperative Wholesale Society, Ltd. (1862), The Scottish Cooperative Wholesale Society, Ltd. (1868), Cooperative Insurance Society, Ltd., The Cooperative Union, Ltd. (1873), and a number of other satellite organizations in the cooperative system.

The Cooperative Wholesale Societies of England and Scotland have today a combined membership of 1,200 affiliated societies, with over 7 million members in England, Wales, Ireland, and Scotland. The two "wholesales," as the British call them, employ 192,000 workers in their retail stores and 78,000 workers in their own manufacturing plants and service departments, making a total of 270,000 men and women in all divisions of their organizations.

The Cooperative Wholesale Societies manufacture clothing, hosiery, leather, boots and shoes, tweed, linen cloth, blankets, bread, butter, flour and meal, sugar, preserves, confections, margarine, biscuits, bacon, lard, pickles and sauces, coffee essence, tobacco products, paper, soap, linoleum, furniture, tinware, brushes, paper bags, cardboard boxes, jute, chemical sundries, floor cloth, and a number of other items. Some of the services provided for its members are: funeral undertaking, laundry, dyeing and cleaning, distribution of fluid milk, legal services, transportation on land and sea, building, and financing.

The English Cooperative Wholesale Society has acquired 2500 acres of farm land at Shrewsbury and Hereford on which fruits and vegetables are grown, and in connection with these estates the society has provided a country home for members who are in ill-health. The Scottish and English Societies own jointly about 3,000 acres of tea plantations in Ceylon. Joint purchasing agencies are maintained in any part of the world where the

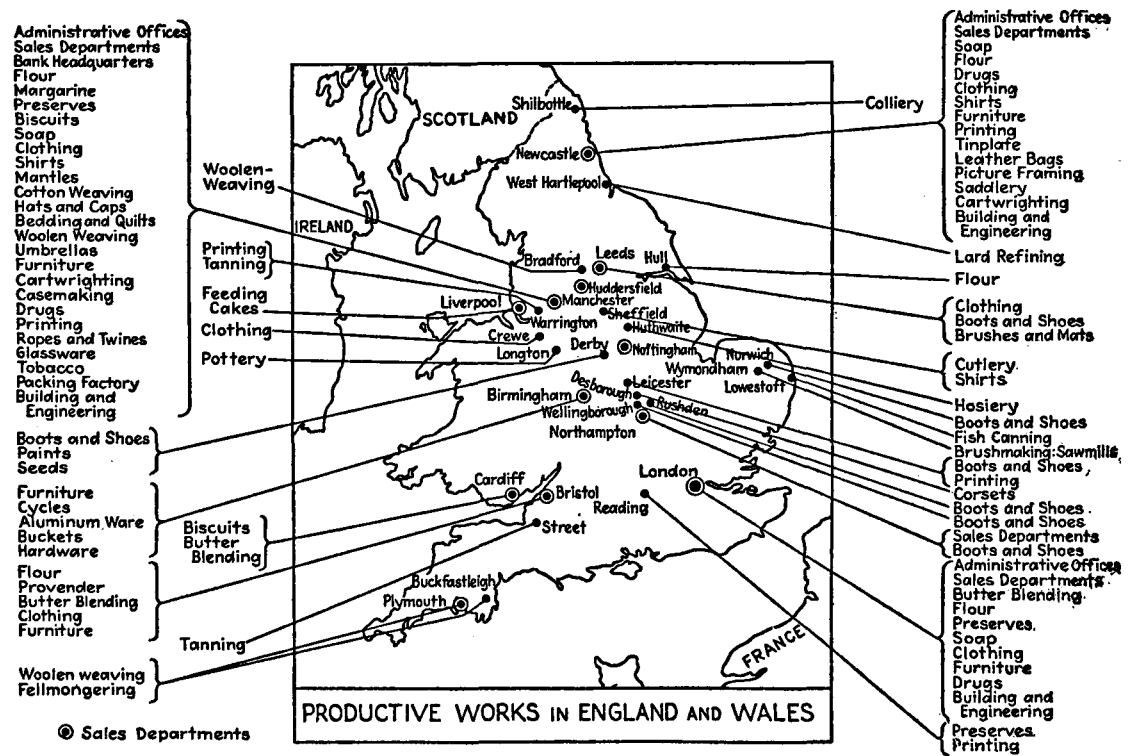


FIG. 1.—Manufacturing enterprises of the C.W.S. (Courtesy of the Co-operative Wholesale Society, Ltd. "The C.W.S. of Today" by George Darling.)

volume of business is large, and warehouses and depots are maintained for storing supplies.

The Scottish Cooperative Wholesale Society established a grain buying organization at Winnipeg, Canada, in 1906. The following year the society adopted the policy of building country elevators and purchasing wheat directly from farmers. From time to time units were added to their line until, in 1924, nineteen country elevators had been acquired in the provinces of Manitoba and Saskatchewan. About this time the extensive activities of the Canadian Wheat Pool made it prudent to curtail activities and reduce the investment in properties at loading points, and to sell several elevators to the Pool. More recently the society has again been active in the construction of elevators; it added two new units in 1935, another in 1936, and plans for expansion continue. Since 1906 the Winnipeg branch of the Scottish Wholesale Society has consigned approximately 50 million bushels of wheat to its mills in Scotland, the quantity in 1935 being nearly 5 million bushels. At one time the society even attempted wheat growing and in 1916 acquired 10,000 acres of land in the Saskatoon district, but due mainly to a succession of poor crops, this venture did not prove successful. In 1926 the land was divided into sections of 360 acres and sold to individual enterprisers.

#### THE RENAISSANCE OF COOPERATION

The simultaneous revival of cooperation in so many European countries during the last half of the eighteenth and the first part of the nineteenth centuries brings into sharper relief this awakening period of material welfare. The movement was a peaceful one in its conquest and less spectacular from the historian's point of view than wars and the affairs of royal families, but by reason of its force, universality, and possible duration, it merits a place of equal rank with such supreme events as the spiritual uprisings of the crusades and the rebirth of letters and arts in the preceding periods of European history. The spontaneity of the self-help movement and its multifarious applications cast doubt upon the claims of various countries to priority in the perception of cooperative ideals and the discovery of principles.

The people in some regions, through specialization, have evolved superior cooperative procedures for some branches of economic activity, and their organizations have served as models

for other communities engaged in the same forms of collective effort.

**In Germany.** It is claimed that cooperative agricultural loan associations existed in the province of Hanover in medieval times, but in the absence of records, one must accept such claims largely on the basis of faith. The history of the *landschaft* as an old institution of Prussian origin provides us with details of its organization and its influence upon the agrarian classes. Under a decree of Frederick William I in 1729, an attempt was made to form a mutual association of landowners in Saxony. This plan failed. Thirty-eight years later (1767) a Berlin merchant named Buring proposed a plan for financing agricultural landowners by forming a district organization, an association which would do away with the necessity of borrowing and loaning money among themselves with all the consequent evils and abuses. Under this plan all rural loans were consolidated into one organization, which would issue low rate interest bonds to be offered in the open money market by the bearer, who in most cases would be the borrower. The investors were to be safeguarded by a conservative method of evaluating properties on which loans were made, by a plan of amortizing the loan at a rate of 0.5 to 1 per cent per year, and by the accumulation of reserves in the district *landschaft*. Frederick the Great put Buring's plan into operation in 1770 by creating the Silesian Mortgage Credit Association. After a trial period of seven years, the popularity of the first *landschaft* resulted in the creation of the Kur and Neumarkische loan institutes in 1777, the Pomeranian Mortgage Credit Association in 1787, one in West Prussia in 1787, and another in East Prussia in 1788. Although these five *landschaften* organizations varied in the methods of conducting their business, they were essentially alike in principle and served as models for most cooperative landowners' credit associations in central Europe.

Personal credit was established on a nationwide cooperative basis in the rural regions by Raiffeisen, and in the villages and urban centers by Schulze-Delitzsch. Associations of the type advocated by these men (*Genossenschaften*) were originally formed at approximately the same time that Robert Owen and Dr. King were heralding the advantages of cooperative enterprise in England. To aid landowners in their capital requirements, the credit union of Württemberg was formed, in 1828, on a nonprofit

basis. The Land Bank of Wiesbaden, established in 1843, probably marked the beginning of organized banking for small farmers and landowners to aid them in breaking the last bonds of old servitudes encumbering the possessions of peasants from feudal times. How similar this story is to that of the Rochdale pioneers who associated to escape the exploitation of capitalist manufacturers and shopkeepers! -

From this date, 1843, to the financial crises of 1873 following the Franco-German war, the boom spirit carried everyone beyond the safe limits of sound business principles. The cooperative credit unions which were organized on an unlimited liability basis fell with double weight upon their members when the financial structure of the country crumbled. For more than twenty years, cooperation practically ceased in the communities where it had thrived most prodigiously. Interest in cooperative enterprises was not revived until 1889, when the German imperial law concerning industrial and provident cooperative societies was passed providing that associations might be formed with limited liability and that periodic government visitations be made to determine their competency. From 1889 to 1895 a great number of associations were formed and consolidated into provincial federations.

**In Switzerland.** The Helvetians, a pastoral people, mentioned as the first inhabitants of that mountainous region now called Switzerland, found collective effort highly advantageous to dairying in that environment. There are still in existence 223 Alpine cooperative societies that trace their origin to ancient and medieval times. Modern cooperative associations, however, were in general formed during the nineteenth century. The earliest ones purchased supplies for members; 600 societies of this type operate in Switzerland today. The Reverend Father Traber introduced the Raiffeisen system in Switzerland shortly after its introduction in Germany. The nature of the development of cooperation in Switzerland again shows the plasticity of the movement. The environment, natural resources, and the character of a people determine the manner in which collective effort will develop.

**In Italy and France.** That portion of the Alps and Jura mountain ranges extending into Italy and France makes claims to antiquity in the organization of productive societies similar to

those of Switzerland. Since the thirteenth or fourteenth centuries, Northern Italy reputedly has had cooperative dairy associations in the district of Friuli. The old cheesemakers' societies of France, known as the *fruitières*, date back to an even earlier period in history. These societies were formed to make cheeses of the Gruyère, Emmenthal, and Fromage Bleu types. Such cheeses were made into 50- to 160-pound sizes to induce proper bacterial growth for flavor, eye formation, and good keeping qualities. The large quantity of milk required for the making of the cheese necessitated assembling it from eight to twenty-five farms, a total of 100 to 250 gallons for each making.

In France, as in England, the weavers pioneered in the field of cooperation. The silk weavers of Lyons founded the Commerce Véridique in 1835. While this society lasted only three years, it adopted the principle of distributing one-fourth of the profits in proportion to purchases. The first mutual associations of nineteenth century design were those of industrial workers. The agricultural productive societies that were formed about the middle of the century owe much to the workers' associations for blazing a trail through a wilderness of economic reforms of which there were always an abundance in France. During the thirties and forties, many social reformers were pressing the cause of cooperative associations for production. Whenever associations were formed during this period, however, their existence was made precarious by an absence of legal sanction and the opposition of the established business organizations.

After the revolution of 1848, the national assembly appropriated 3 million francs for promoting the organization of cooperative producers' associations. Some members of the assembly were out of sympathy with the movement, but they willingly voted for the appropriation with the conviction that a demonstration on a large scale would prove the impracticability of cooperation in the field of industrial production and thus discredit the blatant reformers. The application of cooperative methods in credit, purchasing, insurance, and sale was not general in either France or Italy until the latter part of the nineteenth century.

**In Russia.** With the exception of the ancient patriarchal Russian artels, cooperation was late in its development in this land of peasantry. The old artels, which resembled the trade guilds of Western Europe in many respects, provided a back-



ground for their successors, the cooperative labor societies. The first agricultural cooperative loan and savings association was formed in 1866 at Dorovatovo. All the agricultural cooperative credit societies formed from 1866 to 1895 were hampered by an unsympathetic government and a benighted membership.

**In Denmark.** The seeds of cooperation fell on fertile soil when they were sown on the Scandinavian peninsulas, and in no place did they come to greater fruition than in Denmark.

The fading out of feudalism was anticipated by a Danish national policy of creating an agrarian commonwealth of independent, proprietary farmers. Accordingly, to aid the peasants in owning the land, the government established a credit institution in 1786. This institution was similar to those created in Germany during the same period, but it was lost to agriculture in 1816 by the financial and commercial crises of 1807-1820, induced by continental wars and an intense period of nationalism. In the first decade of the nineteenth century, the idea of self-help began to dawn in the minds of the peasants, and its introduction on the Holsteinborg Estate was ostensibly in the form of a savings society.

In 1852 the social-economist Frederik Dreier advocated to residents of Copenhagen a working-class benefit association for the purpose of buying fuel at cost. Between 250 and 300 residents pooled their orders and bought their supplies from the established fuel dealers on favorable terms. In 1853 this association was reformed and placed under the management of Gerhard Plang. An experiment was made in the collective purchasing of bread, butter, coffee, sugar, oil, and other household necessities, but it was short lived even though the store was patronized by a large number of workers.

The next real effort came in 1866 when the Reverend Hans Christen Sonne encouraged the workmen at Thisted, in Jutland, to form a cooperative store patterned after the Rochdale stores of England. The Thisted association is still in existence as an active business institution. It was not until after 1880 that the tidal wave of cooperation broke over Denmark. Driven by necessity to readjust agricultural production, to improve the fertility of the soil, to seek new trade outlets, and to compete with the Americans in the European markets, the peasants turned to cooperative production and sales associations as a

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means of winning and holding their place of commercial importance. The first cooperative creamery to become a model for other similar enterprises began operations in 1882 and the first bacon factory in 1887. The success of the production associations gave impetus to the consumer cooperative movement. Thus it was that Denmark attained its position of preeminence among cooperative commonwealths.

#### COOPERATION A DYNAMIC MOVEMENT

When the established order of a state or society outwears its usefulness, new institutions arise out of the chaos, and, in the absence of a constituted authority, they are most likely to assume some of the characteristics of the self-help movement. In a democratic state the movement receives a new impetus whenever the electorate is aroused to further activity and will exercise its choices through the ballot. The world has witnessed momentous changes in the rise of the trade guilds in Teutonic and Celtic Europe after the evacuation of the Romans, in the organization of the numberless social guilds during the reformation, the clandestine formation of friendly societies following the suppression and sequestration by the English crown, the emergence of cooperative credit and insurance at the disintegration of feudalism, and, finally, cooperative production and distribution on a large scale following hard on the heels of the industrial revolution. The cyclical progress of the cooperative movement can be attributed to its internal successes and to the establishment of democratic ideals in state government.

An historical study of the self-help movement in several other European countries would correspond in many respects to the developments in those countries reviewed. Cooperative enterprises have been introduced into some eastern nations so recently that they may properly be considered the offspring of the present era.

#### Questions

1. Describe some of the institutions that were organized on a cooperative basis among the Oriental peoples, the Greeks, the Romans.
2. Trace the development of associated effort in the guilds of Medieval Europe.
3. What effect did the enclosure movement have upon the economic institutions in England?

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**4. Did the explorations in the fifteenth and sixteenth centuries cause changes in the economic institutions of Europe? Explain.**

**5. Why were secret societies organized following the sequestration acts of Henry VIII?**

**6. Give reasons for the rise of the Friendly Societies. The Penny Capitalists.**

**7. Did the Equitable Pioneers of Rochdale establish the first successful business cooperative in England?**

**8. Briefly outline the achievements of the consumers wholesale movement in Great Britain.**

**9. What effect did the industrial revolution have upon the cooperative movement in Europe?**

**10. What type of cooperative organization took precedence in continental Europe? Why?**

### III

#### *Development of Cooperative Marketing in the United States*

*The general farm organizations such as the Grange, Farmers Union, Farm Bureau Federation, and the Equity have started many marketing associations and have nurtured many an association through its trying initial period. Low farm prices, wide marketing margins, and excessive freight rates were among the most direct reasons for starting associations in many parts of the country.*

*Although some associations were started shortly after 1800, no significant growth of local associations took place until the last quarter of the past century. From 1895 to 1920 a gradual expansion in numbers of associations, membership, and volume of business took place. This period was followed by a decade of rapid expansion when large-scale sales associations appeared, enabling acts were passed, propagandists were active, and federal and state divisions of cooperative marketing were organized. More than 50 per cent of all associations whose date of organization is recorded were started during the years 1914-1923.*

*More than two-thirds of all cooperative associations are located in the 12 north central states. Another region of extensive development is the Pacific Coast states where some of America's largest, oldest, and best known cooperatives are to be found. Large cotton, rice, forage crop, and citrus cooperatives are found in the south, and in the eastern part of the United States huge fluid milk marketing associations and well-known vegetable distributing organizations are operating. Cooperative auctions for the sale of eggs have become well established in recent years in eastern markets.*

*In 1935-1936, 10,500 farmers' selling and buying associations, having 3,660,000 members and transacting business valued at \$1,840,000,000, were listed with the Cooperative Division of the Farm Credit Administration. Eighty-six per cent of the business was conducted by sales associations—14 per cent by purchasing companies.*



## CHAPTER III

### DEVELOPMENT OF COOPERATIVE MARKETING IN THE UNITED STATES

Agriculture in the United States is carried on chiefly by small unit enterprises. As a result, farmers have found it advantageous to work with one another in accomplishing certain production and marketing tasks. Such informal workers' cooperative associations, as spraying, silo filling, and threshing rings, and cornhusking and barn-raising bees are examples of cooperative efforts in production. Probably in no industry is there such an expression of joint effort in solving the problems of production as in agriculture.<sup>1</sup> Certainly its counterpart is not to be found in industry where successful methods of manufacture, cost reduction, and sales technique are zealously guarded from competitors.

It has been less easy, however, for farmers to cooperate in an effort to solve marketing problems that confront them. During the middle of the nineteenth century, when agriculture expanded extensively in the United States, cooperative marketing was also attempted. The early development of cooperative marketing among the agricultural and horticultural producers in the United States will be briefly recounted.

#### GENERAL REASONS FOR COOPERATIVE ORGANIZATION

Five important developments appear to have directly influenced the associated efforts of farmers during the last half of the nineteenth century. These are:

1. Extensive expansion of agriculture west of the Alleghenies
2. Production of surplus agricultural commodities
3. Low prices of farm products

<sup>1</sup> For a good account of the kinds of cooperative marketing and purchasing associations in the United States, see Ward W. Fetrow, *Cooperative Marketing of Agricultural Products*, Farm Credit Administration, Cooperative Division, *Bul.* 3, 1936, and J. G. Knapp, and J. H. Lister, *Cooperative Purchasing of Farm Supplies*, Farm Credit Administration, Cooperative Division, *Bul.* 1, 1935.

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4. Resentment against high freight rates and wide marketing margins

5. Organizing activities of general farm organizations

Following the development of agriculture east of the Alleghenies the adventuresome farmers crossed the mountains and much to their delight came into the fertile and productive valley of the Ohio. Before long pioneers settled on the fertile lands west of the Mississippi. Obstacles in production and difficulties experienced in marketing grain and livestock are common knowledge to students of economic history. The invention of the breaking plow and the self-binder, the enactment of the Homestead Law, the severance of home ties following the Civil War, the granting of land to the soldiers of the Civil War, and the increased immigration following famines in Europe, all added to the rapid settlement of the West. An extensive production of surplus agricultural commodities followed so that although the farmers were living in a state of plenty, yet on an exchange basis they fared badly.

The tremendous surplus naturally caused prices of farm products to be exceedingly low. From 1864 until 1897, with the exception of two years, 1880 and 1892, the general price level of agricultural products was downward. This brought in its wake difficult times and hardships. During these periods of low prices, farmers found important reason for organizing to improve their unhappy circumstances.

Resentment and opposition were registered not only against low market prices, but also against high freight charges and wide marketing margins on commodities bought. Marketing margins failed to narrow with the decline of commodity prices; antagonism to the so-called "trust movement" in the country increased; the dominance of commission men and organized exchanges in the central commodity markets was looked upon with a great many misgivings; and the exorbitant rates of money-lenders simply added to the difficulties that were already being experienced. Transportation charges were reduced somewhat with the development of the Erie and Ohio canals, though the charges were still considered excessive when compared with prices received for grain and livestock products. It was because of these adverse economic conditions that the farmers, under the able leadership of Oliver Hudson Kelley, organized the Order

of the Patrons of Husbandry, commonly called "The Grange." The influence of this and other organizations upon the associated efforts of farmers constitutes the impetus for the development of cooperative marketing in this country.<sup>2</sup>

#### GENERAL FARM ORGANIZATIONS AND THE GROWTH OF COOPERATIVE MARKETING

The first organization to definitely stimulate collective purchasing of farm supplies and selling of farm products was the Grange. The Grange was organized in 1867, and during the period from 1870 to 1876, it exercised the greatest influence upon associated activities in American agriculture. Among numerous contributions to American agriculture made by the Grange, two stand out prominently: (1) its effectiveness in narrowing retail margins in stores that were supplying farm products, and (2) its legislation affecting the railroads of this country. The general antagonism of the Grangers toward the high marketing charges exacted on commodities purchased caused the development of mail-order houses and local cooperative stores, and these, in turn, forced many local retailers to adopt more efficient methods in the operation of their individual stores. Certainly this had a salutary effect upon the merchandising practices of the day.

The hostility toward high freight rates led the Grangers to press the passage of so-called "Granger legislation" in several states of the Union. The passage of the Potter Act<sup>3</sup> in Wisconsin typified the extreme nature of their demands. Such legislation was responsible for the creation of the Interstate Commerce Commission in 1887. The Grange was engaged in practically every type of marketing activity and, in no small measure, in the manufacture of farm and home machinery and utensils. State purchasing agencies were set up to handle farm commodities; stores were established in many communities; and cooperative selling of many types of farm products became the

<sup>2</sup> For an excellent short description and philosophical treatment of the general farm organization movement see B. H. Hibbard, "Marketing Agricultural Products," Part II, pp. 183-269, D. Appleton-Century Company, Inc., New York, 1921.

<sup>3</sup> Passed in 1874. The act classified the railroads of the state, fixed passenger rates for the different classes of roads, classified freight and fixed tariffs for the same, created a three-man railroad commission, and vested the commission with sweeping powers.

common activities of the organization. In the activities of this organization, we find the roots of much of the development of the cooperative marketing movement of this country.

Another organization which left its imprint upon the marketing activities of the day was the Farmers' Alliance, which had a forerunner in Kansas in 1872 and was organized in Texas around 1875. Although short lived, this organization during 10 years of its most active existence placed a great deal of emphasis upon cooperative activities. Through its influence were organized the Florida Fruit Exchange in 1885, and the Texas Farmers' Alliance Exchange in 1887 which at first handled cotton, grain, and farm implements but later general household supplies. In numerous communities of the Southwest attempts were made to improve the marketing of wool, cotton, and grain. Perhaps the first attempt to sell cotton on a quality basis can be accredited to the Alliance. State sales agents were hired to sell cotton for local alliances.

The next influence in the development of the cooperative movement was the Farmers' Educational and Cooperative Union, which was organized in Texas in 1902. This organization always has emphasized the economic activities of its members. As in those that preceded it, major emphasis was not placed on improving the production of farm products, but rather on obtaining better prices and improving marketing services for grain, cotton, livestock, and other products. It also considered the social and educational problems of its members, and these, as history has shown, are second only to economic considerations. The Farmers' Union became widespread throughout the United States, particularly in the extensive area, south, and west of the Mississippi River. During its life, it has continually stressed the organization of local associations, and in later years, the organization of federated and centralized regional associations. Many livestock shipping associations and cotton marketing associations owe their existence to the activities of this general farm organization. In order to influence prices, in 1904 the Texas Union urged its members to withhold their cotton from the market until a minimum of 10 cents per pound was obtained, and in 1907 and 1908 an acreage reduction program was vigorously advocated. The Union established the first cooperative livestock commission firm in 1917.



The American Society of Equity (1902) was primarily instrumental in developing cooperative marketing organizations in the north central part of the United States. It became influential in organizing many livestock shipping associations in the state of Wisconsin. Cooperative elevators, cooperative stores, and also cooperative terminal elevators have been organized by the Equity. Cooperative packing plants were advocated and started in several communities in Wisconsin, Minnesota, and the Dakotas during the years 1914-1917.

The American Farm Bureau Federation placed the major part of its interests upon the development of farmers' cooperative marketing associations. Appearing at a time when many local cooperative associations were in existence, the organization concentrated its activities on the federation of locals. Its operations during the period 1920-1925 constitute an interesting period in the development of the federated type of association in this country. Grain, livestock, and wool are a few of the commodities which received greatest consideration by this organization.

Other farm organizations have also contributed to the development of cooperative marketing: The Non-Partisan League of North Dakota, primarily a political organization, nevertheless, was instrumental in getting farmers to work collectively in the solution of their problems; The Agricultural Wheel and the Brothers of Freedom and other organizations of less historical importance have been influential in this general movement.

#### HISTORY OF SPECIFIC COMMODITY ORGANIZATIONS

**Dairy.** Just when the first cooperative dairy-marketing organization was established in this country is surely a matter of conjecture. Associations that might be called cooperative were started shortly after the turn of the nineteenth century. Although these companies may not properly qualify as cooperatives, judged by present-day tests, nevertheless the spirit and practical operation of the companies made them distinctly cooperative in character. It is reported that a creamery was built at Goshen, Conn., in 1810. In 1841 Wisconsin farmers around Rock Lake, Jefferson County, made their cheese collectively at the home of Mr. Pickett, and in 1851 the so-called "American system" of associated manufacture of cheese was evolved at Rome, New York. In 1856 a butter factory was established at Campbell

Hall, Orange County, N. Y. The early cheese rings in Massachusetts, dating back to 1835, were cooperative and quite typical of the cheese rings of the Jura Mountains of Europe, where the Swiss and French peasants made their well-known cheeses collectively. For many years the local cooperative cheese factories and creameries were the only types of organization in the dairy industry, but in 1913 representatives of cheese factories in Sheboygan Co., Wisconsin, organized the first federation of cheese factories. The organization of county creamery associations (1917-1920) in northwestern Wisconsin and in Minnesota, later federated into an interstate unit (1921), preceded the Land O'Lakes Creameries, Inc., which was formed in 1924. On the Pacific Coast are some of America's largest cooperative creameries, and since 1911, a federated sales association has been in operation there. Today five large federated sales associations sell about one-fifth of the creamery butter of the United States. The physical characteristics of milk and the small production on the individual farms encouraged collective action of many farmers. It took more milk than one farmer produced to make Swiss cheese of the wheel or drum style. To obtain standardized quality, uniformity of grade, and large quantities of dairy products required cooperative action. A feature of the cooperative movement among the dairymen was the promotional effort that was made by manufacturers of creamery equipment to interest the farmers in cooperative associations. From 1897 to 1905, following a period of intensive promotion, more than 800 creameries and skimming stations were forced to close in the West North Central states. Uneconomical operations had spelled their doom.

Among the producers of fluid milk for city consumption purposes are three main types of cooperative effort. (1) Cooperative retail distribution which started around 1882. This was primarily carried on by farmers adjacent to small cities who wished to sell their milk directly to consumers. In recent years, however, cooperative milk-distributing companies with relatively limited memberships are also operating in large cities such as Cincinnati, Milwaukee, and Oklahoma City. (2) Cooperative wholesale distribution of milk which started about 1899. (3) Collective bargaining between farmers and private distributors which began about 1909. The latter are of two types

(a) those that merely bargain for a price, check weights and tests, and (b) those that in addition to these services also operate processing plants where "surplus" milk is converted into butter, cheese, evaporated milk, or other manufactured dairy products. In more recent years collective bargaining groups were organized by patrons of condenseries and in some localities cooperative condensing plants and flexible processing plants were constructed. Today cooperatives exist for every phase of milk marketing (including its related products).

**Livestock.** The cooperative marketing of livestock dates back to the Colonial period. In the latter part of the eighteenth century, around 1785, a number of agricultural societies were formed for the purpose of improving agriculture in the colonies. The membership was composed of the gentlemen farmers and so-called "dirt farmers" of the day. The Philadelphia society for promoting agriculture, which was organized in 1785, imported breeding stock into this country, and in one sense, this may be considered the beginning of cooperative buying and selling of livestock. As early as 1820, a sporadic venture in cooperative selling started in a small way near Granville, Ohio. Beginning in 1872, the Grange dealt with cooperative livestock marketing, and during the eighties, the Farmers' Alliance in Kansas and Nebraska was especially active in selling stock collectively. Perhaps one of the best known of the early livestock associations was the Goodlettsville Lamb and Wool Club of Goodlettsville, Tenn., which started the practice of selling lambs and wool on a cooperative basis as early as 1877.

The farmers' livestock shipping association at Superior, Neb., which started in 1883, is commonly considered the first association of the more strictly cooperative type. The next association began operations in Iowa in 1904, and for the next few years up to 1910, a number of associations were started in the livestock producing sections of this country. Much of this early movement in the north central states was under the leadership of the American Society of Equity. About 1917, and continuing for the next eight years, the organization of local livestock shipping associations underwent a very rapid expansion, so that by 1925 between 3,000 and 4,000 livestock shipping associations were in operation. In 1889 the first cooperative livestock commission firms were organized on four public markets, but these, as well

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as the one which was begun in 1906, were short lived due to the severe opposition by established private commission firms and the livestock exchanges. Following the successful operation of a firm on the Omaha market in 1917, other associations were organized on every one of the leading terminal livestock markets of the country. Under the leadership of the Federal Farm Board in 1930, the majority of the cooperative commission firms were brought together under the National Livestock Marketing Association. The Farmers Educational and Cooperative Union and the American Farm Bureau Federation were responsible for the organization of about two dozen cooperative commission firms which are still operating on a large scale. Largely since 1930, cooperative truck shipping associations have made their appearances in local communities.

In reviewing the history of cooperative livestock marketing one is impressed with: (1) the sporadic character of organization. Many associations were short lived and showed a lack of continuity of operations. (2) The movement is conspicuous by its many failures during the early years of organization. (3) A relatively long period elapsed between the early associations and the general expansion which took place after 1917. (4) The local shipping associations were performing primarily a shipping service with very little expert selling service involved. (5) Thousands of local associations were started principally in protest to low prices and wide local-dealer margins. (6) The cooperative movement received its greatest support among the small producers of livestock in the middle west and not until the second decade of the twentieth century did the cattlemen and sheepmen of the ranches become interested in cooperative activity. (7) Not until after 1917 did the cooperative commission firms appear on all of the leading terminal markets. (8) After 1930 the number of local rail-shipping associations decreased about 80 per cent from the peak period in 1925 as a result of consolidations, the expansion of truck shipping, establishment of interior packing plants and concentration yards. (9) Cooperative truck-shipping associations are operating in proximity to the large terminal markets.

**Grain.** A cooperative movement that is filled with many thrilling experiences is that of the grain producers. General dissatisfaction with price policies of independent and line eleva-

tors, objections to the grading and docking practices, and general criticism of excessive railway freight charges impelled the farmers throughout the grain producing regions to organize their own cooperative elevators. The first cooperative elevator was established in a region which no longer produces grain in sizable quantities. That was at Madison, Wisconsin, in 1857. Here the farmers organized an association as a protest to the excessive freight rates which were being charged for the transportation of grain from Madison to Milwaukee. In Iowa an elevator was built in 1867, and around 1872, the Grange took an active part in organizing elevators in Iowa, Minnesota, and the general Northwest.

As one looks into the history of cooperative marketing by the grain producers, certain types of organization stand out prominently.<sup>4</sup> The *first* is the local cooperative elevator. The first elevators operated only a relatively short time, and with the downfall of the Grange beginning in 1876, many local elevators ceased their operations. For the past several decades, however, several thousand farmer-owned cooperative elevators have been in existence. The *second* is the cooperative line elevators which were started as early as 1903 to meet the competition of the independent line elevators in certain counties of Kansas and Oklahoma. *Third*, the cooperative terminal sales agencies which were essentially commission firms handling grain for local elevators on a commission basis in the terminal markets. The first of these was organized in 1911. *Fourth*, wheat pools which were of a regional character, usually involving the area of a single state. These pools were formed with the hopeful objective of obtaining a monopoly control of wheat and thus exercise a dominant influence over price. The first of these was organized

<sup>4</sup> FETROW states, *op. cit.*, p. 45, the following: "The development of cooperative grain marketing in the United States may be divided logically into the following periods: 1857-1875, a time of isolated local efforts; 1876-1885, a period of decline in number of local cooperative elevators; 1886-1914, years marked by a revival of interest in this form of cooperation and an increase in the number of cooperative grain elevators; 1915-1920, the period of most active growth of farmers' cooperative elevators, under the additional stimulus of a rapidly expanding wheat acreage; 1921-1929, the time of most rapid growth in cooperative terminal sales agencies, development of wheat pools, and efforts toward establishing a national sales agency. Since 1929 a national sales agency has been in operation, and there has been a revival of interest in the stability of local cooperative elevators."

in 1919, and in 1924–1925 when ten pools were in operation the peak of this activity was reached. The pool movement ceased in 1930. *Fifth*, a national sales agency, which attempted to sell the wheat for many state organizations, was begun in 1920 by the American Farm Bureau Federation. Although a national sales agency, as was typified by the United Grain Growers, Inc., was shortlived, it became a precedent for another organization, national in scope which was incorporated in 1929 as a result of the Federal Farm Board's organizing activities. It was called the Farmers' National Grain Corporation with headquarters in Chicago and is the selling agency for a score of regional grain marketing companies.

Another characteristic of the grain movement is the interest which each one of the general farm organizations had in it. The Grange was primarily interested in local elevators; the Farmers' Alliance had some connection with the cooperative line elevators; the Equity was responsible for the organization of the cooperative terminal sales agency at St. Paul; the Farmers Union started many wheat pools; and the American Farm Bureau Federation sponsored a national cooperative sales association.

**Fruits and Vegetables.** Practically every student of marketing has heard of the success of cooperative marketing among the citrus fruit growers of California. This state is noted for the success of the marketing activities not only of its citrus fruit producers but of many deciduous fruit and vegetable producers as well. However, not only California has been a fertile ground for the development of cooperatives in fruit and vegetable marketing, but other states have many associations to which they can point with pride in this field. The Fruit Growers Union, a cooperative system which was started in 1867 at Hammonton, N. J., is perhaps the first cooperative fruit marketing organization in this country. After a rather checkered career for 30 years it failed. Cranberry growers organized in New Jersey as early as 1872, in Massachusetts in 1895, and in Wisconsin in 1906–1907. The peach growers along Lake Erie organized in 1878, followed by their fellow growers in Delaware in 1881. On the west coast the first organization among the fruit producers was started in 1881. Throughout the entire United States one type or another of fruit and vegetable marketing associations was organized during the period 1875–1900.

In a manner similar to that of other cooperative organizers, the fruit and vegetable growers began with their local associations and later developed federations for centralized selling. The organization of regional citrus and deciduous fruit associations in California, of apple marketing companies in Oregon and Washington, of potato marketing cooperatives in Colorado, Virginia, Florida, Kansas, and Maine, of cranberry sales companies in Wisconsin, New Jersey, and Massachusetts, and of vegetable marketing associations in various parts of the country indicates the diversity of the movement. In some markets, cooperative commission firms were established to handle fruit on the commission basis for either cooperative or noncooperative country shippers. At this time, 1937, some singular successes of cooperative marketing are found among the federated fruit and vegetable associations.

A review of the history of the development of cooperative marketing among the fruit and vegetable producers reveals (1) the large number of associations which were organized throughout the entire country and their subsequent suspension of operations. Reorganization or new organizations followed one after another. (2) The cooperatives were largely ventures in packing, grading, and shipping of fruit, with very little emphasis upon cooperative selling in the central markets, until the beginning of the twentieth century. (3) This type of cooperative organization is perhaps the most widely distributed of all cooperatives; practically every state in the Union has some kind of fruit and vegetable organization. (4) A relatively small number of horticultural and vegetable producers of the United States are included in the organizations—exceptions, however, are found in certain commercial areas. The total membership is not very large, and the total number of associations is not very great within any one state, as may be found, for instance, in the dairy sections where thousands of creameries and cheese factories are located, or in the grain producing regions where thousands of farmers' elevators function. In 1935-1936, 1,063 fruit and vegetable associations with 166,000 members (4.5 per cent of all memberships in United States cooperatives) and transacting 212 million dollars worth of business reported to the Farm Credit Administration. These may be contrasted with 2,270 dairy associations, having 720,000 members (19.7

per cent of total memberships) and having a business of 520 million dollars, or with 3,010 grain marketing associations, having 610,000 members (16.7 per cent of total memberships) and transacting business amounting to 360 million dollars. (5) In many localities the organizations were started when bankruptcy faced the producers. This was particularly true among the citrus growers in California, where the problem of disposing of enormous crops confronted the producers before markets were properly developed. (6) Of all agencies handling fruits and vegetables the cooperatives have been among the most important in establishing definite grades and standards as well as uniform packs. (7) A relatively small amount of cooperative canning of fruits and vegetables is carried on. Cooperative drying of fruits, such as prunes, apricots, and raisins, is however being successfully accomplished by nationally known cooperatives on the West Coast.

**Poultry and Eggs.** Perhaps the first effort of poultrymen to market their eggs and poultry collectively occurred in 1874 when a poultry and produce exchange was started in Chicago by the Illinois State Grange. Other cooperative egg marketing associations were started in California in 1901, in New Jersey in 1905, in New York and Minnesota in 1908, and in Wisconsin in 1910.

Two factors respecting poultry production have had a bearing upon the type and extensiveness of cooperative organization in this industry: (1) the type of poultry production, *i.e.*, whether it consists of merely farm flocks that are side lines to other farming operations or of commercial flocks of thousands of hens; (2) the location of production with respect to the markets for eggs and poultry.

In the Middle West, where most poultry production consists of farm flocks of less than 200 hens, the cooperative handling of eggs has not been extensive. Here eggs are ordinarily received at local cooperative creameries and sold by the creamery directly, or through a central butter-marketing cooperative with an egg and poultry sales department. Egg circles were also started in this region after 1913, but they were not so popular here as in Missouri, Mississippi, Arkansas, New Mexico, and Tennessee. These egg circles, local in scope, concentrated chiefly on the assembly, grading, and packing of eggs and, as a result of their



volume, were able to attract a small premium in price over individual sales prices.

Some of America's finest cooperative associations are found among the large commercial egg producers on the Pacific Coast. Here as early as 1905 commercial egg producers associated to sell their eggs. Today associations of this area not only handle eggs and poultry amounting to millions of dollars, but also purchase feed and supplies on a huge scale. Modern packing plants, feeding stations, and efficient sales organizations have been set up to give the poultrymen the highest class of service possible. Since a large share of the eggs from this surplus producing region is sold in eastern markets, five of the state associations organized in 1922 a central sales agency, the Pacific Egg Producers Cooperative, Inc., with headquarters in New York City. Sales of the latter organization exceeded 10 million dollars in 1934.

In the eastern states where many producers are adjacent to the large consuming markets and where many specialized sales outlets have been developed, cooperation has not progressed very far. Some of the large cooperative farm purchasing associations sell eggs as a side line and, since 1930, nearly two dozen local cooperative associations selling eggs and some poultry on an auction basis have been operating.

Wool. In the history of cooperative wool marketing the Grange again played an important role. As early as 1874 the Granges in Michigan, Ohio, and Kentucky sold wool from their warehouses directly to the mills. It was already mentioned that in June 1877 the Goodlettsville Lamb and Wool Club in Tenn. pooled the wool and sold it by grade. Another local pool which operated for several decades began functioning in 1901 at Greencastle, Ind. Others were started in 1905 in Missouri and in Indiana. History records that a wool auction was conducted by farmers in Utah as early as 1885. Following the organization of local associations, regional and state-wide wool marketing companies were set up. From 1909 to 1924 the National Wool Warehouse and Storage Company, with warehouse and headquarters in Chicago, was the first cooperative regional sales association to sell wool for local pools and individual consignors. The Ohio Wool Growers Association, which was organized in 1918, is a conspicuous example of another large-

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scale selling organization. This association was reorganized in 1924 and is still operating. In 1921 a large-scale sales association was established on the Pacific Coast. Many of the regional wool pools are still in operation, and following the activities of the Federal Farm Board in 1929, the National Wool Marketing Corporation was set up. More than two dozen regional and state-wide wool pools are in operation and practically all of them sell their wool through the national sales association which has headquarters in Boston.

**Cotton.** In the early efforts of cooperative marketing of cotton, the influence of the general farm organizations is again found.<sup>5</sup> As early as 1872 the Grange attempted to market cotton cooperatively. The Alabama, Mississippi, and Georgia Granges took an active part as early as 1875. They not only baled cotton in leased warehouses but they also financed shipments, performed the grading, and transacted sales. Although these operations extended only over a short period of time, they were again resumed when the Farmers' Alliance took an active interest in cotton ginning and marketing in Texas in the early eighties. This association recommended pooling the members' cotton and selling direct to the cotton mills. The Farmers Union as early as 1906 campaigned for better cotton prices and included in its plans such goals as the restriction of production, establishment of cooperative warehouses, withholding of cotton, and fixing of minimum prices. But not until 1921 do we find a rapid expansion in cooperative cotton marketing including the establishment of cooperative gins, cottonseed-oil mills, and state marketing associations. Fired by the enthusiasm with which they were imbued by eloquent orators and stimulated by the discouragingly low price of cotton following the World War, cotton farmers of the South organized huge regional cooperatives of the centralized type during the period 1921 to 1923. No less than fifteen state-wide or regional organizations were started during this period. The cotton cooperatives later organized into federated sales organizations, of which the American Cotton Cooperative Association is an example.

<sup>5</sup> For a good treatment of the history of cooperative cotton marketing see O. W. Herrmann, and Chastina Gardner, *Early Developments in Cooperative Cotton Marketing*, Farm Credit Administration, Cooperative Division, *Circ. C-101*, 1936.

Some of the outstanding features of cooperative cotton marketing associations are: (1) Almost all of the efforts of the organized cotton producers during the early seventies, eighties, and nineties and during 1921 to 1925 were directed to control prices through monopoly influence. (2) All of the early general farm organizations in the South had a part in collective cotton marketing. (3) Centralized types of associations were started during 1921-1923 in most of the cotton states as a result of intensive promotional campaigns. (4) Long-term marketing contracts became an essential part of the plan of organization during the twenties. (5) The establishment of cooperative cotton gins and cooperative cottonseed-oil mills was a further step in the development. (6) Federation of a number of state associations into one central sales organization was effected. (7) During the past decade, important changes in the method of handling cotton were made as a result of liberalizing the contracts, offering optional pooling arrangements, and establishing interior classing offices. Today, there is little mention made of monopoly control of cotton markets and fixing of prices, but in its place service to producers and efficient marketing are stressed.

**Tobacco.** Reports indicate that attempts were made in 1862 by Connecticut farmers to market tobacco cooperatively. Local efforts to improve tobacco marketing inspired by the Grange and Society of Equity predominated until 1920 after which state-wide tobacco pools with memberships running as high as 100,000 were organized in all of the principal tobacco producing sections. These large pools of the postwar period were organized as highly centralized associations. Rigid 5-year nonrevokable contracts under which all tobacco was pooled on an annual basis were the hubs around which these giant organizations revolved. Of the seven large associations operating in 1925, only the two smallest ones were still running in 1935. Speed in organization was emphasized over permanency. Mismanagement, growers' discontent, opposition from the outside, unfavorable price comparisons, delays in making final settlements, and failure to achieve monopoly control over prices which promoters had assured producers were some of the causes of wholesale contract violations and dismal failure of the five largest associations. During the depression years of the thirties, attempts were again made to establish central sales associations

in South Carolina, Virginia, Kentucky, and Tennessee, but thus far none of them have been outstanding successes. Under the new organization plans producers have some options respecting their sales, namely, tobacco may be sold in the sheds, at auction, or on a pool basis. Likewise, the hope of monopoly control of tobacco markets has given way to a more sane ambition of rendering efficient marketing service.

**Other Commodities.** Forty-one years ago California walnut growers established local associations to grade, pack, and sell their crops through brokers. United effort of these early locals was attempted in 1905, but not until 1912 did a successful federation become a reality. Today, this same federation, the California Walnut Growers Association, handles in excess of 85 per cent of the state's walnut crop and with its "Diamond" brand walnuts has achieved a fine national reputation.

The almond growers also began cooperating in local associations as early as 1897, and in 1910 a federation of locals was organized in order that a better sales system might be established. This federation is a going concern today, marketing approximately one-fourth of the state's almond crop.

Rice growers in Louisiana, California, and Arkansas organized their present associations in 1921 as nonstock, centralized types of associations. Earlier attempts had been made in Louisiana in 1911 and in California in 1915, but these ventures were not permanently successful. From one-fourth to one-third of America's rice crop is now handled cooperatively by three associations.

Interesting historical accounts could be given of the formation of cooperative associations among producers of hay, beans, seeds, wine grapes, peanuts, honey, pecans, maple sirup, ginseng, fox furs, sugar beets and sugar cane, soybeans, cut flowers and bulbs, avocados, cherries, strawberries, and bush fruits. The producers of these products experienced in varying degrees the same conditions which led to the organization of associations treated in this chapter, namely, dissatisfaction with prices received, operating margins exacted, and services given. Purchasing associations were encouraged by the additional factors of high prices and inferior quality of the supplies being bought. Varying degrees of success and failure have marked the experiences of associations handling these specialty products.

## REGIONAL DEVELOPMENT

Cooperative marketing has not developed to the same extent in all of the states of the Union, or for all types of agricultural commodities (see Figs. 2, 3). The 12 north central states lying east and west of the Mississippi River are the center of this development. Here, a few years ago, 70 per cent of all cooperative associations were located. These included the thousands of cooperative dairy marketing associations, thousands of cooperative livestock shipping associations, approximately 3,000 farmer elevators, and hundreds of cooperative fruit and vegetable, poultry and egg, tobacco, ginseng, and other miscellaneous farmers' organizations. In this area cooperation has constantly grown from the small local associations to some of the most outstanding federated and centralized associations to be found in this country.<sup>6</sup> It is not implied in these statements that farmers in this area have not also met with adversity in their organization and that failures are not to be found, but the movement has progressed and the spirit of cooperation has thrived in this territory.

On the West Coast, along the Pacific waters, the large citrus marketing organizations are of both national and international importance. The California Fruit Growers Exchange, the California Fruit Exchange, the Mutual Orange Distributors, the Wenatchee-Okanogan Cooperative Federation, the Yakima Fruit Growers Association, the Challenge Cream and Butter Association, the Tillamook County Creamery Association, Pacific States Livestock Marketing Association, the Washington Cooperative Egg and Poultry Association, Pacific Wool Growers, and the Poultrymen's Cooperative Association of Southern California are merely a few of the renowned associations that dot the western coast. Cooperation has made a singular success among the producers of the commodities handled by these and other associations located here.

<sup>6</sup> Some of the central marketing organizations in this area are the Land O'Lakes Creameries, Inc., Central Cooperative Association, Twin City Milk Producers Association, Wisconsin Cranberry Sales Association (member of American Cranberry Exchange), Farmers National Grain Corporation, American National Fox and Fur Breeders Association, Wisconsin Cooperative Wool Growers Association, Equity Cooperative Livestock Sales Association, Chicago Producers Commission Association.

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In the eastern part of the country, cooperation among fruit producers, poultrymen, and dairymen is to be found. The

**BUSINESS OF FARMERS' COOPERATIVES**  
BY GEOGRAPHICAL AREAS

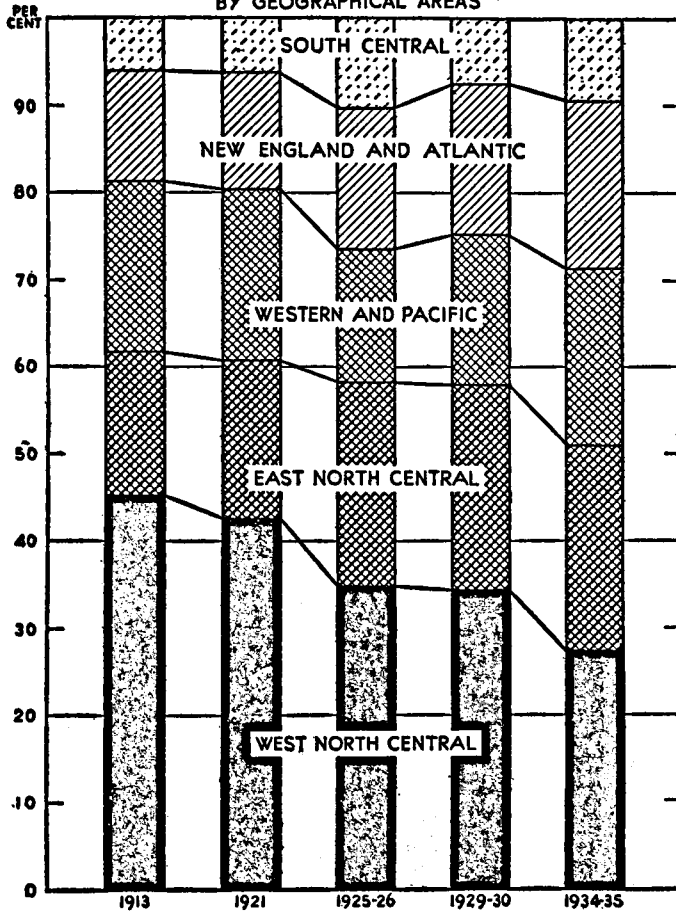


FIG. 2.

Source: Elsworth, R. H., "Statistics of Farmers' Cooperative Business Organisations 1920-1935." Farm Credit Administration, Bul. No. 6, Figure 7, p. 14. Washington, D. C. 1936.

associations are not usually so large as those in the central part of the country, although exceptions are to be found in some of

the very large cooperative milk marketing associations, of which the Dairymen's League Cooperative Association is an example.

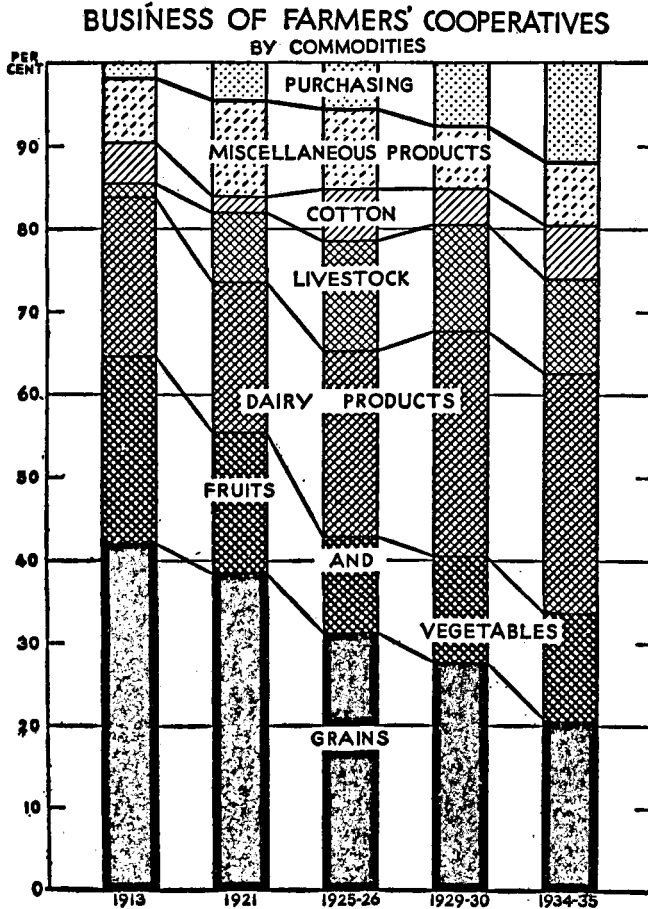


FIG. 3.  
Source: Elsworth, R. H., "Statistics of Farmers' Cooperative Business Organizations, 1920-1935." Farm Credit Administration, Bul. No. 6, Figure 8, p. 15. Washington, D. C. 1936.

Cooperative purchasing associations, however, are more important here than in other parts of the country. Such associations

as the Cooperative Grange-League Federation Exchange (G.L.F.) of New York and the Eastern States Farmers Exchange of Massachusetts are nationally known.

In the South, cooperation has not developed to nearly so great an extent as in the North. Notwithstanding, some successes are found among the fruit and cotton producers, and rice growers. But considering membership and total volume of business transacted cooperation has not made so much headway here as in other sections of the country.

It is true that one or more types of cooperative organizations from the local to the highly extensive national organizations are to be found in nearly all states of the Union, and the development on the regional basis indicates somewhat the spirit with which the problem has been mutually attacked by the growers. Table II indicates the geographical importance of farmers' cooperative effort and the amount of business carried on cooperatively for various commodities in 1935-1936.

#### PERIODS OF COOPERATIVE DEVELOPMENT

If one examines the types of organizations that have been developed in this country, the movement logically divides itself into the following periods: (1) period of local associations; (2) period of federated and centralized associations; and (3) period of national cooperative marketing associations. But rather than to analyze the development on the basis of the types of associations, it will be found more instructive to inquire into the various periods of activity. Analyzed in this fashion, we find that there are six definite periods to be considered.

1. The period of experimentation preceding 1870. During this period a number of cooperative dairy establishments were started, and as indicated above, a number of fruit, cotton, livestock, and wool marketing associations commenced. Although not organized according to the Rochdale plan, the spirit and the effect of the organization were cooperative. At best the associations were primarily local in scope and their activity was usually short lived. Exceptions in the state agents that sold cotton for local Granges should be mentioned.

2. The period of Granger activity 1870-1880. The Grange was responsible for the organization of hundreds of cooperative associations in many states of the Union. During the years

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1870-1875, the Grange was particularly active in organizing and operating sales associations. But after 1876, a decline in the Grange was followed by a sharp decline both in the number and in the importance of the associations which it had established. This period will always be looked upon as one of great activity among the farmers of this country in their early marketing ventures. Even though replete with dismal failures, this period had its favorable effect upon the agricultural life of the nation.

3. Period of inactivity. From 1880-1895 there were relatively few farmers' associations started and attempts were sporadic in character and took place in many isolated villages and hamlets of this country. This statement is not to suggest that there was no organization whatsoever during this period, but in comparison with the number of associations that came into existence in the following decades, this period is one conspicuous by its absence of activity. In all likelihood the waning activity of the Grange contributed to this condition. Mention should be made, however, of the activity of the Farmers' Alliance during this decade in the state of Texas among the cotton and grain producers.

4. Period of gradual expansion, 1895-1920. According to the reports received by the United States Department of Agriculture showing the dates of organization of thousands of cooperative associations, it is evident that during this 25-year period associations developed rather slowly throughout the entire United States. It was during this period that the greater number of livestock shipping associations and grain elevators became organized. There was in these years a gradual increase in the number of cooperative creameries and cheese factories and fruit and vegetable associations. The promotion activities among creameries took place at this time, and the disastrous experiences of farmers' cooperative meat packing plants also occurred during the latter part of this era. Perhaps it is no exaggeration to state that cooperative associations for every important type of commodity came into existence during this quarter-century period. Up until 1920 local associations were the predominant type of cooperative organizations.

5. Period of rapid expansion, 1920-1930. This decade is marked by the immediate and the secondary postwar depression periods in agriculture and industry. During this time coopera-

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tive marketing received greater emphasis than at any time. Never before had the subject of cooperative marketing received such widespread attention from farm leaders, educators, lawmakers, the courts, politicians, and citizens in general. During this period the Capper-Volstead Act, most state cooperative marketing acts, the act creating the Division of Cooperative Marketing (1926), and the Agricultural Marketing Act (1929) were passed. During the close of this period the Federal Farm

PEAK TEN-YEAR PERIODS FOR ORGANIZING FARMERS' BUSINESS ASSOCIATIONS.

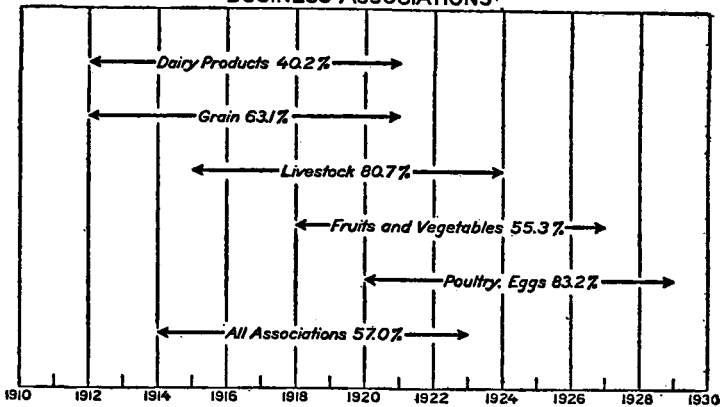


FIG. 4.

Source: "Statistics of Farmers' Selling and Buying Associations, United States, 1863-1931." Federal Farm Board, Bul. No. 9, Figure 2, p. 4. Washington, D. C. 1932.

Board was exceedingly active. The courts took a distinctly more liberal attitude toward the organization and operation of farmers' associations. Governmental and businessmen's commissions investigated the circumstances of farmers and recommended the organization of cooperative marketing associations as a means of alleviating depressive conditions.

Following 1921, hundreds of associations were organized every year—not only locals but the regional, federated, and centralized ones—and during the later years, commencing in 1930, associations that were national in character were set up. It was during this period that the highly centralized types of associations with their influence upon the central markets became prominent, and it was also during this time that the most organized opposi-

tion to the cooperative movement became active. The numbers of associations increased so that at the end of the period between 15,000 and 20,000 cooperative companies dotted the land. More than 200 centralized, federated, and terminal sales agencies were in existence. It is estimated that 3 million farmers belonged to the various companies, and during 1929 as much as 2½ billion dollars of farm business was conducted by the associations. Truly, it was a period of most rapid expansion and one of extensive operation. Individual companies handled as much as 60 million dollars of business in a single year (see Fig. 5).<sup>7</sup>

6. Period of adjustment and readjustment, 1930—. The depression of the thirties, or the secondary postwar depression, as it is sometimes called, is characterized by the numerous adjustments which many of the associations that were developed in the preceding decade had to make. With the very sharp decline in farm prices, numerous cooperative associations were forced to sell inventory stocks for less than the loans which were made upon them. Others experienced difficulties of a different character. During this period the effects of motor truck transportation were keenly felt by livestock shipping associations and by fruit and vegetable marketing associations that were organized primarily for using rail shipping service. In the livestock field, the development of interior packing plants

<sup>7</sup> "The Cooperative Division of the Farm Credit Administration has record of the organization dates of 16,178 cooperative marketing associations formed prior to 1932. About 50 per cent of these are still in operation. Of the associations for which the date of organization is known, about 6 per cent were organized prior to 1900; 20 per cent prior to 1910; 62 per cent prior to 1920; and 89 per cent prior to 1925. The 10 year period of greatest organization activity was 1914 to 1923, during which more than 50 per cent of all recorded marketing associations were formed. The peak for a single year was reached in 1920, when 1,779 associations were set up. The period during which the height of organization activity was reached differs somewhat for the several commodity groups. The most active period for organization of associations to market dairy products and grain was during the 10 years 1912-1921, inclusive. Forty per cent of all associations for handling dairy products and 63 per cent of all grain marketing associations were organized during that period. About 81 per cent of all livestock marketing associations were formed during the period 1915-1924. Many of these were local shipping associations. Fifty-five per cent of all fruit and vegetable marketing associations were organized during the period 1918-1927. Of associations for marketing poultry and eggs, 83 per cent were organized from 1920-1929." Fetrow, *op. cit.*, p. 2.

and concentration yards also had a telling effect upon the local shipping associations that had been consigning stock by rail to terminal markets. During this period of adjustment to lower costs of operation, many associations found it necessary to restrict or consolidate their expanded activities of the earlier decade and thus perfect economies in operation within their

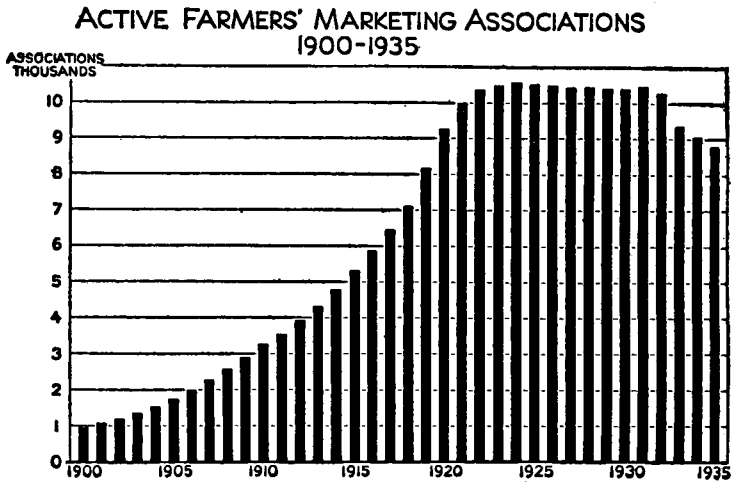


FIG. 5.

Source: Elsworth, R. H., "Statistics of Farmers' Cooperative Business Organizations, 1920-1935." Farm Credit Administration, Bul. No. 6, Figure 6, p. 12. Washington, D. C. 1936.

individual companies. In the marketing of cheese, for example, the number of cooperative warehouses of one company was reduced from sixteen to five.

At this time, also, the new political administration at Washington placed less emphasis upon cooperative marketing associations than did the outgoing administration. All in all, this period marked a gradual decline in the number of associations and their memberships (see Fig. 5). Quite naturally, as a result of the sharp reduction in the value of farm products the gross business of the companies in 1932 decreased from  $2\frac{1}{2}$  billion dollars in 1929 to approximately  $1\frac{1}{2}$  billion dollars. At this time details of organization were modified and operating practices were most carefully scrutinized in order that economies could be effected. There is a probability that this era will be marked by

an increasing efficiency in the operation of the remaining associations.

#### COOPERATIVE PURCHASING AND SERVICE ASSOCIATIONS

Cooperative purchasing of farm and household supplies dates back to the days of the Granger movement in the seventies. Local Granges bought feeds, seeds, fertilizer, flour, salt, sugar, and other products in carload lots on the basis of pooled orders of their members. The goods were distributed from the car door. Such arrangements entailed no overhead expense for warehouses, office force, manager's salary, and other items of cost incident to operating a local supply store. The savings consisted chiefly of the difference in price between carload lot quotations and local retail prices (less freight and minor handling expenses). However, much grief for local officers of the Grange accompanied such ventures; some farmers failed to call for the products previously ordered; some lacked cash for payment; the party supervising the unloading had to stand losses resulting from spilling, torn sacks or errors in counting; and many farmers were reluctant to pay for their orders when local retail prices had dropped below the car door prices. Most of those in charge became discouraged. A number of states established state purchasing agents to effect better purchases than the local groups could arrange.

Other farm organizations to this day sponsor local group buying. The Alliance, Farmers Union, Farm Bureau Federation, and the Equity locals engaged in this rather informal type of business. It is evident that the benefits were distinctly limited and that no significant impression could be made on the general level of prices which a formal large-scale association could achieve.

Today purchasing of farm supplies is carried on by three different groups: (1) informal groups, such as described above; (2) farmers' sales associations; and (3) regularly established purchasing agencies that are local or regional in scope. The informal groups still pool their orders and obtain their supplies from wholesale dealers, brokers, mills, or cooperative wholesale organizations. Farmers still get their supplies direct at the car door. Many local marketing groups—creameries, cheese factories, and packing houses—buy supplies and carry them in stock for their

## 72 EVOLUTION OF COOPERATIVE BUYING AND SELLING

members. Most large-scale marketing associations have departments that buy supplies for their member locals or directly for their farmer members. Thus, the Land O'Lakes Creameries, Inc., purchases a wide variety of supplies and equipment for its member creameries as well as dairy and poultry feeds for farmers who patronize the creameries. The large poultry and egg marketing associations on the West Coast handle thousands of tons of poultry feeds, egg crates, liners, and other equipment needed by their members. The Poultry Producers of Central California sold 101,030 tons of feed and poultry supplies in 1934 which were valued at \$10,628,418. Four other poultry and egg associations sold approximately \$6,500,000 of feed and supplies in the same year.

Regularly established purchasing associations that carry farm supplies in stock are found in all of the states. These establishments are comparable to most local feed and supply businesses, except that the farmers operate them on a cooperative basis. Associations that serve much larger areas in a wholesale capacity are found in several parts of the country, especially in the East where the two largest associations, the Cooperative Grange-League Federation Exchange, Inc., Ithaca, N. Y., and the Eastern States Farmers Exchange, Springfield, Mass., operate. In 1935-1936 the former sold feed, seeds, supplies and fertilizer at a wholesale value of \$42,000,000 to its 100,000 patrons located in three eastern states. The latter sold similar products valued at \$17,730,134 to more than 73,000 patrons in the northeastern states. Mills, laboratories, processing plants, storage plants, and local retailing units are parts of the large cooperative systems that these associations have set up. The Pacific Supply Cooperative organized in January, 1934, to serve as a central purchasing organization for farmers' cooperatives in the Pacific Northwest, sold products valued at \$3,000,000 in 1936 to seventy local associations. This wholesale organization is expanding rapidly.

The Ohio Farm Bureau Federation has organized seven subsidiary corporations to serve Ohio farmers. Their varied activities indicate the multiplicity of services which cooperative purchasing and service associations can render, to wit:

Cooperative marketing—sales \$1,000,000 in 1936

Cooperative purchasing—sales to 78 county associations \$6,750,000 in 1936

**Cooperative insurance—**

1. Automobile: 171,876 policies in force in July 1936, ten years after being organized, serving farmers in 8 states
2. Fire: serving eighty-eight counties, 12,759 policies in force in June 1936, organized in 1934
3. Life: 15,864 policies in force in June, 1936, insurance in force \$15,452,738, organized in 1930.

Cooperative credit—2,054 loans aggregating nearly \$1,000,000.

Rural electrification—organized in 1935 to help local units get electric power.

In a number of mid-western states the Farm Bureau Federation has been active in fostering cooperative purchasing among its members. The Farm Bureau Services, Inc., of Lansing, Michigan purchased for its members 2¼ million dollars worth of products in 1936, and the business of the Indiana Farm Bureau Cooperative Association, Inc., Indianapolis, Indiana was in excess of \$5,000,000 in 1936. The latter organization served eighty-nine affiliated associations and had net savings of \$131,000 in 1936.

The Farm Credit Administration, Cooperative Division, lists 2,112 purchasing associations having 950,000 members and transacting \$254,000,000 business in 1935-1936 (see Table II). Of the total cooperative business in the United States, cooperative purchasing associations accounted for 13.8 per cent of the total in 1935-1936 and only 2 per cent in 1913.

Since the first cooperative oil association was started at Cottonwood, Minn., in 1921, 1,000 to 2,000 associations, principally in the rural areas of the north central states, have sprung up. Local and county associations are served by cooperative wholesale petroleum distributing companies of which there are about a half dozen. In Minnesota, where the largest number of local and county associations operate, it is estimated that from 7 to 10 per cent of the gasoline business of the state is cooperative.

A number of large cooperative wholesale oil-distributing companies that sell gasoline, lubricants, batteries, tires, and other related supplies to the local cooperatives have made rapid progress since 1930. The Farmers Union Central Exchange, Inc., St. Paul, Minn., in 1931 had ninety-one affiliated companies, and in 1936, 233. Sales in 1936 were 3¾ million dollars. In 1935 a modern office building and oil blending plant was constructed. Another wholesaling organization which sells

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**TABLE II.—FARMERS' MARKETING AND PURCHASING ASSOCIATIONS, ESTIMATED MEMBERSHIP AND ESTIMATED BUSINESS,\* WITH PERCENTAGES FOR GEOGRAPHIC DIVISIONS, LEADING STATES, AND SPECIFIED GROUPS, 1935-1936 MARKETING SEASON†**

Geographic division, state, group	Associations listed‡		Estimated membership‡		Estimated business‡	
	Number	Per cent	Number	Per cent	1,000 dollars	Per cent
<b>Geographic division:</b>						
West North-Central.....	4,599	43.8	1,287,190	35.2	499,610	27.2
East North-Central.....	2,670	25.4	1,080,620	29.5	462,220	25.1
Pacific.....	829	7.9	197,460	5.4	278,970	15.2
Middle Atlantic.....	481	4.6	204,660	5.6	192,640	10.5
West South-Central.....	636	6.0	226,740	6.2	106,610	5.8
Mountain.....	460	4.4	142,500	3.9	88,160	4.8
East South-Central.....	250	2.4	240,370	6.6	63,220	3.4
South Atlantic.....	395	3.8	162,190	4.4	75,990	4.1
New England.....	180	1.7	118,280	3.2	73,380	3.9
<b>Total.....</b>	<b>10,500</b>	<b>100.0</b>	<b>3,660,000</b>	<b>100.0</b>	<b>1,840,000</b>	<b>100.0</b>
<b>State:</b>						
Minnesota.....	1,401	13.3	380,600	10.4	149,050	8.1
Illinois.....	706	6.7	334,540	9.2	162,100	8.8
Iowa.....	954	9.1	289,130	7.9	117,640	6.4
Wisconsin.....	1,086	10.3	217,050	5.9	94,150	5.1
California.....	448	4.3	79,830	2.2	196,430	10.7
New York.....	272	2.6	128,540	3.5	142,280	7.7
Missouri.....	435	4.1	191,500	5.2	80,530	4.4
Ohio.....	322	3.1	205,840	5.6	84,550	4.6
Nebraska.....	532	5.1	160,320	4.4	60,900	3.3
Indiana.....	254	2.4	195,190	5.3	57,450	3.1
Michigan.....	302	2.9	128,000	3.5	63,970	3.5
North Dakota.....	542	5.2	95,330	2.6	29,460	1.6
All others.....	3,246	30.9	1,254,130	34.3	601,490	32.7
<b>Total.....</b>	<b>10,500</b>	<b>100.0</b>	<b>3,660,000</b>	<b>100.0</b>	<b>1,840,000</b>	<b>100.0</b>
<b>Marketing:</b>						
Dairy.....	2,270	21.6	720,000	19.7	520,000	28.3
Grain (also dry beans, rice).....	3,010	28.7	610,000	16.7	360,000	19.6
Livestock.....	1,040	9.9	600,000	16.4	250,000	13.6
Fruits and vegetables.....	1,063	10.1	166,000	4.5	212,000	11.5
Cotton and products.....	311	3.0	300,000	8.2	110,000	6.0
Poultry and products.....	154	1.5	93,000	2.5	69,000	3.7
Wool and mohair.....	114	1.1	51,400	1.4	11,000	0.6
Tobacco.....	14	0.1	60,000	1.6	11,500	0.6
Nuts.....	52	0.5	16,000	0.4	13,100	0.7
Miscellaneous¶.....	360	3.4	93,600	2.6	29,400	1.6
<b>Total marketing.....</b>	<b>8,388</b>	<b>79.9</b>	<b>2,710,000</b>	<b>74.0</b>	<b>1,586,000</b>	<b>86.2</b>
<b>Purchasing.....</b>	<b>2,112</b>	<b>20.1</b>	<b>950,000</b>	<b>26.0</b>	<b>254,000</b>	<b>13.8</b>
<b>Total marketing and purchasing.....</b>	<b>10,500</b>	<b>100.0</b>	<b>3,660,000</b>	<b>100.0</b>	<b>1,840,000</b>	<b>100.0</b>

† Reported in *News For Farmer Cooperatives*, Farm Credit Administration, vol. 3, no. 10, January, 1937.

\* Estimated membership and estimated business for each association are credited to the State in which the association has its headquarters.

‡ Includes independent local associations, federations, large-scale centralized associations, sales agencies, and independent service-rendering associations, but not including subsidiaries or associations only renting unsold property.

§ Includes members, contract members, shareholders, shippers, consignors, and patrons. Some associations engaged primarily in marketing also engage in purchasing and some associations engaged primarily in purchasing engage in marketing. The purchasing business handled by the marketing associations amounted to \$68,000,000 and the marketing business done by the purchasing associations amounted to \$7,000,000. The final figures after making proper adjustments are marketing \$1,525,000,000; purchasing \$315,000,000; total \$1,840,000,000.

¶ Includes cooperative service organizations serving marketing and purchasing associations, such as cooperative auditing, management, and trucking associations.



supplies principally to local cooperative oil companies is the Midland Cooperative Wholesale, Minneapolis, Minn., which was organized in 1926. In 1936 it served 175 affiliated associations and sold products valued at slightly more than 3 million dollars. Both of these rapidly growing institutions serve local associations that are located in the states from Michigan to Montana. The Consumers Cooperative Association of North Kansas City, Mo., organized in 1929 with six retail oil cooperatives as members, sold in 1936, \$3,756,000 of supplies to its 342 member affiliates in eight central western states.

Cooperative retail stores were organized in urban centers by workingmen in the early fifties and in rural areas by members of the Grange in the seventies. Many failures and disappointments are associated with the cooperative ventures in this field. Today about 1800 of the 1½ million grocery, meat and general stores in the United States are cooperative. These stores are found principally in the rural areas of the middle western states, Minnesota, Michigan and Wisconsin. The competition of mail-order houses, chain stores and cooperative buying groups; the individualism of American people; the generally high level of wages and improved standard of living of American workmen; the absence of the urge to save a few cents a day on buying groceries; and in many instances the downright inefficient manner in which the poorly financed and poorly located stores were run explain in a large measure the numerous failures.

A number of cooperative wholesale establishments handling groceries, dry goods, hardware, and other supplies also serve the local stores. Of these the largest is the Central Cooperative Wholesale of Superior, Wis., a federation of about 100 stores with sales of nearly 3 million dollars in 1936. National Cooperatives, Inc., is a national wholesale organization that sells petroleum products and certain automobile supplies to regional wholesale associations.

Among the numerous cooperative associations rendering service for their members are those that provide financing, insurance, telephone service and electricity. In July, 1937, 6,183 local credit unions<sup>8</sup> provided a personal financing service

<sup>8</sup> A credit union is a cooperative association designed to encourage thrift and provide credit to its members for provident purposes. In essence it is a cooperative bank granting installment credit to consumers.

for their members at rates considerably below the usual rates charged for similar credit by private finance companies. Since the depression of the thirties, these credit unions multiplied very rapidly. In 1936 about 4,000 were organized under state laws and 1,100 under the Federal Credit Union Act (June, 1934). Practically all of the unions are located in urban centers because of the fact that their success depends largely upon personal acquaintanceships within small groups and also because of the fact that the credit needs of farmers in their productive operations are not adequately served by the unions, but are being served by production credit associations and national farm loan associations. Mutual fire insurance companies, of which there were approximately 1,900 in 1937 carrying about 55 per cent of the total fire insurance on farm buildings, include some of the oldest cooperative undertakings of farmers. Today a number of the larger companies have expanded into the fields of automobile, casualty, hail, windstorm, life, accident, and livestock insurance. Farmers' telephone companies were organized shortly after Alexander Graham Bell invented the telephone and in many localities provided a sorely needed communication service at a cost within the reach of many. Since 1934 special emphasis has been placed upon cooperative rural electrification under government sponsorship. This will bring the "high line" for the first time to many farmers in some of America's best rural sections.

Cooperative purchasing and service associations in the United States are found in the following fields: retail stores; oil stations; utilities; hotels, restaurants and boardinghouses; fuel; housing; burial; educational; publishing; insurance; laundries and dry cleaning; bakeries; hospital and medical service; auditing; credit; recreation (parks); milk distribution; garages; manufacturing; mail-order houses; management; and library.

#### Questions

1. What was the marketing program of the Grange during the decade 1870-1880? Of the Farmers Union?
2. What were some of the outstanding features of the organizations established by livestock producers?
3. What principal types of cooperative marketing associations were organized by the grain producers? When did the grain pool movement cease?

4. In what section of the country is the largest number of cooperative associations? The smallest number? What state in 1935-1936 had the largest volume of cooperative business? What fraction of all cooperative business is handled by purchasing associations?
5. Describe the period of 1920-1930 from the standpoint of the development of the cooperative marketing movement in the United States.
6. Through what types of associations are farm supplies purchased?
7. What economic conditions facing the farmers caused them to organize marketing associations during the last quarter of the past century?
8. How do you account for the fact that consumers' cooperative retail and wholesale associations have not made significant progress in this country except in a relatively few isolated places?
9. What developments have taken place among cotton cooperative associations in recent years that have held the members to their associations?
10. What reasons can you give for the relatively small number of members and small volume of cooperative business in the New England, South Atlantic, east south-central, and west south-central states?

## IV

### *Cooperative Marketing Abroad*

*Cooperative buying and selling is a world-wide movement varying largely in the degree in which it has become established in the different countries. Cooperative purchasing among farmers or city consumers has developed extensively in some countries, notably in England, Scotland, and Sweden, while cooperative selling of farm products is most common in other countries, such as Denmark, Finland, and Canada. The cooperative credit movement is extensively developed in eastern countries such as Japan, China, and India.*

*Denmark is the outstanding example of a country in which cooperative selling of farm products and purchasing of farm supplies have succeeded on an extensive scale. Nine-tenths of the butter, nearly nine-tenths of the bacon, one-fourth of the exported eggs, two-fifths of all seeds, two-thirds of the imported feedstuffs, one-third of the imported fertilizer, and one-fourth of the exported cattle are handled by the thousands of Danish farmers' cooperative associations. Many factors, of which the Danish folk schools are one, have contributed to this marked development.*

*A fair proportion of the retail trade in many European countries passes through cooperative channels, to wit, one-fifth of the Danish, one-fourth to one-third of the Finnish, one-seventh of the British, and one-tenth of the Swedish. Wholesale houses organized on a national and on an international basis are also operated successfully by cooperatives abroad. Most of the development of the cooperative retail and wholesale business abroad antedated the organization of the private chain-store system.*

*The economic conditions and the social environment in which cooperative sales and purchasing associations were established in foreign countries are quite unlike those found in most places in America. The principles of organization found successful abroad are generally adopted by American associations, just as certain principles discovered by American sales associations are applicable elsewhere.*



## CHAPTER IV

### COOPERATIVE MARKETING ABROAD

During the years 1920–1925 a large number of farm leaders, either individually or as members of committees, went to Europe to study cooperative marketing. This trek to the successful cooperative marketing associations on the Continent was inspired largely by the success of Danish cooperation. Ever since the eighties, cooperative marketing for various types of commodities has been carried on successfully in several countries of Europe. The basic reasons for their success, the forces that held the cooperatives together, and the principles which were adopted were the object of study by the Americans, who hoped to apply later, in whatever manner possible, the elements of foreign success to American conditions. As a result of many investigations, numerous publications and reports have been prepared revealing the conditions that were actually found or were reported to the investigators.<sup>1</sup>

In this brief survey of cooperative marketing abroad, the basic principles of organization, the types of commodities that were sold successfully through the cooperatives, and the environment in which the cooperatives became successful will be discussed.

**Cooperation a World-wide Movement.** Many people have heard of the cooperative movement in Denmark, but relatively few know that cooperative marketing is successfully carried on for one commodity or another in practically every country of the globe. Among the illiterate farmers of India, as well as among the educated producers in Australia and New Zealand,

<sup>1</sup> Reports such as *Cooperation in Foreign Countries* prepared by the Federal Trade Commission, Washington, D. C., in 1925, and the Report of the Saskatchewan Overseas Livestock Marketing Commission, 1927, Saskatchewan Department of Agriculture, Regina, Canada, typify the reports that have been published. The most recent account of cooperation in foreign countries is contained in the Report of the Inquiry on Cooperative Enterprise in Europe 1937, which was prepared by the President's Committee after an extensive tour of several countries in the summer of 1936.

cooperation has proved to be a workable marketing scheme for the many small growers. This general magnitude and importance of the movement undoubtedly merit the attention of everyone who is interested in the marketing of farm products and the price of farm produce. It has been reported that more than 285,000 organizations or societies, with a membership exceeding 40 million persons, are in operation in different parts of the world.<sup>2</sup> Cooperative laws are reported to have been passed in 129 states and countries. The annual value of the business of the cooperatives throughout the world is estimated to exceed 5 billion dollars. Although cooperation is practiced extensively, a relatively small amount of the total agricultural produce of the world is sold through cooperative associations. Private tradesmen who buy from producers to resell through the wholesale and retail markets still handle the bulk, likely as high as 85 per cent, of all agricultural products. But when one considers that very little had been done in the field of cooperative marketing prior to 1880 and that, in most countries of the world, extensive sales activities began at or about the time of the depression of 1921, it is apparent that the proportion of total goods now handled by cooperatives constitutes a sizable amount.

#### TYPES OF COOPERATIVE ACTIVITIES

In the United States the outstanding type of cooperative activity is that of agricultural producers marketing their own produce. Much less has thus far been accomplished in the field of consumer cooperation or in the field of cooperative credit, although the increasing activity in these fields is distinctly promising. In other countries of the world, however, cooperative credit and consumer cooperative societies have been most significant.<sup>3</sup> The agricultural cooperative marketing societies are of minor importance in most countries.<sup>4</sup>

<sup>2</sup> Cooperation in Foreign Countries, Letter from Chairman of Federal Trade Commission, p. xi, 1925.

<sup>3</sup> The term "society" is used abroad as "association" is used in America.

<sup>4</sup> "The agricultural cooperative marketing societies now to be found on the international market were not improvised suddenly. They are the present outcome of, and have behind them, a long process of evolution, the successive phases of which were parallel to the phases of development of marketing in general, and may be briefly outlined as follows:

"(a) In rural districts where economic conditions are still fairly primitive,

The cooperative movement has taken place among both urban and rural people. Although consumer and credit societies are not strictly confined to wage earners and persons of the lower classes, these people do constitute a vast majority of their membership. It is quite natural that in the food importing countries, such as England and Germany, the first cooperation should be among consumers; whereas in the food exporting countries, such as in the United States, Canada, New Zealand and Australia, the principal emphasis in cooperation should be upon agricultural cooperative marketing associations.

In this chapter, the cooperative credit and cooperative consumer societies will not be discussed. The work of F. W. Raiffeisen and Herman Schulze of Delitzsch in Germany, of Luzzatti and Antonio Maffi in Italy, of Fourier in France, of Plunkett in Ireland, of Høgsbro in Denmark, of Kagawa in

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cooperatives will be found, each member of which belongs to the society both as producer and consumer, *e.g.*, dairy cooperative societies (*fruitières* in the Jura, Savoy, Switzerland) and combined milling and baking societies (France, Czechoslovakia, etc.), which return to their members in the form of cheese, flour, or bread their produce of milk or corn.

“(b) Where marketing conditions have become more advanced and the separation between rural and urban centers is accentuated, the village trader appears, who combines the functions of grocer, draper, agent for fertilizers, etc., with those of intermediary for the disposal of agricultural produce in the towns, besides which he generally keeps the rural producer in a state of dependence by the practice of usury. It is for the purpose of replacing this middleman *that multiple-function cooperatives* are formed, such as the German Raiffeisen funds, the Czechoslovak *Kampelicky*, and the Irish or Indian general purpose societies, village societies, etc.

“(c) The development of the rural cooperatives, together with the development of regional and national markets, leads to the creation of powerful central cooperative societies for commercial purposes (the purchase of materials and agricultural machinery and the sale of agricultural products).

“(d) Finally, the specialization of certain countries or certain regions in a given form of agricultural production (butter, wheat, fruit, flax, etc.) which can be disposed of only in distant markets leads to the creation of agricultural cooperative marketing societies for particular products (the sale may be preceded by a more or less important process of transformation). These cooperatives correspond to the most advanced stage reached by agricultural economy in its relations with world economy.” *The Part Played by Co-operative Organizations in the International Trade in Wheat, Dairy Produce, and Some Other Agricultural Products*, C.E.I. 14, International Labour Office, Geneva, Switzerland, p. 6, 1926.

Japan, and of Hannes Gebhard of Finland, is fully described and analyzed in many works on cooperation. It should be pointed out, however, that one of the first needs of the small agricultural producers in European countries was credit. In a country where land is scarce and where the continuous cropping of land requires relatively heavy outlays for fertilizer, the necessity for credit to carry on the yearly productive operations is ever present. Rural cooperative credit societies of the Raiffeisen type,<sup>5</sup> through which credit could be obtained at fair rates instead of at the usury rates of the loan "sharks" were of tremendous economic importance to small landholders. As a result of experience with cooperative credit societies, it was simply a next step to organize cooperative stores for the purchase of commodities used in the household. The precedent established by British self-help movements was basic to the growth of numerous cooperative wholesale and retail societies, not only of England and Scotland, but of Germany, France, and the Scandinavian countries as well. The extent of consumer cooperative societies and their spirited operations in the fields of production are well known to students of economic history (see page 37 of this volume). The experiences which rural cooperators have had in both the credit and distributing societies were important forces in assuring the success of agricultural societies formed in the decades following the eighties. In England, Germany, France, Czechoslovakia, Sweden, Poland, and Belgium consumer cooperation is primarily among the urban people, whereas, in Denmark, Finland, Esthonia, Yugoslavia, and in Russia, it is chiefly among farmers.

In most countries, except in Denmark, Finland, Norway, Sweden, Holland, Switzerland, and other food exporting countries, cooperation among agricultural producers has received little attention, and, measured by the annual turnover, is small in

<sup>5</sup> The principles laid down by Raiffeisen have become as basic to cooperative credit unions as those of the Rochdale pioneers to consumers' cooperative stores. Their main features are: the local bank is owned and operated by, and in the interest of, its borrowers who are its members; par value of shares is small and payable in installments; unlimited liability; serves a single village or two; operations not conducted for profit; good character is the basis of a loan; limited dividends if any are paid; loans made to members only; low rate of interest; undividable reserves; inexpensive management elected by members each of whom has one vote.



volume. However, in this study of cooperative marketing, attention will be focused upon marketing activities rather than upon other types of cooperation. In order that this movement may be particularized, it is deemed advisable to concentrate attention upon cooperation in several countries in which agricultural cooperative marketing has proved distinctly successful. For this purpose the experiences of Denmark, Canada, Australia, and several other countries will be reviewed briefly.

#### COOPERATION IN DENMARK

In order to visualize the setting of the cooperative marketing movement in Denmark, it is necessary to consider a few characteristics of the land and its people.<sup>6</sup> Denmark is predominantly rural—a land of small farms. Fifty per cent of the farms are not larger than 30 acres, the bulk being between 20 to 70 acres. Most individuals own their farms which are neat in appearance and the centers of a happy rural life. The state encourages ownership of farms with the result that about 93 per cent of the 204,000 farms are owned by the operators. Extensive use is made of agricultural machinery, commercial fertilizers, and feed concentrates. Agriculture and fishing are the two main industries. On most small and medium-sized farms, the usual returns from livestock enterprises constitute 80 per cent of the gross income. The country, however, is only slightly less than one-third as large as Wisconsin, one-sixteenth as large as Texas, or about the size of Vermont, Rhode Island, and Connecticut combined.

In 1935 the population of Denmark was approximately  $3\frac{2}{3}$  millions. Of this number about 60 per cent live in towns. As a result of this proportion of rural to urban population, the produce grown on the farms is greatly in excess of the needs of the country. About one-eighth of the butter made in Denmark is consumed at home. Consequently, the Danes must look to an export market for a good share of their products. The fact that Denmark supplies from one-fourth to one-third of the butter

<sup>6</sup> A number of publications, reports and bulletins describe Danish cooperation. The reader may refer to Chris L. Christensen, *Agricultural Cooperation in Denmark*, U. S. Dept. Agr. Dept. Bul. 1266, for one of the most lucid descriptions of the movement. See also Harald Faber, "Cooperation in Danish Agriculture." Longmans, Green & Company, New York, 1931.

entering world markets and provides Great Britain with two-thirds of her bacon and one-third of her egg imports shows how successfully she has marketed her surpluses during the past fifty years.

Loss of the German market following the war with Prussia in 1864, and the competition with cheaper grain and feedstuffs from America during the sixties and seventies necessitated two important changes in the agriculture and rural life of this small nation. (1) It was necessary to concentrate upon animal production and more intensive agriculture. Cheap feed from abroad became a boon to animal husbandry in contrast to its dire effects upon grain growing. (2) An overseas trade would be necessary to take the place of the German market which was lost in the sixties. As a result, investigations were made of market demands in England and Scotland, and instruction was given to the rural producers as to the type and character of produce that the overseas markets demanded. Prior to 1887 the Danes supplied the German market annually with 200,000 to 300,000 live heavy, lard-type hogs. Through high tariffs and embargoes, the German market was lost, and after 1887, the British market was developed intensively. Among other things, this necessitated raising the bacon-type of hog instead of the fat-type, and substituting dairying in place of small grain production. Outlets were provided for millions of pounds of dairy products which could be produced to advantage in Denmark.

This loss of the German market and of a part of the Danish country, namely, Schleswig-Holstein, brought upon the people an intense feeling of nationalism—not a narrow economic nationalism such as permeated the thinking of the people following the World War but a political nationalism. The social educators of the day urged the citizenry to build a strong nation for the restoration of a desirable economic life. As a result, the spirit of working together for the solution of a mutual problem became deeply ingrained in the minds of the people. The economies of large-scale farming were possible through cooperation without losing the benefits which small landholding afforded. Cooperative credit unions were started in 1850, and cooperative stores in 1866. Cooperative marketing was but a next step and began in the eighties.

Another factor of particular significance was the influence of educators. A folk high school was established by Bishop Grundtvig in 1844, the same year the Rochdale cooperative started. From a handful of students, this institution for adult education has grown to a point where approximately 6,000 to 7,000 students from the farms annually receive instruction in these schools (fifty-nine in 1934). These schools are not vocational in character, but the subjects which are taught are of a cultural character—history, political science, economics, geography, religion, and civics. Young men between the ages of seventeen and twenty-five attend during 5 to 6 winter months, and young women during 3 summer months. These schools, with seventy to ninety pupils each, keep alive the spirit of cooperative association and have been one of the real creative forces in the development of cooperative marketing. Teachers that are inspired with “the living word” give force and vigor to the teachings.

The geography of the country must not be overlooked, for it relates directly to the type of cooperative associations that were established. The bulk of the country consists of the promontory Jutland, two main islands of Fünen and Zealand, and many small islands consisting of Lolland, Bornholm, Falster, Møen, and others. Moreover, the entire country is only 16,608 square miles in area. Small local associations, therefore, are most important. Considering that the United States is 182 times as large as Denmark, it is apparent that a geographical problem unknown to the Danes is faced in the organization of cooperatives in this country. With this statement of the land and people of Denmark, one can better understand why the cooperative marketing institution has grown rapidly in the country and is the principal type of marketing method used by the vast majority of agricultural producers.

**Cooperative Marketing.** “The agricultural achievements of Denmark are not matched by any other country in the world, area and population considered. . . . Denmark is, today, perhaps the foremost nation in the world with respect to scientific production and marketing.”<sup>†</sup> In these terms a Canadian commission

<sup>†</sup> Report of the Saskatchewan Overseas Livestock Marketing Commission, 1927, pp. 34, 54, Saskatchewan Department of Agriculture, Regina, Canada.

appraised rural Denmark. What brought this about for a country that has only a poor to fair soil, no exceptional climate, and no particular advantages with respect to markets? Several factors have contributed—the thriftiness which land ownership engendered (both quantity and quality production were sought); the operation of family-sized farms on which family labor was freely used; the concentration upon animal husbandry (cows, hogs, poultry) using the cheaper feedstuffs, grain and oil cake from abroad and the more intensive crops, such as mangel-wurzel, beets, and other root crops produced at home; the establishment of cooperative credit unions and purchasing associations through which ample capital and farm supplies could be obtained at savings over regular sources of supply; the adoption of scientific methods in agriculture fostered by the cow-testing associations, pig-breeding stations, agricultural shows, and agricultural schools; and lastly, though not least, the establishment of sound cooperative marketing associations for every commodity.

There are two types of cooperative associations in Denmark:

1. The general educational societies organized to disseminate scientific and technical information. About 90 per cent of the farmers belong to various kinds of these general agricultural societies.

2. The business societies consisting of the (a) commodity sales associations, (b) cooperative stores and purchasing societies, and (c) cooperative credit unions. In 1933, 1,669,862 persons, nearly half of the total population, were listed as members of 6,860 cooperative societies in Denmark. Today more than 85 per cent of all farmers belong to the cooperative business organizations. Only the cooperative marketing associations will be looked into here. Among the pioneers were Anders Nielsen and Bishop Grundtvig who promoted cooperation with a zeal that laid the foundation of a permanent institution in the country. The first distributive store in Denmark was established in 1866, and the cooperative movement in agriculture began about 1880.

**Butter.** Butter production is Denmark's chief industry. Nearly 90 per cent of the milk is converted into butter. The first cooperative dairy was established at Kaslunde, Fünen, Denmark, in 1875. Another appeared at Hjedding in 1882, founded by Stilling Andersen which became the basis of organiza-

tion for succeeding plants.<sup>3</sup> Each creamery has a 5- to 20-year contract (generally 10 years) with its members, and only members may deliver milk to the plant. A cooperative dairy is not ordinarily started until about 150 producers supplying milk from approximately 1,000 cows are secured as members. All milk is pooled, a substantial advance payment is made, and a final payment at the end of a 6- or 12-month period closes the transaction. Milk is graded and paid for accordingly.

There are twenty-three district societies which serve the local cooperatives. These district societies are amalgamated into three provincial associations. These provincial associations in turn are organized into the National Federation of Danish Creameries, which is a member of the National Council of Cooperatives. In addition to these various types of associations designed to market the Danish butter or represent the interests of Danish butter producers, a number of other organizations are established. In 1933 eleven cooperative export associations sold the butter for 641 dairies or 45 per cent of the 1,402 dairies in the country. In 1933, 47 per cent of all butter exports were handled by these eleven companies. These eleven export associations, organized after 1894, are of various sizes, and since 1918 have been associated into the Federated Danish Cooperative Butter Export Association for general, and not marketing, purposes. The most important outlet for Danish butter is the British market, and for years the Danes with their highly standardized Lur brand butter have received a premium over New Zealand and Australian butter. The buttermakers have their own organizations as do the creamery managers. Several thousand cow-testing associations have been established for the purpose of improving the productivity of the dairy herds.

In the field of dairying the Danish cooperative creameries have been the example, not only for other cooperative dairy marketing associations in the world, but for demonstrating the possibilities of cooperative effort correctly applied to a particular commodity. All butter which is exported abroad under the Lur brand must

<sup>3</sup> Christensen points out that in 1922, 1,335 of the 1,661 creameries were cooperative. In that year there were 11 export associations, with a membership of 546 dairies, which exported 38.8 per cent of all butter exports. Faber reports 570 creameries, out of 1,665, as members of the export associations in 1930. In 1933 there were 1,402 cooperative dairies which handled 90 per cent of all the milk received at dairy plants.

meet the government specifications with respect to high quality. These restrictions are very rigid, and as a result of intensive field service among producers and buttermakers, the butter is of such uniformly high quality that laymen cannot detect differences in the products from the several creameries. Milk is delivered daily and only a sweet cream butter is produced. This is sold in firkins or tins in the most competitive markets of the world.

**Bacon.** Between 3 and 4 million hogs are handled annually by the Danish cooperative bacon societies. In 1887 the first cooperative abattoir was erected in Horsens, Jutland. It had 1,218 members and received 24,000 hogs the first year. In 1916 the plant was rebuilt, and today it has a capacity of 3,000 hogs per week. About 85 per cent of the bacon produced is marketed through sixty cooperative societies that have a membership of approximately 180,000 persons (1933). Sixteen small private concerns were in operation a few years ago and handled about 15 per cent of the total bacon business. The packing business is not so centralized as in the United States; each plant serves a relatively restricted area and receives approximately 100,000 hogs and a limited amount of other livestock from about 3,500 farmers. These cooperative societies furnish two-thirds of the bacon consumed in England. The cooperative plants did not altogether displace existing plants but were erected to meet the needs of the producers as the hog industry expanded. There were seventeen private plants in 1890, twenty-one in 1921, and only sixteen in recent years.

Eighteen of the local cooperative organizations processing bacon were federated into a cooperative export society called the Danish Cooperative Bacon Trading Company, Ltd. This company was incorporated in England in 1902 by three cooperative Danish bacon societies. This one society sells close to one-third of all the bacon produced by the cooperatives and is one of the most important distributors of bacon in the British Isles. It has offices in England as well as in Denmark. Unlike the cooperative central-marketing companies in the United States, some of the capital stock of this organization is held by the retail stores that buy from it, and the net profits are divided between the member cooperative packing plants and the purchasing retailers.

In the bacon factories, one finds an illustration of remarkable coordination of marketing and production. This close adjust-

ment was not achieved in Denmark until the cooperative societies were established, and is found nowhere else in the world for any type of livestock. Every farmer is informed as to the weight at which his hogs should be marketed, and the manager of a cooperative bacon plant knows the number of hogs and the amount of bacon which the plant will receive during a given period of time. Hogs weighing from 176 to 220 pounds are demanded since these furnish the type of bacon preferred in the English market. Hogs are paid for on a basis of the dressing yield and quality rather than upon a live poundage basis. As a result of this very close coordination of production and marketing, Danish bacon finds no superior on the English market. In order that the high-class Lur brand bacon may be produced, the Danes have discovered that the cross of a Yorkshire boar with a native Landrace-type hog produces what is believed to be the most excellent type of bacon hog in the world.

**Eggs and Poultry.** It is reported that the first cooperative egg exporting society was established in 1895. This organization, the Danish Cooperative Egg Export Association, has 700 local branches with 45,000 members (1933) which constitutes only a small percentage of all egg producers. These egg and poultry associations handle about one-fourth of the eggs and poultry and have done much to perfect the system of marketing eggs, both at home and abroad. In 1932, 30 per cent of all eggs in the British market were from Denmark. This represented 85 per cent of all eggs sold by the cooperatives. Every egg sold through the association is stamped with the number assigned to the producer who delivered the eggs. This makes it possible, at all times, to identify the products of any producer. As a service to their members, the handling of eggs has become a side line of many butter and bacon factories.

**Seed Associations.** During the past decade thirty-one local societies have been organized for the purpose of growing and selling pure bred seeds. In 1925 there were 2,557 members in such associations. The Danish Farmers Cooperative Association for Seed Growing some years ago agreed to look after the production of genuine, pedigreed seed while the Cooperative Wholesale Society agreed to attend solely to the distribution through its retail stores. This illustrates again how producers' and consumers' cooperatives can work together.

**Cooperative Cattle Export Associations.** Fifteen cooperative cattle export associations handling 39 per cent of the meat and cattle exports were in operation in 1933. Their organization is similar to that of the creameries and bacon factories. Each association sells its own cattle, but for other general purposes, a national federation has been formed. The cattle, which are chiefly for slaughter, are appraised by a committee of three men, a payment covering the appraised value is made at once, and at the end of the year any surplus is prorated among the members on the basis of their patronage.

**Cooperative Purchasing Associations.** The Danish farmer has to rely upon the importation of seeds, oil cake, corn, and fertilizer. For this purpose 1,280 local cooperative societies were organized for the purchase of seed, and 2,839 local cooperative societies with a total of 150,000 members (1933) have cooperated to purchase fertilizer, feedstuffs, and coal. The Danish Cooperative Manure Society handled 35 per cent of the artificial manure used in the country (1933), and the Cooperative Fodder Societies received 67 per cent of the total net imports of feedstuffs in 1933. More than 40 per cent of all imported seeds are handled by the cooperatives. Other types of cooperatives, such as a cooperative cement factory, cooperative insurance societies, and a cooperative bank are found in this country.

Marketing societies have joined with other societies to present the interests of agriculture before the government, Danish industries, and abroad. Three great agricultural societies, the Federation of Danish Agricultural Societies, the Federation of Danish Cooperative Societies, and the Federation of Danish Small-holders' Societies, belong to a joint society, the Agricultural Council. Experimental work, livestock shows, and rural education are some of the joint activities.<sup>9</sup>

**Characteristics of Danish Cooperation.** An analysis of the cooperative effort among Danish farmers shows that the following characteristics identify the movement.

1. The organizations are born of necessity. It has already been pointed out that the loss of part of the country in 1864, as well as the German market, necessitated an overseas trade. This export market could be developed best through associated

<sup>9</sup> See Christensen's discussion, *loc. cit.*, of miscellaneous marketing and purchasing associations in Denmark.



rather than individual effort. It was also found that individual creameries located on farms that made butter from the milk of large herds obtained better prices for their large and regular shipments than was obtained by small producers of even higher grade butter. Therefore, if the advantages of regular shipments and large-scale operations were to be attained, the small producers were forced to cooperate with one another. The spirit of nationalism gave impetus to the cooperative movement.

2. The cooperatives are characterized by the unlimited liability which each of the members must bear. No statutes are provided for the incorporation of cooperatives. In most countries of the world, through the act of incorporation, the liability of the individual members is restricted to the value of the capital invested in the corporation, but in Denmark cooperation was undertaken without the protection of limited liability. Danish cooperatives are unincorporated. All liability is held jointly and severally by the members of the association, with the result that a good deal of conservatism is injected into the associations.<sup>10</sup> The directors, who were usually the larger and more progressive farmers, were forced to pay special attention to the financial affairs of the association if bankruptcy for the cooperative, as well as possible bankruptcy for its members, was to be averted. A natural outcome of this unlimited liability feature is the establishment of many small, closely knit local associations. However, the liability of local associations for the debts of the central sales associations is restricted.

3. Control of the local association, the primary type of cooperative activity in Denmark, rests with the local officers. These strong locals have been the bulwark of a successful cooperative marketing system, just as the locals have proved to be so valuable in organizations such as the California Fruit Growers Exchange and other West Coast federations.

4. Danish organizations have grown from the "bottom up," *i.e.*, from the farmer to the organization, rather than from the organization to the farmer. This perhaps has caused a certain amount of slowness in organization but, at the same time, has led to an element of permanency. As a result of this feature there

<sup>10</sup> Oftentimes, however, in cooperative dairies the liability of a member is fixed in proportion to the quantity of milk delivered during the term of the contract.

is an absence of the centralized type of associations which certain leaders have advocated in such glowing terms in this country. The Danish Cooperative Egg Export Association, organized previous to the local branches, centralizes the sales of eggs through the one association, but each branch maintains its autonomy. It is a federated society in which the central sales association was built at the same time that the first locals were. As more locals were organized, the membership of the central increased.<sup>11</sup>

5. Organization is on a commodity basis. It is not uncommon to find a Danish farmer belonging to as many cooperative societies as the number of products he produces. A man may sell his hogs through a cooperative bacon society, his milk through a cooperative creamery, his eggs and poultry through a cooperative egg and poultry association, and buy his pure bred seeds through a cooperative seed association, his commercial fertilizer through a cooperative fertilizer association, and his farm supplies through a cooperative feed association. He may also belong to a cooperative store at which his wife would buy the needs of the household, and a cooperative credit society may be open to him through which his credit needs are met. Cooperation on a commodity basis is one of the outstanding features of Danish cooperation. It is somewhat surprising that this particular feature should have become so firmly established in Denmark where the spirit of cooperation is as deeply ingrained as it is in the people. It appears that through a system of bookkeeping and accounting it might be possible to set up cooperative societies to handle a variety of commodities. But evidently it was expedient to set up separate associations in each of which there was an identity of interests of all producers. To a certain extent this principle of commodity specialization has broken down in later years in those plants where commodities, other than the main products, are being handled as side lines. Thus the cooperative bacon factories, which also sell eggs and poultry for their members, have deviated from the rigid application of the principle.

6. There is a small amount of coordination between consumer and agricultural cooperatives. Consumer stores, whose members

<sup>11</sup> The Danish Farmers' Cooperative Association for Seed Growers is a centralized type of organization having a contract between the central and each member and is an exception to the rule.

are chiefly rural folk, have not become closely associated with the agricultural cooperative movement. There is, of course, a mutual relationship between these two types of businesses, but it has not reached a much higher scale of cooperation than is found in other countries of the world where both types of activity exist side by side. The seed producers and the cooperative wholesale societies within the country have a working arrangement whereby one acts as the distributing agent and the other the producing agent.

7. The use of the membership contract is universal. Contracts of 1 to 20 years duration have been used by the various commodity marketing associations. Exclusive dealing with members is considered essential. It is again rather interesting to note that the contract was deemed an essential part of the organization among the Danes where the spirit of cooperation appears to be so deep seated. Evidently the greater volume of business which the use of a contract assured was considered highly essential by the cooperators who would be individually or jointly liable in the event of the bankruptcy of their organization.

A clause usually found in the constitutions and bylaws of Danish cooperatives relates to the arbitration of disputes between members and their associations. Each party individually selects one person and jointly a third to arbitrate a case. Such arbitration of disputes is a cheaper and often a more expeditious way of settling differences than through court action, but difficulties with nonmembers are settled through court action. Cooperatives in America could save much of the litigation arising from contract violations if boards of arbitration were used.

8. A close coordination of production and marketing, as exemplified by the Danish bacon industry, indicates the importance of extending cooperation as far back into the production operations as possible. The outstanding success of the Danish cooperative packing plants depended upon two things, (a) a regular supply of hogs with which to keep plants operating at optimum capacity and (b) upon the continuous production of uniform, high quality bacon demanded by the British market. As a result the marketing of a product without a peer in the markets of the world has been made possible. A highly standardized, uniform product is shipped regularly to foreign countries.

Such coordination has not been achieved in many countries of the world. Many American farmers still deliver cream of all grades and quality to their cooperative creameries, and many Canadian wheat producers haul grain of many varieties to their pools.

9. The nonstock type of organization predominates. Even in the bacon factories which require large outlays of capital for buildings, machinery and current expenses, the nonstock type of organization is used. The fixed and part of the working capital is usually obtained by a loan from banks which is guaranteed by the members. Within the larger associations these loans are divided among the different districts, and the farmers in each district become jointly and severally liable for their proportionate share of the debts.

10. The system of pooling is universally adopted. Advance payments are made shortly after delivery of products and final payments are made periodically, usually at the end of the year as in the bacon societies. Price quotation committees name the weekly prices for hogs and butter, and advance payments are made on the basis of these quotations. Very careful grading is practiced in all associations and payments are made only on a grade basis.

11. Part of the success of Danish cooperation is definitely attributable to the Danish people's high schools and agricultural schools. These schools inculcate in the minds of the young people the principles as well as the advantages of cooperation. They have done much to popularize and idealize cooperative marketing.<sup>12</sup>

**Some Other Aspects of Danish Cooperation.** In view of the long experience which the Danes have had in their local coopera-

<sup>12</sup> "Mr. Madsen-Mygdal, former Minister of Agriculture for Denmark, in analyzing the reasons for Denmark's success in profitably entering the British and other markets, places the emphasis upon the following factors: Competition, notwithstanding the extent to which cooperation is practiced, has been made a cardinal feature of Denmark's national economic policy; farming is broadly based upon ownership; the farmers have been given access to cheap and abundant capital; the farm has been organized on the basis of family labor; and above all the driving force of cooperation has been harnessed and put to effective use in every phase of the country's agricultural industry." Report of the Saskatchewan Overseas Livestock Marketing Commission 1927, p. 36, Saskatchewan Department of Agriculture, Regina, Canada.

tives, and their district and provincial associations, it appears somewhat incongruous to find the number of cooperative export societies which compete with one another. About forty of the cooperative bacon factories sell individually through private agents in England, and only eighteen (in 1926) are members of a central selling agency. Although a butter quotation committee establishes a price for all of the cooperatives, it, nevertheless, appears that certain economies in administration, as well as merchandising, could be achieved through consolidation of the eleven butter export societies. Furthermore, these butter export societies do not restrict their membership to cooperatives but sell butter for private creameries as well. Only about one-third of all cooperative creameries cooperate with each other in selling their butter through the export associations. Although a number of these are merely warehousing and shipping associations that do very little with respect to the actual merchandising of butter, still eleven appear as an excessive number. If it is advisable to organize the local associations into centralized groups for more effective transportation, shipping, and routing of their products, would it not be equally advisable to consolidate the export activities into one, or at best, only a few associations? American associations such as the California Walnut Growers Association, the California Fruit Growers Exchange, the American Cranberry Exchange, and the National Livestock Marketing Association have shown the possibilities of cooperation on a scale much larger than has been achieved by any of the Danish cooperatives.

Cooperation in Denmark, however, has been a more impelling force in rural habilitation than in any other country. The changes in agriculture and farm operations at the suggestion of cooperative groups, agricultural societies, and agricultural schools have been more marked in Denmark than in other countries. Cooperatives have been the media through which "better farming, better business, and better living" have been brought to the rural folk in the gateway country of the Baltic.

#### COOPERATIVE MARKETING IN CANADA

Measured by the number of associations, there are ten times as many cooperative sales associations as purchasing societies in the various provinces of Canada. The first efforts at cooperation

were started in the eighties and since that time about 3,500 organizations (1936) have been developed with a membership of approximately 320,000 persons.<sup>13</sup> These organizations are found from Prince Edward Island and Nova Scotia in the East to British Columbia on the Pacific Coast. Table III lists the number and kinds of Canadian associations.

The principal types of cooperative organization are those for the marketing of wheat, livestock, fruits, and milk. The wheat associations constitute approximately two-thirds of all the cooperative business associations in Canada; nearly one-half of the members of all cooperatives belong to the grain associations. The livestock cooperatives rank next in importance but are followed very closely by the dairy cooperatives when the value of business handled is considered. Fruits and vegetables are marketed principally in the western provinces and more than 100 associations, doing a business of close to 8 million dollars per annum, were operating in 1932. Other cooperatives are found among the poultry producers, as well as among the sheepmen who market their wool collectively.

**Type of Cooperatives.** In Canada local associations constitute the bulwark of cooperative activity. The thousands of cooperative grain elevators, cooperative creameries, and cooperative livestock-shipping associations provide the basis upon which provincial associations or federations are developed. For each commodity, a provincial organization has been put in operation to handle the products assembled, graded, and shipped by the local associations. These provincial associations are further united into interprovincial associations of which the Canadian Livestock Cooperative (Maritimes), the Canadian Poultry Pool, Ltd., The United Grain Growers, Ltd., and the Canadian Cooperative Wool Growers, Ltd. are illustrations. These organizations are principally the sales associations for the local and provincial companies. Some of these, particularly the grain associations, have provided terminal facilities at the principal export markets of Canada.

During the period 1925-1930, Canadian cooperative grain-marketing associations received world renown through the

<sup>13</sup> RICHARDS, A. E., *Farmers' Business Organizations in Canada*, *Dominion of Canada, Dept. Agr. Bul.* 173, 1934. This bulletin gives an excellent statistical summary of Canadian cooperation.

colossal activities of the Canadian Wheat Producers, Ltd., which was the central sales pool for the three provincial wheat pools. This organization had offices abroad as well as in the leading markets of Canada. The amount of grain which it sold annually was in excess of 100 million bushels, and its influence

TABLE III.—COOPERATIVE ASSOCIATIONS IN CANADA\* 1936

Province	Total	Agricultural							Non-agricultural	
		Marketing					Purchasing	Miscellaneous		
		Dairy	Fruit and vegetables	Grain and seeds	Live-stock	Poultry				Miscellaneous
Alberta.....	83	9	...	4	23	2	3	40	1	1
British Columbia	100	12	53	1	2	1	1	24	2	4
Manitoba.....	64	5	1	2	2	1	..	49	...	4
New Brunswick.	47	13	1	..	18	1	..	12	1	1
Nova Scotia.....	150	5	50	..	34	1	3	33	1	23
Ontario.....	282	50	33	11	29	7	9	90	21	32
Prince Edward Island.....	19	14	1	1	1	1	1			
Quebec.....	168	58	25	17	11	18	11	28		
Saskatchewan...	383	3	...	3	5	1	..	238	133	
Total.....	1,296	169	164	39	125	33	28	514	159	65

\* Directory of Cooperative Associations in Canada 1936, *Dominion of Canada, Dept. Agr., Farmers Bul. 9*, p. 6, Ottawa, Canada.

Number of associations does not represent places of business, for there are nine grain marketing associations listed in the three prairie provinces which operate 2,100 country elevators.

upon the grain markets of the world was rather significant. As a result of advances to wheat producers in 1929 in excess of sales receipts, the interprovincial pool faced serious financial difficulties, and only the assistance of the government of Canada saved the entire cooperative wheat movement from becoming wrecked. The dominion pool itself was discontinued, but the separate provincial pools have maintained their autonomy and sell wheat for member locals.

**Features of Canadian Cooperation.** The features of cooperative organization which the Canadians have found workable include the following:

1. The application of the principle of pooling for the sale of grain, which has not proved successful everywhere in the United States, has been adopted on a large scale throughout the Dominion. The collapse of the Canadian Wheat Producers, Ltd., did not, however, undermine the value of pooling per se, but simply revealed the difficulties which any business will meet when too liberal advances are made prior to a sharp drop in commodity prices. The pooling of livestock, grain, fruits, and milk is common in each of the commodity organizations.

2. Marketing contracts are used generally. Sixty-two per cent of the marketing associations in 1932 had contracts with their members. These were for periods of 1 to 10 years. Many of the contracts were of a continuous character with provisions for cancellation during certain periods. Practically 50 per cent of the contracts were for 3-year periods, however. The laws of Canada legalize the contracts, and damages can be collected for failure to comply with the same.

3. Some cooperatives are beneficiaries of direct governmental assistance. Liberal financial aid is given by some provincial governments. For example, in 1911, \$206,171 was advanced to the Saskatchewan Cooperative Elevator Company, and varying amounts were granted for several years afterwards on mortgages, so that by 1925 the total indebtedness to the government was \$2,386,738.28. The Dominion government itself subsidizes the Canadian Seed Growers' Association to the extent of \$10,000 per annum and smaller subventions are made for miscellaneous purposes to the association.<sup>14</sup> A counterpart of some of these financial assistances is found in the activities of the Federal Farm Board during the Hoover Administration in the United States.

4. Organization on a commodity basis has been generally followed. In some of the provinces where one-crop farming is carried on, it is quite natural that a single commodity should be the only article sold through the cooperative. The adoption of the commodity principle in marketing is not restricted to these provinces alone but applies with equal force to the eastern provinces where several enterprises are found on individual farms. The other usual principles of cooperative organization are found among Canadian associations.

<sup>14</sup> "Agricultural Cooperation in the British Empire," pp. 33, 34, George Routledge & Sons, Ltd., London, 1925.



## COOPERATIVE MARKETING IN SELECTED COUNTRIES

**Irish Cooperation.** Ireland produced one of the outstanding inspirational leaders of agricultural cooperative organization in the person of the late Sir Horace Plunkett. Sir Horace's catchy phrase "better farming, better business, better living" became the slogan of cooperatives not only in Ireland, but throughout the world during the decade of the twenties. Plunkett did much to promote the cooperative creamery movement in Ireland which started with the first cooperative plant at Dromcollogher in 1889.<sup>15</sup> His influence at congresses, cooperative meetings and through printed publications on the subject did much to inspire others in the cooperative movement. In 1894 he organized the Irish Agricultural Organization Society (I.A.O.S.), now with headquarters in Plunkett House (Dublin), which has proved to be the chief motivating force in agricultural cooperation. Its primary concern is organizing and promoting cooperative societies, and contributions of the member cooperatives and the government finance its activities. Much of the cooperation in Ireland, aside from the cooperative creamery movement, consists of "general purpose" societies that take in farm products and sell farm and household supplies. Relatively few consumer cooperatives, such as abound in England and Scotland, are in existence.

In their creameries an interesting development in cooperative manufacture took place. Most of the creameries in Ireland were privately owned, and as a result of the excessive number, the individual turnover was very low and the costs of operation were relatively high.<sup>16</sup> Through the passage of the proper

<sup>15</sup> ANDERSON, R. A., Horace Plunkett—Brief Sketch of His Life and Work, paper before the Conference on Development of Agricultural Cooperative Business, Aberystwyth, Wales, May 27, 1932.

<sup>16</sup> WILLIAMS, J. GLYNNE, New Developments in Cooperative Organization and Finance, paper before Conference on Development of Agricultural Cooperative Business, University College, Aberystwyth, Wales, May 27, 1932. Mr. Williams writes: "One of the most interesting developments in agricultural cooperative organization which demanded legislation took place in Ireland in 1928. . . . When the Irish Free State attained dominion status Irish cooperators were fortunate in having a government sympathetic to cooperation and more particularly to agricultural cooperation. It was realized in 1926 and 1927 that a large number of privately owned creameries, to put the fact plainly, were redundant. For obvious reasons owners were

legislation in 1928, brought about by the influence of cooperative leaders, the creamery business was practically turned over "lock, stock and barrel" to the farmers and their cooperative organizations. A large number of plants were closed, the size and efficiency of those operating were increased, the entire creamery system was placed on a cooperative basis, and to open any new creamery it was virtually necessary to obtain a permit on the grounds of public necessity. The Irish creamerymen have failed, however, to cooperate with one another in establishing a central selling agency. The Irish Associated Creameries, a cooperative sales agency organized in 1927 to sell butter for 154 creameries, failed within 3 years. This illustration is chosen to show that in Ireland cooperation, in a sense, was forced down from above upon the individual producers in the country. It shows how the government, through legislative action and

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quite willing to sell these properties at a reasonable price to any farmer-owned organization prepared to purchase. The reconstituted Irish Agricultural Organization Society took up the matter, but two main difficulties appeared to be insuperable (1) the necessary capital was not available, (2) certain properties were unsuitable, but nevertheless as factories, they were formidable competitors for the milk supply available.

"The method adopted to meet this difficult and national problem is unique and interesting. Civil servants as representatives of the state became registered as the 'Dairy Disposal Company' to purchase plant and buildings of creameries considered redundant, and these properties were then offered for resale to farmers' cooperative societies. Any property purchased by this company and not taken over by the farmers could be operated by the company on behalf of the state. To provide the necessary capital the Creamery Act, 1928, was passed. This act permitted the government to advance capital to farmers' cooperative societies but also forced members to take up share capital prorated at £ 1 share per three cows. To limit creamery activity in any area no new creamery could be established in an area except by permission of the Minister of Agriculture. As there probably would be some deficiency in the price paid by the farmer-owned societies when compared with the price paid by the dairy disposals company this was to be met by subsidy from Government Funds to the extent of a maximum of £95,000.

"By October 1931, 170 proprietary creameries had been purchased by the Dairy Disposal Company, 44 of which had been transferred to cooperative societies. Of the remainder, 79 had been closed and 47 were still held by the company. Creamery plants purchased from proprietary owners numbered 23. In addition 17 cooperative creameries had been taken over by mutual agreement, 4 of which were closed and 13 being operated temporarily."

financial assistance, can replace private organization by cooperatives. But it also demonstrates that unless the seeds of cooperation are sown in a well prepared soil their roots will not penetrate deeply enough to maintain a superstructure. Today, Irish cooperative creameries are essentially processing plants and are not especially successful marketing agencies. Their interest has been in the technical and not the commercial aspects of butter production and marketing. The success of this movement will perhaps depend as much upon the economies and efficiencies of manufacture as upon the change from private to cooperative management. To credit the success of this rationalization of the creamery movement to the cooperative organization *per se* is, no doubt, overlooking the possibility that success might have been possible under a rationalized system of private management.

Cooperatives, other than the creameries, also operate in Ireland. In 1934 there were 374 trading societies in Ireland, two-thirds of which were creameries. Others are cooperative bacon plants, egg, flax, and general societies. Ninety-two rural credit groups also operated in 1934. The depression of 1921-1922 and of the thirties took a heavy toll of the cooperatives in the country. Federated sales associations are practically nonexistent—there being only one in 1933; consumer-producer relations are not developed. Despite all of the constructive work of Plunkett, Father Finlay, R. A. Anderson, and George W. Russell (A.E.), "cooperation has not yet, indeed, come fully into its own."

**Australian Cooperation.** The cooperative experiences in Australia relate principally to the cooperative sale of exported farm products of which wool, wheat, and dairy products predominate. During the period 1920-1935 the establishment of both voluntary and compulsory pools for the various commodities has been common. Through agricultural legislation, particularly in Queensland, a compulsory pool may be set up for the marketing of a particular commodity when the majority of the producers at a popular election vote in its favor. Thus, in 1932 there were no less than fourteen commodity pools in operation, some of which were started as early as 1922 and were renewed annually, either without opposition or with a substantial majority to assure continuous operation. For example, the egg pool was

constituted in 1923 by an 87 per cent majority, and renewed in the following years by large majorities. Under the Wheat Pool Acts, a wheat pool was established in Queensland in 1921 by a 97½ per cent majority; continued in 1924 by an 89 per cent majority and again in 1928 without any opposition. It is apparent that the compulsory pools, although conducted by a majority which is interested in cooperative activity, certainly modify the principle of voluntary cooperation which is ordinarily considered the basis of cooperation.

The Australian cooperative organizations have been maintaining a fairly close relationship with the Cooperative Wholesale Society of England. For several years following 1924-1925 the Western Australia Cooperative Wheat Pool, which was the largest individual wheat exporter in Australia, was financed by the Cooperative Wholesale Society of Great Britain. In 1925 nearly 3 million pounds were advanced by the C.W.S.

The cooperatives in Australia are not organized strictly on a commodity basis, but deal in most agricultural commodities and buy from and sell to farmers. ". . . Agricultural cooperation in Western Australia has developed on its own lines and in defiance of some of the accepted traditions of the movement."<sup>17</sup> Producers' Markets, Ltd., is a cooperative handling fruit, poultry, eggs, and vegetables. It was reported that the general manager of the Westralian Farmers, Ltd., the large central organization of the cooperative movement in Western Australia, said that, "Commodity marketing as preached by Sapiro is unsuited to a small pioneer producer as Western Australia. Few commodities could afford individual administrative costs." This latter society sets up either autonomous locals, or establishes associations of its own in communities where local leadership is lacking.

The Australian cooperatives do not have a centralized selling policy such as is found among the American, Canadian, and Danish Cooperatives, but they cooperate with the cooperative associations of New Zealand and South Africa in maintaining a sales agency in London, the Overseas Farmers' Cooperative Federation, Ltd. The Westralian Farmers, Ltd., deals with the Overseas Farmers' Cooperative Federation of London in selling wheat in Europe.

<sup>17</sup> "Yearbook of Agricultural Cooperation, 1930," p. 226, George Routledge & Sons, Ltd., London, 1930.

**Union of South Africa.** Cooperation in the Union of South Africa has also been most important among the agricultural producers. Cooperative associations for the marketing of wool, wheat, maize, eggs, and meat (slaughterhouses) are in existence—437 societies with a membership of 85,000 were reported.<sup>18</sup> Compulsory pooling has not achieved the position that it has reached in Western Australia. Under the Cooperative Societies Act of 1922, cooperative associations in South Africa are prohibited from trading with, or on behalf of, nonmembers. This, it will be noted, is considerably different from the federal cooperative law in the United States. The government of the Union of South Africa has assisted the voluntary cooperatives by passing legislation calling for compulsory pools in the event that the majority of the producers vote in its favor. This has been done for tobacco. In some quarters cooperation is still regarded as the principal means of replacing the middleman, securing his profits, and raising prices. Hence, many believe that cooperatives can accomplish these things if all producers are compelled to belong to the same. Not all farmers in the Union feel this way about a cooperative, but many understand “that cooperation is business and must in order to succeed follow ordinary business procedure.”

**New Zealand.** In New Zealand all of the cheese produced in 1930 was manufactured in cooperative plants and fully 90 per cent of the butter was made cooperatively. Some of the cooperative creameries are the largest in the world and are models of technical efficiency. One, for example, makes 50 million pounds of butter and 12 million pounds of cheese annually, besides casein and dried milk. Government grading of all exported butter and government assistance to creameries in producing uniform, high quality butter has stimulated cooperation. Although creamery supplies are purchased through a centralized agency, still no outstanding success has been made in marketing butter through a central cooperative sales agency. A New Zealand Producers' Marketing Association, consisting of about 100 of the 500 cooperative dairy companies, ships butter to its London subsidiary, the New Zealand Produce Association, Ltd. This producers' cooperative is financed by the Cooperative Wholesale Society of Great Britain and through its London affiliate supplies butter to the C.W.S.

<sup>18</sup> “Yearbook of Agricultural Cooperation 1933,” p. 50, P. S. King and Son, Ltd., London, 1932

The sale of fruit cooperatively by seventy-three associations (1929) through the New Zealand Fruit Growers Federation, Ltd. (established in 1906) is an illustration of successful federated activities on the Islands. Only pears and apples are exported. Following the passage of the Fruit Control Act in 1924, fruit was brought, as butter already had been, under the control of the government with respect to shipping, grading, and marketing.

A cooperative wheat pool, similar to the Canadian wheat pools, was organized in Canterbury. Among the producers of meat and wool, there is very little cooperation in marketing. Honey producers have their Cooperative Honey Producers' Association and engage in export operations.

Although New Zealand farmers have shown zeal in organizing local cooperatives, still, with the exception of the fruit export association, they have quite generally failed in centralizing selling.

**Finland.** Finland is a predominantly rural country in which agricultural cooperation plays an important part. Three types of cooperative effort are found among the farmers: (1) cooperative stores, wholesale societies, and purchasing associations, (2) cooperative credit institutions and insurance societies, and (3) cooperative processing plants and sales organizations. Particularly prominent among the latter is the Valio Butter Export Cooperative Society, exporters of the famous Valio brand of butter. Organized in 1905, this cooperative has grown consistently so that in 1935 it handled approximately 93 per cent of all Finnish butter exports. A high degree of perfection has been attained in the butter through a careful system of grading, processing, packing, and shipping by the modern creameries which belong to the society. Sales are not confined to the export markets, nor is only butter handled, but local sales of milk and cream, butter, cheese, and other dairy products swell the annual turnover. Through its educational service departments, it has expanded dairying throughout Finland and has supervised the erection of new plants in many places. In 1934 there were 684 cooperative dairies, which produced about nine-tenths of all the butter and seven-tenths of all the cheese of the country. Organized on strictly cooperative principles, it has done for Finland what the cooperative dairies and their overhead organizations have done for Denmark. It has, however, carried the idea

of central selling further than the Danes have in their country. Cooperative slaughter plants and numerous egg and poultry associations are also found in the country.

**Norway.** In a number of other countries, cooperative marketing by farmers has played an important part. In Norway, many cooperative city milk-distributing societies have operated successfully. "At the end of 1930, the number of persons in Norway engaged in agriculture as a primary occupation was roughly 125,000, of whom nearly half were members of requirement societies, 40 per cent of the consumers cooperative movement, 35 per cent of cooperative dairies, 24 per cent of cooperative slaughterhouses, and 10 per cent of cooperative egg marketing societies."<sup>19</sup> The 10 cooperative slaughterhouses, 440 cooperative egg circles, local fruit, vegetable, honey and wool cooperatives, and the central societies for the dairy, poultry, and livestock cooperatives attest the diversity and extent of the cooperative movement in the country. Cooperative fisheries and cooperative sale of forestry products are also found.

**Sweden.** In Sweden cooperation has progressed as it has in Norway. Cooperative milk distribution in Stockholm is one of the largest enterprises of its kind in Europe. In 1935, there were reported to be 730 cooperative cheese and butter factories; 24 slaughterhouses (1929), and 29 egg and poultry associations (1929) in addition to the city milk distributing societies. More than two-thirds of the milk is processed in cooperative plants. Federations for egg, forestry products, livestock, fruit, and dairy societies have been set up, and, as in several other countries of Europe, have maintained harmonious relations with the organized consumer societies. Cooperation among rural producers has not progressed nearly so much as among urban dwellers.<sup>20</sup>

**Switzerland.** Switzerland is considered by many as the cradle of cooperation. Centuries ago the peasants in the Jura Mountains made cheese collectively in their *fruitières*. But it was not until the beginning of the present century that organized marketing associations appeared. Small cooperative dairies were

<sup>19</sup> "Yearbook of Agricultural Cooperation," p. 92, P. S. King & Son, Ltd., London, 1933.

<sup>20</sup> For a colorful description of cooperation in Sweden see Marquis W. Childs, "Sweden—The Middle Way," Yale University Press, New Haven, Conn., 1936.

started, and these formed federations within the various cantons. The cantonal federations organized national associations. In 1907 the federations organized the Swiss Milk Producers' Union in which fluid milk, condensed milk, and cheese producers were united. Later in 1911 a cheese export company, the Emmenthal Cheese Exporting Company, was set up. Ninety-five per cent of the Swiss Dairymen belong to cooperative societies of which there are 5,000. Twenty-four federations were in operation in 1930, and these had membership in the Swiss Dairy Union. Members of local societies carry unlimited liability. In addition to the processing and marketing societies, a large number of local associations, federated into 8 central organizations, exist for the purpose of importing and buying in large quantities members' requirements. One distinctive feature of Swiss cooperation is the close working relationship which the cooperative and private cheese exporting companies maintain.

In the "Report of the Inquiry on Cooperative Enterprise in Europe 1937," the diversity of the cooperative movement in Switzerland is shown by listing the following associations:

- 3 large federations of consumers' societies having 879 local member associations with 418,300 members in 1933
- 2,866 dairy and cheese-making societies
- 709 agricultural purchasing societies
- 1,436 cattle raising societies
- 426 water supply societies
- 323 electrification societies
- 206 agricultural-processing societies
- 87 soil-improvement societies
- 83 grazing societies
- 787 loan and savings societies
- 783 cooperative insurance societies
- 263 building and housing societies
- 140 cooperative restaurants.

In 1934, the Federation of Agricultural Societies of Eastern Switzerland (V.O.L.G.) had 310 local member societies with 23,000 farmer members. It acts as distributing agent for farm supplies and household goods and markets many farm products except milk and dairy products which are handled by another federation. One distinctive feature of the local societies affiliated with the V.O.L.G. is the joint and individual liability of its



members. As in other countries, this large wholesale society operates flour and feed mills, processing plants, and large storage plants and has in its employ about 300 persons.

**Other Countries.** About two-thirds of the butter and one-half of the cheese produced in the Netherlands come from cooperative dairies that are members of the *Allgemeene Nederlandsche Zuivelbund*. More than two-thirds of the dairies in Esthonia are cooperative, and these produce approximately 85 per cent of the dairy products. In Latvia the Central Federation of Cooperative Dairies exported one-half of all the butter of the country. About 90 per cent of all butter exports comes from cooperative plants.

In Egypt the cooperative movement began in 1909 through the efforts of Omar Loutfy, the father of Egyptian cooperation, but it was not until after the World War that the movement actually developed. After the passage of cooperative acts in 1923 and 1927 and the establishment of a government loan fund, the number of agricultural associations increased from 162 in 1928 to 587 in 1933 and the membership quadrupled.<sup>21</sup>

In the Philippine Islands, some cooperative effort among producers of tobacco and copra is carried on. In China very little agricultural cooperation is practiced, except in the field of cooperative credit.

In Japan farmers' cooperative marketing associations and cooperative purchasing societies have made considerable progress since 1900. In 1931 there were nearly 8,000 of the former and 10,000 of the latter. Local marketing associations are affiliated into more than 100 federations, and many of the federations are united into two national marketing organizations for raw silk and rice grain, respectively. The most important commodity bought by the purchasing associations is fertilizer.

In India, where perhaps the largest number of people of any country are members of cooperatives, the cooperative credit societies flourish, but the strictly agricultural marketing groups are not to be found in large numbers. Much difficulty has been experienced in organizing the Argentine producers, and in South American countries in general, cooperatives have not been important. Cooperative marketing is found among farmers in other

<sup>21</sup> RASHAD, IBRAHIM, "Agricultural Cooperation," Egyptian Government Printing Office, Cairo, 1935.

countries than those listed here, and omission here does not in any manner deprecate its importance in those countries.

#### INTERNATIONAL COOPERATION

In 1895 the International Cooperative Alliance was founded for the purpose of unifying the cooperative activities of many countries of the world. This organization publishes an official organ and sponsors annual congresses at which the principles and practices of cooperation are discussed. International cooperation is primarily between the cooperative consumer societies.<sup>22</sup> Efforts at uniting producers' cooperatives of several countries have been made, but the progress is slow. The International Confederation of Agriculture, headquarters in Paris, and the secretariat at Brougg, Switzerland, through membership on the International Committee for Cooperative Relations comes in contact with the International Cooperative Wholesale Society (I.C.W.S.). In 1933 about 200 million dollars of international cooperative trading was negotiated for the member wholesales by the I.C.W.S.

**Cooperation of Consumer and Producer Societies.** At many of the meetings of the International Cooperative Alliance and at the national cooperative congresses held in the different countries, the possibilities of closer cooperation of the consumer societies on the one hand and producer societies on the other have been discussed and encouraged. It has always been felt by the leaders of cooperation that in order to have a complete cooperative society there must be a gradual working together of consumer and producer groups to eliminate the middlemen and drive out speculation in the handling of the necessities of life. It was deemed a workable scheme, for example, to have the farmers of the Canadian prairies sell their wheat to the S.C.W.S. (Scottish Cooperative Wholesale Society) in Glasgow in such a way that both would gain from the transaction. As a matter of fact, the S.C.W.S.

<sup>22</sup> The cooperative wholesale societies of Sweden, Norway, Denmark, and Finland organized a central buying agency, the Nordisk Andölsförbund (N.A.F.), with headquarters at Copenhagen for the purpose of having one agency buy imported goods for its five member societies. In this case an international cooperative was set up to take the place of private middlemen's services. According to reports this international cooperative venture has proved to be highly successful.

bought 1,730,000 bushels of wheat in 1928-1929 from the Canadian Wheat Pool.

An amalgamation of consumer and producer societies is difficult to achieve wherever prices and profits are the chief considerations in their business transaction. Where reciprocal trade relations do not prevail or where no interdependence between groups exists, the consumer cooperatives attempt to buy at the lowest prices possible consistent with the quality of goods obtained. The sales associations, on the other hand, have their primary zeal in obtaining the highest prices obtainable in market places. One is interested in low prices—the other in high prices; and to effect a close cooperation between the two groups that are so price conscious is almost an insuperable task. This statement is not meant to suggest that there cannot be some cooperation, even a great deal, between the two groups, nor that it is inadvisable. Far from it. In many instances sales associations would prefer to sell to consumers' groups and consumers' groups would prefer to buy from sales associations, if they could obtain goods at as low prices as from other traders. But when price advantages are sought it is perfectly apparent that neither shows the other any priority over any other trader in the market. This is far from the type of cooperation which some enthusiastic leaders have in mind when they speak of consumer-producer cooperative activities.<sup>23</sup>

Some real efforts have been made to coordinate the activities of these two groups. For example, the C.W.S. of England and the New Zealand Producers' Cooperative Marketing Association organized in 1921 a London Company called the New Zealand Produce Association, Ltd., in which the New Zealand Marketing Company and the C.W.S. hold the same number of shares. The New Zealand Cooperative attends to the handling, consignment, insurance, and financing of shipments of butter from New Zealand;

<sup>23</sup> The attitude of two scholars in the field of consumers' cooperation on this issue is described in Chap. XXVIII in the book "Cooperation" by F. Hall, and W. P. Watkins, Cooperative Union, Ltd., Manchester, England, 1934.

For an interesting account of the conflict in some countries and harmony in others existing between consumers' cooperatives and agricultural sales associations at this time in Europe, see Chap. XIII, "Consumer Cooperatives and Agriculture," Report of the Inquiry on Cooperative Enterprise in Europe, 1937, U. S. Government Printing Office, Washington, D.C.

and the London affiliate, advised of the shipments, handles the butter on its arrival in London, determines its price and arranges its sale. The C.W.S. is not obliged to buy from the London company, nor is the company obliged to sell to the C.W.S. A sale to the C.W.S. is consummated provided the price is mutually agreeable. In other words, a commission agency was set up jointly by producer and consumer societies for the purpose of handling butter sent by a cooperative society in New Zealand. The operations of the company, however, are very much like those of any dealer who strives to get the highest prices for his produce in the market.

The large cooperative wholesale societies constitute an important market for producers' associations but at the same time become important competitors if buying agents for the wholesale societies establish offices in the producers' territory and buy from private and local cooperative groups. It appears logical that the facilities of established consumers' groups should be used to provide the producers' organizations with supplies which the companies and their members need. Illustrations of such reciprocal relations follow.

In 1932 the Danish Union of Cooperative Slaughterhouses purchased 250,000 bacon wrappers from the Scottish Cooperative Wholesale Society which illustrates reciprocal trade relations between producer and consumer cooperatives. For years (since 1881) the C.W.S. of Manchester maintained offices in Denmark for the purpose of buying butter from the cooperative creameries. The C.W.S. of England has also maintained direct contact with the Finnish Valio organization. The arrangement between the Danish Farmers Cooperative Association for Seed Growing and the C.W.S., whereby the former agrees to produce the seed required by the latter and the latter to distribute it through its retail stores, has been mentioned. Supplies in excess of the C.W.S.'s needs may be distributed by the seed growing association.

In Austria, for instance, a producing country, the imports of butter and cheese are very small: the local (consumer) cooperatives obtain their supplies from the agricultural cooperative marketing societies or directly from the producers. As regards butter, over 62 per cent comes from the marketing cooperatives; nearly 35 per cent is bought direct from the farmers, and the rest is supplied by the Wholesale Society. In Finland

the distributive cooperative societies obtain their supplies direct from the countryside. One of the two chief central organizations purchases 78.67 per cent of its butter and 25 per cent of its cheese from the agricultural cooperatives. The other does not directly undertake the distribution of butter and cheese, as its local societies obtain their supplies from Valio, the Central Sales Office of the Cooperative Dairies. The Swedish Cooperative Union . . . buys all its butter from the agricultural cooperatives and all its cheese on the open market. . . . The Swiss Union of Distributive Co-operative Societies, which covers most distributive societies, obtains the whole of its cheese supply, or 1,607,000 kilograms, from the Swiss Agricultural cooperatives (1925), except for 5,000 kilograms imported from Italy. For butter, on the other hand, the supplies obtained from the Swiss agricultural marketing societies cover only a small proportion of the requirements of the Union. Its imports of butter in 1925 amounted to 1,412 tons, or nearly 16 per cent of the total imports of butter in Switzerland in 1925. The greater part (over 78 per cent) of the imports of the Union came from the Danish cooperatives.<sup>24</sup>

As far as the information at present (1925) available shows, Switzerland for butter and Great Britain for dairy produce and wheat are the only countries in which the distributive societies have direct and constant relations with the agricultural cooperatives of the exporting countries.<sup>25</sup>

Swiss purchases of Danish butter are made direct from the cooperatives in Denmark, and likewise, English and Scottish C.W.S. purchases of wheat are made direct from the Canadian cooperatives. "Conversely, the Canadian Distributive Societies, which are now making rapid progress in the Canadian provinces, obtain their groceries and manufactured goods from the British Wholesale Societies."<sup>26</sup>

#### GENERAL OBSERVATIONS

The following observations are made after inquiring into the extent and nature of cooperative activities in the various countries of the world.

<sup>24</sup> The Part Played By Cooperative Organizations in the International Trade on Wheat, Dairy Produce, and Some Other Agricultural Products, League of Nations, International Labour Office, C.E.I. 14, pp. 23, 24, Geneva, 1926.

<sup>25</sup> *Ibid.*, p. 26.

<sup>26</sup> *Ibid.*, p. 23.

1. It appears that cooperative principles can be successfully applied to the marketing of any kind of agricultural products. As far as the characteristics of the commodity itself are concerned, there seems to be no limit to the application of the cooperative principle for its distribution. Perishable, as well as nonperishable commodities, staples or nonstaples, seasonally produced or continuously produced goods, commodities sold upon highly organized exchanges or in the absence of such exchanges—all these are sold through organized associations in some place or another throughout the world. Whether it be for pure bred seeds, fat cattle, copra in the Philippines, cotton in the South, or honey in Australia seems to make no difference whatsoever to the successful application of cooperative business technique. It can be said, therefore, that the principles can be successfully applied throughout the world for all types of commodities.

2. The characteristics of the people are significant in determining the extent of cooperative organization. Among the agricultural exporting nations, cooperative sales of farm commodities are more important than cooperative purchases. But, among the importing nations cooperative purchasing associations play a more important role. Among the well-educated farmers of Denmark who are steeped in the history and experience of cooperative associations, this method of doing business is common, but among the isolated producers in Argentina, it has been much more difficult to inculcate the spirit of cooperation. The system of land tenure, the methods of land management, the size of individual farms, the credit standing of the producers, and the experience in cooperative activities of one kind or another, all affect the extent to which the sale of farm products is carried on cooperatively. Although universality of nationality, of language, and of religion are important in uniting and maintaining farmers in cooperative groups, yet exceptions among American farmers are sufficient to show that such universality of social institutions is not necessary to insure the success of a business organization such as the cooperative.

3. Most successful cooperative organizations in different parts of the world are organized on a single commodity basis, but organization on a multiple commodity basis does not, in the least, spell failure. The general principle of organization on the commodity basis, in contradistinction to organization on a geograph-

ical basis, has proved its merits repeatedly. The experiences of many cooperatives in the United States and elsewhere confirm this opinion. It appears that there is a greater unanimity of interest when the organization is on a strict commodity basis. Through wise management and an accurate system of accounting, operations of a multiple commodity organization are not only feasible, but can be highly successful.

4. In most European and Asiatic countries cooperative agricultural credit associations were basic to cooperative marketing associations. This was not the case in North America, however. In both rural and urban centers of the United States credit unions became widespread during the depression years of the thirties. It has not been discovered, however, that the credit association is fundamental and must necessarily precede the organization of cooperative marketing associations. It becomes an excellent training school, however, for those who later engage in cooperative marketing activity on a much larger scale than is usually conducted by the cooperative credit unions.

5. Public policy in practically every nation of the world has favored the development and progress of cooperative marketing. Laws legalizing cooperative associations are enacted in most countries, and although these laws vary in their completeness and in their details, they nevertheless give positive approval of the principles of cooperative marketing.

6. Relatively little of the total business of handling farm products is carried on by cooperative associations. Despite the approval of this method of marketing, farmers in many parts of the world, with the exception of Denmark, still market only a small proportion of their total produce through the cooperatives. For the world at large, certainly not more than 10 to 15 per cent of all agricultural produce is handled by farmers' associations. This percentage is not so small when one realizes that cooperative marketing is less than fifty years old in most countries. Significant results have been achieved in the field of special commodities, but in the field of the staple commodities, particularly those for which organized exchanges exist, marked changes in either the method of handling or in the prices obtained have not been realized.

7. Consumer-producer cooperation is still primarily in the realm of discussion rather than in the realm of reality. It is significant

that the International Cooperative Alliance is taking steps toward a closer interworking relationship between consumers' and producers' organizations in various parts of the world. In special cases, reciprocal trading has been established. It may be added, however, that of the business which has been carried on between cooperative consumer and producer groups, practically all of it is conducted on the same basis as that governing transactions with private concerns. The possibilities of a more efficient relationship than this are questionable.

8. There is general acceptance of the principles of cooperation as adopted by the English Societies. It is true that in some countries, as in Western Australia, modifications of these principles have been made. The enabling acts of some countries prohibit dealings with nonmembers which was a policy generally followed by early societies. In other countries, however, this principle is not adhered to, and a much more liberal interpretation is made with respect to dealing with nonmembers. On the whole it is significant that the type of cooperation which the English flannel weavers followed in 1844 is the kind which consumers' cooperatives have found as workable schemes of organization and operation.

9. In many places state control, or positive state encouragement, of cooperative marketing is found. In Ireland, Russia, Germany, and Italy close control by the state is characteristic of the system of cooperative marketing. In the Danubian countries, the East, and the Near East government aid and actual government subsidy of the cooperative movement are positively welcomed and to many are indicative of the soundness of this system of marketing. This is quite unlike the attitude of farmers and cooperative leaders in western countries concerning the government's relation to cooperative business. In Western Australia, cooperation is encouraged to such an extent that compulsory pools are set up following a vote in their favor. This is simply a recognition of the merits of voluntary cooperation and is an attempt to obtain for all producers the beneficial results which voluntary cooperation makes possible for a limited number.

10. Nowhere have the cooperatives successfully set aside the established laws of economics for any permanent period. Challenges to the general application of the laws of supply and demand and definite attempts by some associations to establish monopoly



prices under conditions of highly competitive production and to engage in operations contrary to the general principles of economics have shown repeatedly the basic necessity of recognizing economic principles. Temporary successes have been made when there was an apparent overthrow of the accepted principles of economics, but nowhere has a permanent change been made. It is of interest to see in the history of cooperation in many countries that cooperative leaders have relied upon "self-help through mutual help" rather than on state aid, protection through tariffs, and on subsidies as means of permanently improving agriculture.

#### Questions

1. What different types of cooperative activity are found in the countries of the world, and where do the special types predominate?
2. Why has cooperative marketing become so important in Denmark?
3. What are the leading characteristics of Danish cooperative associations? Of Canadian cooperatives?
4. What is the I.A.O.S. and what functions does it serve?
5. What features are found in Australian cooperation that are not found among cooperatives in Denmark and the United States? In Swiss cooperatives?
6. Examine the monthly publications of the International Cooperative Alliance and report the general nature of the subject matter treated.
7. What do Hall and Watkins in their book "Cooperation" have to say about the relation of producer to consumer cooperatives?
8. What general conclusions can be reached about the practicability of applying the cooperative method of marketing to different commodities in different countries of the world?
9. What principles of cooperative organization have been generally followed by the associations in the different countries?
10. What notable progress has the Swedish cooperative movement made? (See Marquis Childs, "Sweden—The Middle Way.")

**PART II**  
**THE ECONOMIC PHILOSOPHY OF COOPERATIVE  
MARKETING IN THE UNITED STATES**

### *Basic Economic Concepts of the Cooperative Movement*

*The philosophy of a people at any given time will determine the system of organization that they will adopt to govern their economic activities. Broadly speaking, their choice is limited to three main types of economic systems.*

*One type, known as laissez faire, is characterized by lack of organization. In a laissez-faire economy it is every man for himself. Each individual is supposed to know his own desires. He is to be free in exercising his ingenuity to accumulate wealth and to spend it. Advocates of this system believe that the net resultant of freedom of enterprise and lack of restraint in one's conduct toward others will be the greatest good for the greatest number and the aggregate national income will exceed that produced under any other system of economy.*

*Planned economy is another system. In this system, the authority is centered in some individual or group of master minds to draft, direct, and control the activities of the masses toward definite goals in such a way that the greatest social good may be attained. Individual rights to free enterprise are restricted, the ownership of property for certain uses limited, contractual relations curbed and public exchange transactions regulated. Usually, control is attempted by artificially stimulating prices of some commodities and stabilizing or reducing them for others until a parity is established upon some predetermined base.*

*Cooperation is a resultant system of economy. It is a synthesis combining the desirable qualities of the laissez-faire economy and the planned economy. Insofar as it is possible, the undesirable features inherent in the two older systems are not transmitted to the new system of cooperation. Cooperation broadens the base of democracy extending it into the economic and social fields of endeavor for the benefit of all those who possess the intelligence to control and direct human activities on a mutual basis.*



## CHAPTER V

### BASIC ECONOMIC CONCEPTS OF THE COOPERATIVE MOVEMENT

The signing of the Declaration of Independence was a momentous occasion for Americans. The historic document issued by the Continental Congress on July 4, 1776, gave political expression to the critical philosophy of John Locke which, nearly a hundred years earlier, had been presented in the Bill of Rights in England.<sup>1</sup>

The development of a more secure economic status has been an evolutionary process since that time. Labor, handicraft workers, consumers and peasants have not always enjoyed the freedom of political and economic expression, and for hundreds of years individual rights were restricted by royalty. In more recent times individual rights were favored disproportionately over the rights of society. The masses did not enjoy economic freedom equal to that extended to the dominant groups in government, the merchants and manufacturers. The businessmen declared for freedom from oppressive governmental and legal restrictions, and they were granted certain rights, franchises, and privileges of free enterprise. Industrialists not only received freedom from governmental restrictions in their activities, but they invoked the aid of the government in situations where free enterprise failed to give them adequate protection against the encroachments of others. Thus we observe the curious phenomenon of a business class petitioning government intervention when its own interest, such as the security of property and the sacredness of contracts against violence and nonperformance, were affected, but valiantly defending the right of free enterprise against social classes in less influential circumstances. Government has been slow in recognizing the need of the exploited masses for protection against ruthless free enterprise.

<sup>1</sup> The essence of Locke's philosophy was the defense of individual liberty against the divine right of kings or the church.

It is only in comparatively recent times that the government has interceded between manufacturers and consumers to safeguard public health by enforcing pure food and drug acts. Better working conditions, shorter hours, and social security legislation indicate an increasingly humanitarian consideration of the laboring population. The agrarian class has made some progress in securing reform in market organization and more adequate facilities for financing farming operations. Much of the success of these reforms is directly attributable to organization on the part of the masses—organization to avoid the ravages of free enterprise and the evils of competition. Organization has been made possible by laws giving consumers, farmers, and workers the right to form cooperative associations. This is democracy in business.

As long as industrial organizations operate on a corporate basis, there is danger that bargaining power may become unbalanced. The only means for maintaining any semblance of equality in bargaining power and for avoiding exploitation is to form corporate associations manned by the common classes. Whenever an individual becomes a member of a cooperative association, he makes a declaration of independence. He declares his self-reliance and his right to guide his business activities and to plead his own case for government intercession in compensating for the limitations of free enterprise.

The major systems of organizing society for economic activity, and the relative merits and shortcomings of these systems, form the subject matter of this chapter.

#### HOW THE LAISSEZ-FAIRE SYSTEM OF ECONOMY DEVELOPED

The most ardent advocate of a competitive economic order was Adam Smith. He had a theological concept of divine abundance which formed the background for his treatment of the science of political economy. Smith was inspired early in his life by Francis Hutcheson, one of the greatest teachers of the eighteenth century. The core of this teacher's philosophy was the implicit faith he placed in nature, a benevolent Deity and a virtuous mankind. Hutcheson, more than anyone else, was responsible for Smith's acceptance of John Locke's view of philosophy.

Smith diffracted the views of these two philosophers into his economic concepts. By means of specializing labor he showed how the earth might become a haven of abundance, with the

gracious endowments of a divine munificence. This munificence, it was implied, would most strongly affect the merchants and the State; for it was recognized that abundance resulting from the division of labor was limited only by ability to find market outlets. Smith believed that most men were inherently good and that they could be entrusted with freedom of action. The ability of man to direct his own affairs for his own interests would, in Smith's opinion, grow out of this freedom, and when each individual pursued his own selfish ends the "greatest good for the greatest number" would be realized. This was Smith's formula for amassing the *wealth of the nations*. What Smith failed to realize, however, was that freedom would permit the strong to combine against the weak and limit the advantage of free enterprise.

There is very little comfort in the foregoing chain of reasoning for those who hope to escape the evils of competition by organized effort. Smith's influence upon economic thought is incalculable. To this present day his premises are basic to such maxims as "competition is the life of trade," and the "law of supply and demand is inevitable." Commons points out the importance of these fundamental assumptions in giving direction to economic thought in the following comparison of Hume and Locke:

Hume derived both self-interest and justice from scarcity, but Smith, Locke, and Quesnay derived them from abundance. If there is abundance of nature's resources, no person can injure any other person by taking from him all he can get, if he does this by exchanging his own labor for that of the other. The other has abundance of alternatives to which he can resort if he is not satisfied with the terms of exchange offered. And the one who makes the offer does not suffer if it is not accepted, because he also has abundance of alternatives. Enough will be left for others to take all they can get by a similar method. Self-interest cannot injure anybody in a world of abundance. . . .<sup>2</sup>

If there were unlimited abundance of everything, there would be no self-interest, no justice, no property, no ethics.<sup>3</sup>

In his thirteen years of tenure at Glasgow University, Smith attended the weekly meetings of a political economy club, and there associated with the most eminent merchants and manufacturers of Scotland and England. Occasionally Smith jour-

<sup>2</sup> COMMONS, JOHN R., "Institutional Economics, Its Place in Political Economy," p. 161, The Macmillan Company, New York, 1934.

<sup>3</sup> *Ibid.*, p. 6.

neyed to Edinburgh to spend a pleasant week end or holiday with David Hume and his friends. This group was as much interested in the problems of agriculture as were the members of the Glasgow circle in manufacturing and trading. In this way Smith maintained his contacts with both the practical and the theoretical world of economics and, through the latter, formed some definite impressions about the production of wealth in a nation. England was rapidly becoming an industrial nation, and Smith discovered the unusual possibilities of production through division of labor. Prior to the time he met the Physiocrats, his discourses upon the subject of economics in the Glasgow classrooms were limited mainly to problems of production.

In 1764 Smith went to Europe where he began writing "The Wealth of Nations." On this visit to the Continent, Smith met Voltaire at Geneva and in Paris, and through his friend, David Hume, was introduced to distinguished members of the Physiocratic School. Here he met Quesnay and Turgot, who brought to his attention the problem of the distribution of wealth in society. The Physiocrats' criticism of mercantilism, their emphasis upon agrarianism and fiscal policies broadened Smith's horizon and inspired him to expand his treatment of the subject of economics.

Smith's contact with the leading thinkers of his time enriched and clarified his vision and resulted in his philosophy concerning the welfare of the State, as summarized briefly under the following points:

1. His basic assumption was that there is, to use the words of Bagehot, "a Scotchman inside of every man," and since this is the case, every man should be permitted to do as he pleases because:

2. If every man is exerting himself to his utmost in getting ahead in the world, he will certainly be the best judge on matters concerning the use of his time and his money. Who could decide better than he what enterprises should be developed, how they should be run, and what effect they might have on the other members of the community? At least, it was safe to assume, according to Smith, that the individual could decide these questions more effectively than any magnanimous politician, invested with position and power.

3. On the basis that every man is given free rein and all politicians and lawmakers are bridled, it was concluded that if the

net results of every individual's activities were added, the sum total of national wealth would be larger than under any other system of economy. This was Adam Smith's recipe for making nations rich.

If the old fires of competition burned brightly in the early part of the industrial revolution, their embers still glow in varying degrees of intensity, for competition still exists in a virile state in industries of small capital requirements and those less subject to the advantages of the division of labor.

#### PHYSIOCRACY A BARREN SOIL FOR ORGANIZATION

The narrowness of the physiocratic doctrines admitted no concepts so broad as those identified with the cooperative movement. Implicit faith in the savagery of a *natural order* was considered of paramount importance in directing the economic affairs of man. The Physiocrats failed to distinguish between the selfish interests of an individual and his duties to society. On the contrary, they held them to be identical, and this view prompted Gournay to label the idea *laissez faire, laissez passer*, i.e., liberty for all in the pursuit of personal interests will result in the greatest good for society in general. Rousseau, a contemporary and critic of the Physiocrats, challenged this thesis in his celebrated statement that "personal interest is always in inverse ratio to duty, and becomes greater the narrower the association and the less sacred."

That the doctrines of physiocracy provided a barren soil for the growth of cooperatives is apparent in the other recommendations offered by this school of thought for the advancement of society. The importance of primary utility in the production of agricultural products was overemphasized. The Physiocrats believed that land was the only factor in production which returned to its owners and cultivators "outputs" in excess of "inputs." This excess over costs was called the *produit net*, a concept which today still intrigues and ensnares some of the less enlightened rural residents. The Physiocrats thought that their position within the confines of this grand postulate was impregnable. Their security, they believed, rested on the assertions of Cantillon:

If the prince and the proprietors of lands close their estates and will not suffer them to be cultivated, it is clear that there would be neither food nor raiment for any of the inhabitants; consequently, all the



individuals are supported not only by the produce of the land which is cultivated for the benefit of the owners, but also at the expense of these owners from whose property they derive all that they have.<sup>4</sup>

The modern version of the Physiocrats' thesis was expressed or implied in the Farmers' Holiday movement of the Middle West in 1933-1934.

We have this day declared a National Farmers' Strike to become effective at 12 o'clock noon on Oct. 21, 1933, which strike will remain in operation until our farm products bring the cost of production, and until we are refinanced under the terms of the Frazier Bill; and will include:

1. We will pay no taxes or interest until we have first cared for families.
2. We will pay no interest bearing debts until we receive the cost of production.
3. We will buy only that which complete necessity demands.
4. We will stay in the homes which we now occupy.
5. We will not sell our products unless we receive the cost of production but will exchange our products with labor and the unemployed for the things we need on the farm, on the basis of cost of production for both parties.<sup>5</sup>

All occupations except farming were regarded as sterile, for none produced a surplus in excess of "inputs." Manufacturing simply changed the form of materials and made them useful. Professional and personal services were regarded as parasitic. Trade was considered desirable when confined to simple, direct, and free transfers of material goods from producers to consumers. Buying and selling for profit was looked upon with disfavor because it absorbed too much of the *produit net*, limiting the amount available to agriculture for the next crop season. The Physiocrats believed that the affairs of the State should be entrusted to an absolute hereditary monarch, and they would not have favored any form of democracy in either state or commercial enterprises.

#### LAISSEZ FAIRE: INDIVIDUALISM NOT COOPERATIVISM

The 75-year period comprising the last quarter of the eighteenth century and the first half of the nineteenth was marked by

<sup>4</sup> CANTILLON, RICHARD, "Essai sur la Nature du Commerce en Général," p. 43, translated by Henry Higgs, Macmillan Company, Ltd., London, 1931.

<sup>5</sup> Proclamation calling a Farmers' National Strike by the National Farmers' Holiday Association Conference, St. Paul, Minn., Oct. 19, 1933.

significant changes, politically, economically, and socially. The study of the social sciences was markedly advanced in this period by a dominant group of writers who became known as the Classicists. The Classicists were Thomas Robert Malthus, David Ricardo, James Mill, J. R. McCulloch, and Nassau Senior. Adam Smith and John Stuart Mill are also included in this school by most writers but not without some words of qualification.

Malthus differed from Smith in his approach to the economic science in that he followed Hume in his major premise. He assumed that the prime cause for collective action in society was scarcity and that scarcity was the basis of the economic science. Without the presence of scarcity on every hand, there would be no economic science.

In an attempt to repudiate the thesis of the perfectability of man presented by William Godwin in *Political Justice*, Malthus framed a law of population which cast such a gloom over economics that it depressed everyone who studied his essays on the subject. After Carlyle read these publications, he dubbed political economy the "dismal science."

Starting from the major premise of scarcity as the foundation of economic science, Malthus formulated the theory that people tend to multiply faster than foodstuffs can be produced. He presented a picture of human beings combating the specter of scarcity and struggling against the adverse ratio of food to population. He believed that, as time went on, people would be crowded farther and farther out on the margin, thus finding it increasingly difficult to eke out an existence from a niggardly nature. This observation led to the formulation of the law of diminishing returns in agriculture by West, and at the same time it formed the basis for the Ricardian theory of rent.

Labor, according to Ricardo, would get only enough wages to sustain life and multiply in numbers sufficient to supply industry with workers. The theory of the wages fund grew directly from this doctrine. Real wages in general were low and never could rise appreciably. Trade unions and all types of relief were considered of no importance in alleviating the conditions of common laborers. The Classicists attributed the unfortunate condition of workers to the ignorance and lack of foresight of the workers themselves. They believed that profits of industry were directly influenced by the wages of labor—for the short-time

period when wages were low, profits would tend to be high; and when wages were high, profits would be low.

The capitalist landlord who lives on the fruits of appropriation finds that with an increasing population he can exact more and more income in the form of rent because: (1) The differential return on good pieces of land becomes greater as new fringes of marginal lands are brought into cultivation. (2) He profits by rising prices more and more because a greater amount of human labor is required to produce a given unit of food products at the margin.

In brief, the picture presented by the Classicists through their large and abstract generalizations was one which held little hope for a large portion of the total population. It was a system in which the strong found it easy to exploit the weak, and as long as it remained a philosophy of industrialism, little hope could be held out for those who maintained that a man should be master rather than object of his destiny. Cooperative efforts of laborers, according to these beliefs, could do little to improve their status. It was this school of economic thought that provoked other thinkers to suggest methods of intervention.

#### THE THEORISTS' COMPROMISE ON THE SUBJECT OF VALUE

The scarcity concept suggested by Hume and developed in economic theory by Malthus and his followers formed an absolute basis for determining value from the supply side of the market. The Neoclassicists reasoned that if economic goods are scarce because man is obliged to wrest them from a meager store of nature's resources, then the obvious explanation of value is to be found in the "labor pain" or "labor force" required to produce such goods. Since farmers form the membership of agricultural sales associations, they will tend to stress the costs or sacrifices involved in providing supplies for the markets.

Jevons began his explanation of value by assuming that all value is based upon utility. On studying the nature of utility, he discovered that it tends to diminish with each increment, and hence he derived the law of diminishing utility. As utility diminishes it approaches a margin, and the price paid by a person for the marginal unit determines the value of the goods. Now, if the laborer who is a member of a consumer cooperative retail store momentarily forgets he is a laborer and weighs in his mind the

utility of an article, he will be inclined to favor utility as a gauge in pricing household necessities.

The storm of controversy between the hard-headed materialists and the psychic marginists raged until the close of the nineteenth century when Alfred Marshall deductively reconciled them by providing for each a place of honor in the halls of Exchange. In the philosophy of the classical and neoclassical schools of economic thought, the forces of materialism and hedonism are so deified that mortal man has only to await the pleasure of the gods in the determination of just values.

#### THE PLANNED ECONOMY—A SYSTEM OF COMPULSORY COLLECTIVE ACTION

The economic doctrines of the Mercantilists provided no more stimuli for cooperative action than those identified with either the Physiocrats or the Classicists. While their system is suggestive of the powers of organized action, it is inimical to the philosophy of cooperation because mercantilism was based primarily upon the exploitation of labor, and it exaggerated ownership of property, especially of the precious metals. The economic philosophy of Sir James Steuart, the brilliant Scottish theoretician and last great exponent of mercantilism, favored government supervision and control of industry. He believed that individuals should be restrained in their activities of wealth getting when those activities conflicted with the interests of the state or of society in general. Accordingly, he set himself to the task of outlining and making more explicit a broad program of state control, in which he suggested that the statesman must intervene and direct the activities of the masses if public interest was to be advanced to the same degree as private interest. Mercantilism in Steuart's time was a complex system of state control and regulation, in which tradition required the regimentation of the masses to produce the maximum national economic prosperity. In this period of intense nationalism, a policy of power was security against the attack of belligerent neighboring states. All able-bodied laborers were directed to be gainfully employed in producing goods that could be exchanged with the outside world at an advantage. The object in striving for a "favorable" balance of trade and inducing a flow of precious metals into a country was to maintain a nation at its full fighting strength. Gold and silver

were not an end but a means to sustaining a nation's integrity. It was, in every sense of the word, a planned economy in which the government assumed definite directional responsibilities.

The mercantilistic program of that era was, in brief:

- I. Policies Respecting Trade
  1. Maintain high tariff walls
  2. Develop a powerful merchant marine
  3. Establish colonies to promote trade
  4. Explore and develop new areas to secure cheap raw materials and sell finished goods for the development of the new country
  5. Trade with other nations where best bargains could be consummated
  6. Secure an excess of exports over imports—a "favorable" trade balance
- II. Policies Respecting Manufacturing
  1. Encourage certain types of manufacturing by
    - a. Giving direct bounties for production
    - b. Granting franchises and monopoly privileges
- III. Labor Policies
  1. Control entrance to occupations by adherence to strict apprenticeship rules
  2. Govern the supply of labor and transfer workers to those industries needing manpower
  3. Determine physical conditions under which employees should work
  4. Regulate hours of labor and the rate of pay
- IV. Promote agriculture as a source of cheap raw materials for manufacturing and for the support of a nation on a self-sufficing basis in time of war

Mercantilism has its counterpart in the strong nationalistic tendencies which have been developing in the countries which participated in the late World War. Reconstruction of the battle-torn countries called for a high degree of organization and governmental guidance in directing labor, controlling trade, arranging finances, and stimulating manufacture. This experience in building nations anew has resulted in a most aggressive form of competition among rival political states in their efforts at self-containment and national consciousness.

These countries assert their independence and seek to maintain the wholesome respect of their neighbors by manifestation of power. Power of organization for offense or defense—whether it be a war against depression and unemployment, or an armament program—calls for a high degree of integration in primary production, manufacturing, and distribution. In order to attain these

ends, control of industry and business is vested in some governmental authority. Under such authority, the individual finds himself in a position exactly opposite to the one which he holds in a laissez-faire economy, for in a strongly nationalistic state, individual rights and interests are subordinate to the interests of the nation as a whole. Cooperatives would have been subjugated to the national authority under this philosophy.

Commentators who attempt to predict the drift of politico-economic affairs do not agree in their observations of the direction the cooperative movement is taking in such countries as Nazi Germany, Fascist Italy, and Soviet Russia. The International Cooperative Alliance has consistently maintained a respectable aloofness in its relations with representatives from these countries. It earnestly protested the emasculation of the movement by a strongly centralized government, as illustrated by Germany's decree of 1935.

A law passed by the German government on May 21 and published in the Reichsgesetzblatt of May 24 will have a tremendous influence, the extent of which cannot yet be fully foreseen, on the German consumers' movement. The "Law on Consumers' Societies" as it is officially called—"Law against Consumers' Societies" would have been a better name—is such a severe blow to consumers' cooperation that the German consumers' movement—once so proud—will be completely crippled and robbed of all possibility of development. It is not out of the question that this may be the beginning of the end of the movement—if an organization which has been deprived of all opportunity of development may, indeed, be called a movement. . . .

The bill has three main objects, namely:

1. To restrict the development of the consumers' cooperative movement
2. To decimate (or, more accurately, to halve) the funds of the consumers' movement
3. To create the possibility, and the legal conditions, for a complete transformation of the method of business of the consumers' societies, including the deprivation of their cooperative character.<sup>6</sup>

Karl Walter, in his study of Italian cooperation, is of the opinion that the cooperative movement is playing an important part in shaping the policies of the Fascist state.<sup>7</sup>

<sup>6</sup> A Heavy Blow to the German Consumers' Movement, *Review of International Cooperation*, (London), June, 1935, no. 6, p. 214.

<sup>7</sup> WALTER, KARL, "Cooperation in Changing Italy," p. 75, P. S. King & Son, Ltd., London, 1934.

Freppel Cotta found in 1935 that cooperatives in Italy enjoyed free initiative and democratic control when their activities were confined to economic purposes.<sup>8</sup>

A reviewer of Cotta's book questions whether the influence of the fascist state upon Italian cooperatives is for the best when considered from a long time point of view.

Just a word about the methods of control exercised by the government. The most important are those placing the cooperatives under the Minister of National Economy who has the power not only to inspect but to dissolve their managing boards and to appoint a representative of his own to run the organization. In the final analysis, this is complete control.<sup>9</sup>

#### SOCIAL AND ECONOMIC REORGANIZATION ADVOCATED

The horrors of the French Revolution were still vivid in the minds of the critics of the early nineteenth century. They realized the necessity for some changes in the organization of society, but they were mild, almost timid, in their Utopian and idealistic schemes for social reform. Their failure to project bolder and more drastic plans may be attributed possibly to the fact that most of them were of the *bourgeoisie* class and a few of the aristocracy. Moderation in ideas, too, was considered a virtue, for the rulers of that period were not noted for their tolerance of free speech and an untrammelled press. The events following the French Revolution had shaken the confidence of the critics in the ability of the untutored masses to govern themselves in an acceptable manner or to manage their economic affairs. The critics desired the alleviation of the deplorable conditions of the masses, but they feared that if the masses were given freedom to overcome some of the most apparent evils in the political and industrial system of that time, they would become intoxicated with power and attempt to use it in excess of good reason. Accordingly, the recommendations of these critics of the nineteenth century social order are characterized by suggestions for modifications that would make the system of government and industry run more smoothly.

<sup>8</sup> COTTA, FRÆPPEL, "Agricultural Cooperation in Fascist Italy," P. S. King & Son, Ltd., London, 1935.

<sup>9</sup> HOBSON, ASHER, *Journal of Farm Economics*, vol. 17, no. 3, pp. 605-606, August, 1935.

**The Swiss Critic.** Sismondi, for example, accepted classicism in economic thought. His suggestions for reform typify those of his contemporaries. He favored the development of industry and corporate freedom, but he proposed to curb corporate competition which was based upon exploitation, by restricting child labor, prohibiting work on Sunday, and shortening hours of labor. He was one of the first to suggest a form of unemployment insurance in which the employers would be obligated to maintain workmen at their expense during old age, periods of illness, and temporary shutdowns. Sismondi's recommendations, like those of Owen, St. Simon, and Fourier could be projected from the upper strata of society down to the poorer working classes. Their persistent, underlying principle held to the belief that the *bourgeoisie* must keep control in their hands and effect a paternalistic relationship with their more unfortunate contemporaries.

**St. Simonism.** St. Simon, likewise, was not clearly opposed to private property. He did not distinguish between the "haves" and the "have-nots," but instead, drew a line of demarcation between those who toiled and those who toiled not. He believed that everyone except the halt and the lame should be made to do some type of useful work. If all people could be put to work, he contended, the productivity of the masses would ameliorate their material welfare and improve their moral conditions. Workers were to be classified into three groups: (1) savants, (2) artists, and (3) laborers.

Like many of his contemporaries, St. Simon had an antipathy toward those who engaged in trade and exchange, and this idea found expression in the monastic order which was created in his memory. He thought that many of the evils of society originated in the market transaction because it permitted men to exploit one another. St. Simon visualized a form of society in which exchange would take place without the use of a medium, so that everyone would be occupied in exploiting the earth and not his fellowman.

**Owenism.** One of the most remarkable men developed by the incidents of the Industrial Revolution was a Welshman, Robert Owen, who began work as an apprentice shopboy when he was ten years of age. For 20 years (1780-1800), he acquired much experience in several business ventures before becoming part owner and manager of the New Lanark cotton mills on the river Clyde in Scotland. This establishment employed nearly 2,000



workers, 500 of whom were children of from five to twelve years in age. For many years, various parish workshops in Scotland had apprenticed children to the New Lanark mills.

In addition to the virtual slavery of children, many women were drawn into this type of employment at very low wages. Men were brought to the cotton mills from Ireland where the peasants were starving, and from the Highlands of Scotland where the crofters were being driven from the land to make room for sheep enclosures and game preserves.

The millworkers of New Lanark were, on the whole, better treated by David Dale, the former owner, than laborers were by most of the cotton barons of that period, and several of the reforms for which Owen received much credit were initiated by Mr. Dale. Apparently Owen thought there was still some opportunity for improvement for he described the laborers at New Lanark as "a collection of the most ignorant and destitute from all parts of Scotland, possessing the usual characteristics of poverty and ignorance. They were generally indolent and much addicted to theft, drunkenness, and falsehood, with all their concomitant evils, and strongly experiencing the misery which these ever produce."

Owen revolted against these social conditions. He was influenced by William Godwin's philosophy and was certain that meanness in character was the product of an unfavorable environment. He had faith in humanity and believed that men are by nature neither good nor bad, but that the low state of their culture in the English industrial centers was caused by deplorable working and living conditions. He consecrated his life to the cause of the poor by choosing to be their leader and benefactor instead of exploiting them to amass a private fortune.

One of the first measures taken by Owen to improve the New Lanark environment was to close all retail liquor shops and replace them with provision stores operated by the company. Only the best quality goods were stocked—including fine whiskies—which were supplied to the workers at cost. Next, he put a second story on all the low one-room dwellings in the village, doubling the size of each family's quarters which he insisted must be kept clean. The program of refuse disposal, clean streets, sanitation, and orderliness in the homes met with much resistance at first but the institution of a health visitation committee charged with the responsibility of visiting all homes and making reports

soon overcame this resistance. It was not long before New Lanark was reputed to be the model manufacturing village in Great Britain.

To discipline workers while on the job and to prevent theft in the factory, Owen invented the silent monitor system. This consisted of a small square of wood, painted a different color on each side. Black signified bad conduct, blue stood for indifference, yellow for fair demeanor and white indicated excellence. A record was kept of all workers from day to day, and in time, there was a marked change in the attitude of the workers. All fines previously levied for infractions of rules were abolished.

Probably Owen's most famous experiment at New Lanark was his school system. After reducing the length of the laboring day from seventeen to ten and three-quarters hours, he provided an adult educational system to improve the knowledge of his laborers. After 1809, he instituted infant schools in which dances, drills, singing, amusements, and a study of pictures, charts, and natural objects were emphasized. He permitted no child under the age of ten to work in the factory. It is said of Owen that he derived his inspiration for educational reform from Rousseau and Pestalozzi, but he was not conscious of this debt until he visited the Continent in 1818 where he met such men as Oberlin, Fellenberg, and Pestalozzi.

During the quarter century Owen was master at New Lanark, he was never entirely free from the opposition of his partners. Their interference caused him to leave New Lanark in 1824 and migrate to America to escape the intolerance, prejudice, and customs of older societies. He bought 20,000 acres of land for £30,000 at Harmony, Indiana, from a religious colony of German peasants known as the Rappites. "Here, then, in the heart of the United States, Owen proclaimed the power which governs and directs the universe and every action of man—'permit me to announce a new empire of peace and good will to men.' He concluded his address, it is stated, by inviting the 'industrious and well-disposed of all nations' to come to New Harmony."<sup>10</sup> They came, but not all of them were industrious!

The publicity given to Owen's plans for a new society over-sold New Harmony to the American public. Eight hundred

<sup>10</sup> PODMORE, FRANK, "Robert Owen, A Biography," vol. I, p. 291, Hutchinson & Co., London, 1906.

volunteers arrived at New Harmony within the first few weeks and many more came later. This noble social experiment lasted only three years. In 1828, the lands were divided and the mode of living reverted to individualism. A similar voluntary community established at Queenwood, England, also failed.

While Owen was occupied with these experiments, his philosophy spread rapidly among the laboring classes of England. They attempted to do in their own communities what Owen had done at New Lanark. They tolerated commercialism to acquire a fund to finance the establishment of a new-type community. Incidentally, this method of business proved that trade could be carried on without profit.

The organization of Labor Exchanges was an attempt to market cooperatively the handicraft products of labor. In his book, "The New Moral World," Owen lists the causes of the evils which prevail in the world, and among these causes he mentions:

The monetary system of all nations

The practice of buying and selling for a moneyed profit

The present practice of producing and distributing wealth

Force and fraud, as now prevalent in every department of life in all countries

The falsehood and deception now prevalent over the world.<sup>11</sup>

Cooperatives in all countries have wrestled with these conditions which Owen deprecates and have been responsible for improving them somewhat. In Owen's estimation these evils were especially prevalent in trade, and he sought to minimize them by a new type of organization in which values would be based upon labor. The unit measurement of value was time (labor hours), and book credit or labor notes were issued to those bringing goods to the exchange for barter. The price of goods was determined by combining money costs for raw materials with labor time spent in production plus a penny per shilling to cover the cost of operating the exchange. From 1830 to 1835 the Labor Exchanges had a period of mushroom growth throughout England. The most notable exchange was the Gray's Inn Road Exchange of eight hundred forty members organized by Owen personally in 1832. None of the exchanges survived more than

<sup>11</sup> PODMORE, *op. cit.*, vol. II, pp. 479-480.

a few months. Their main limitations were: the acceptance of goods for which there was no demand; transferability of labor notes was not restricted to laborers; the exchange created no reserves to absorb losses.

The humanitarian philosophy of this great man was a novel phenomenon in a world steeped in commercialism. His insistence upon making the world a better place to live in, and his spectacular Lanarkian reforms made a deep impression upon the laboring classes and aroused them from a state of lethargy to one of cooperative action. Owen had no respect for a capitalistic profit system. In his management of the New Lanark mills, he set aside 5 per cent annually for capital, and remitted the remainder of the profits to the employees as wages.

Owen believed that there were three dominant institutions in the capitalistic system, which like Geryon, the Greek mythical monster, form barriers to the happiness of man. These are (1) private property, (2) religion, and (3) marriage.

In his recommendation for abolishing property, the idea of a "just price" is implied. Goods should be sold at cost. The "just price," of course, was considered to be the labor embodied in the commodity. His attack on profits is most pointed in the classic statement that "Competition is war and profits are the spoils of war." In the struggle for profits, industries irrationally produce more than can be taken from the market by the extent of profits exacted in the labor bargain. Profits are unjust and a perpetual menace to society, according to his belief.

**Fourierism.** The terrible drama of the French Revolution produced a critic of the social and economic order whose contributions to the ideas of association have caused a grateful posterity to establish him in a place of honor almost as elevated as that accorded Robert Owen. Charles Fourier, son of a cloth merchant, was given a liberal education and a bequest of 100,000 francs which he invested in foreign trade at Lyons. He lost his fortune in the siege of Lyons when the revolutionists used his cotton bales for barricades and his provisions to feed the soldiers. Fourier was imprisoned and narrowly escaped the guillotine in the Reign of Terror.

The chaos and suffering of this great struggle drew Fourier's attention to some of the acute problems of human society. More particularly, his thoughts were directed toward the laws

and institutions which perverted mankind and engendered social discord and evil. His philosophy was based upon the *law of social attraction* which has its origin in three primary and twelve secondary passions universally experienced by man. These passions are the forces emanating from man's soul which give direction and meaning to all human phenomena. Of these passions, one, namely, syntheism, tended to make men cooperate with others in the performance of labor.<sup>12</sup>

The twelve passions form the basis for twelve distinct characters. Through a system of classes, orders, genera, species, and varieties, the twelve characters could be combined mathematically in 810 different ways in different individuals. Maximum harmony prevails in a society in which the optimum number of combinations is reached. It was estimated that communities of 1,500 to 2,000 persons or 300 to 400 families would be necessary to combine characters in the 810 different ways.

Accordingly, Fourier proposed to reform society by organizing communal associations of this size and housing them in magnificent living quarters, the *phalanstères*. The "Palace of Association" was to be the focal point of life in the domain of three square miles allotted to each association. It would contain banquet halls, ballrooms, grand saloons, reception halls, studios, a library, a museum, an enclosed piazza, greenhouses, and a winter garden housing evergreens and exotic plants. The central part of the *phalanstère* would form the social center of the association, corresponding to the four social passions of man. One wing would represent the material side of life or the five sensual passions. In this wing the halls of industry would be located, but only mechanics of a light and refined nature would be permitted and the heavy industries would be separately housed. The other wing, representing the human intellectual element, would provide facilities for the mental training of the associates. A temple was to be erected at the end of each wing, the "Temple of Material Harmonies" corresponding in some respect to the present-day opera, and the "Temple of Unityism" in which the associate would celebrate by rites and symbols his connection with the new social order of universal life and harmony. The observatory, signal tower, and communication system on the roof of the palace would

<sup>12</sup> FOURIER, CHARLES, "The Social Destiny of Man," pp. 6-8, translated by Henry Clapp, Jr., Robert M. Dewitt, New York, 1857.

be used to maintain contact with the outside world and neighboring *phalanstères*.

Each individual in the community would be allowed unhampered freedom for self-expression. The rights of labor were to be respected and property rights in the ownership of shares in the communal property were to be recognized. Surplus earnings, under this grandiose plan, were to be apportioned by giving five-twelfths to labor, four-twelfths to capital, and three-twelfths to talent. All labor was to be made pleasant and rewarded according to grade. The gradations were classified as necessary, useful, and agreeable, the agreeable jobs paying the least.

Fourier prophesied that such abundance of material goods would result from the harmonies in production and the savings effected by the communal mode of life that 10 years of labor by an associate would produce enough material wealth to enable him to live in elegant leisure for the rest of his life.<sup>13</sup>

In brief, Fourierism was a plan to eliminate the friction and evil that result from competition without foregoing the benefits of competition. The introduction of new inventions and machines was strongly advocated because the distribution of industrial products could be equitably arranged. The greater productivity of the workers using improved machines would clearly manifest the superiority of integral cooperation both in leisure time made available to the workers and in the richer material life which all the associates as consumers would enjoy. Unlike other systems of social reform, trade and exchange for profit were not opposed. Fourierism was a plan for decentralizing large city populations and eliminating the attendant evils of urban life, while escaping the isolation and drudgery associated with rural life on family-sized farms.

Fourier waited all his life for some philanthropist who would provide the capital necessary to give his plan a trial. "He announced publicly that he would be at home every day at noon to meet any one disposed to furnish a million francs for an establishment based on the principles which he had published, and it is said that for 12 years he repaired to his house daily at the appointed hour."<sup>14</sup>

<sup>13</sup> ELY, RICHARD T., "French and German Socialism in Modern Times," p. 95, Harper & Brothers, New York, 1883.

<sup>14</sup> ELY, *op. cit.*, p. 85.

After Fourier's death, several attempts were made to establish *phalanstères* in France. Only one, the modified *familistère*, founded at Guise by a manufacturer, Godin, became noted for its accomplishments. Gide and Rist mention the Fourier Communities at Bournville, Port Sunlight, and at Agueta Park in Holland.<sup>15</sup>

In America, Noyes reports, more than thirty Fourierist colonies were organized. The most noted of these was Brook Farm near Cambridge, Massachusetts, which included in its membership such famous persons as Albert Brisbane, Horace Greeley, Charles A. Dana, George Ripley, Margaret Fuller, George William Curtis, Nathaniel Hawthorne, and W. H. Channing.<sup>16</sup>

**Blanc's Theory of Workers' Cooperatives.** It was Blanc who first suggested industrial cooperation. He had little faith in the agrarian Utopias of Owen and Fourier because such schemes, in his opinion, included the control of too many variables in human nature to attain success. After the Revolution of 1848, Blanc found opportunity to project his theory of *the right to labor*. His contention was, that if laborers could not find work, it was the duty of the government to provide them jobs because every human being has the right to happiness. He cited the riot of Nimes, the massacre of Lyons, the revolution of Paris to prove his thesis that competition would finally result in extermination of the proletariat. By the same token, he anticipated the decline of the *bourgeoisie* because all classes in society rise or fall from the same series of causes. "When justice is exercised, all have the advantage; when right is obscured, the whole suffers. A people in one class that is suppressed resembles a man who has a wounded leg. The injured leg prevents him from using the good one."<sup>17</sup>

Blanc suggested that social workshops be organized in order that workmen would own and control the tools, machines, and other instruments of production. He perceived that it would

<sup>15</sup> GIDE, CHARLES, and CHARLES RIST, "A History of Economic Doctrines," translated by William Smart and R. Richards, p. 255, D. C. Heath & Company, Boston.

<sup>16</sup> NOYES, JOHN HUMPHREY, "History of American Socialisms." J. B. Lippincott & Co., Philadelphia, and Trubner & Co., London, 1870.

<sup>17</sup> BLANC, LOUIS, "Organization of Work," translated from 1st ed. by Marie Paula Dickore, University of Cincinnati Studies, Ser. II, vol. VII, no. 1, pp. 12-13, January-February, 1911.

be difficult for any group of individuals to raise the necessary capital and come to a general agreement among themselves in setting up an industrial workshop. In order to make the plan practicable, he proposed that the government assume the responsibility of arranging the "hierarchy of functions" and organizing the *Ateliers Sociaux*. The support and sanction of the government would be merely a temporary arrangement until the workmen became acquainted with one another and were able to select their leaders and direct the enterprises on their own initiative. Blanc believed that the State should provide the initial capital without interest charges and assume the risk of any failures, but other than this, he did not believe in state paternalism. After a number of workshops were established, they could be federated into larger associations which would assume directional control and coordination in the production of particular commodities.

Blanc's enemies planned to discredit his program by authorizing the organization of national workshops to be managed by confederates. The laborers who swarmed into Paris in response to a general call were betrayed, and Blanc found it necessary to flee to Belgium and later to England, to escape the anger of the workers.

Based on the concept of *from each according to his capacity and to each according to his needs*, income from the various enterprises would be divided into three parts: (1) one part of income for wages, (2) another portion for the repayment of loans and the creation of new reserves for capital expansion, and (3) the remainder of profits to be distributed as a supplement to wages. Blanc had no confidence in the theory of the perfectability of man as a basis for reforming society which played such an important part in the systems of Owen and Fourier.

**Proudhon's Objection to the Profits System.** Proudhon, who called himself "the man of the people," foreshadowed Marx and Engels, and contributed very little of direct practical use to the cooperative movement. However, his scathing criticism of rent and profits of capitalists did emphasize some of the limitations of the existing order. Property owners were thieves, contended Proudhon, because they demanded profits and levied rents from properties which they should never have been allowed to own. He disagreed with Kant who argued that because the supply of land was limited, it should be owned. On the contrary, because



the supply of land was limited, it should not be owned. Proudhon had no objection to the ownership of anything if its supply were unlimited.

He observed that through association men were able to produce more than the aggregate total they could produce or acquire if each worked alone in his own individualistic way. The surplus product resulting from association should, he maintained, be kept in a reserve for the use and benefit of society. How Proudhon could induce men to form associations for greater productivity when individual incentives for organization were removed is difficult to understand. The supply of public spirited and socially minded men who form associations for the satisfaction of altruistic accomplishment is limited.

Proudhon's chief positive reform was his advocacy of exchange banks. Labor notes were to be used in these banks as they had been in the Labor Exchanges formed by Owen. Products would be exchanged without the intervention of a medium of exchange and labor would gain possession of the instruments of production.

The critics of capitalism argued for the abolition of property without accomplishing their objective. However, the practical effect of their denouncements was to cause legislative bodies to qualify and limit private ownership of property and to remove some of its more debasing influences.

**Old Ideas of Reform Brought Up to Date.** The French and English critics, undaunted in an age of violence and disorder, challenged the prevailing philosophies with new theories and ideals and laid broad foundations for social reform which is being formulated and advocated by many notable social scientists. For example, some of the reforms of the "New Deal Era" bear a close relationship to the ideas of the early eighteenth century philosophers.

Fourier's back-to-the-land movement has its counterpart in the Subsistence Homesteads and the green-belt garden towns.<sup>18</sup> His "equality of classes in industries of equal rank" was given expression in the parity price formula of the Agricultural Adjustment Administration. Under this formula, all farmers, whether producing products for export or domestic consumption, were to

<sup>18</sup> Green-belt garden towns at Washington, D. C., Cincinnati, and Milwaukee are decentralized modern housing communities in rural areas sponsored by governmental agencies.

receive prices which would give them equal purchasing power. Likewise, industrial organizations leveled out their differences in operating practices under the watchful eye of the blue eagle of the National Industrial Recovery Administration.

The influence of Owen and Sismondi is still felt in the field of labor reform, for the struggle against child labor and the employment of women for long hours at starvation wages continues. The enactment of the Social Security Act and the tightening of laws to make minimum wages, shorter hours, sanitation, safety, and workmen's compensation a reality proceed almost imperceptibly onward toward the goal of Owen and Sismondi. Another instance of precedent established by Owen is reflected in the Pure Food and Drug acts which have been written in state and federal statutes. The defeat of the bill sponsored by Tugwell to strengthen government supervision of food and drug supplies indicates that the battle for this type of humanitarian reform has not been completely won. Undoubtedly, Owen would have approved of the Securities and Exchange Commission established to review the activities of exchange members and promulgate measures for the protection of the investing public against unscrupulous and fraudulent practices in the purchase and sale of securities.

The soundness of Blanc's dictum, "Everyman has a right to work and it is the function of the government to provide work when the laborer is unable to find employment himself," has been acknowledged. The PWA, CWA, FERA, WPA and a host of similar agencies are based on this thesis. "In 1929, government employees of all kinds numbered 7.1 per cent of all wage and salary earners in the United States and got 8.7 per cent of all wages. . . . In 1935, government jobholders made up 9.2 per cent of the salaried and wage-earning population and got 16.1 per cent of all the pay."<sup>19</sup>

Blanc's thesis that the government should extend credit to workmen to enable them to gain possession of property and the instruments of production foreshadows the present government policy of liberal extension of credit. Within recent years, credit has been made available to the American people through the PCA, FCA, HOLC, FHA, and regional agricultural banks.

<sup>19</sup> *Barron's*, vol. 16, no. 48, p. 10, Nov. 30, 1936.

Thus, in this period of acute economic distress the forces of government made many needed adjustments, which under the laissez-faire system of economy would have required a long period of time to equilibrate.

#### THE SYNTHESIS—COOPERATIVE ACTION

Cooperation is a synthesis of the laissez-faire system of economy and of a planned economy. It is an attempt to combine whatever is good in both economies while eliminating the undesirable features inherent in each of them. It cannot be resolved into aspects of either of the systems. It is a direct challenge to the private profit system. Its natural range of application or latitude extends from a position in which private initiative and freedom of action are preserved in a large measure to one in which the member sacrifices some individualistic functions in coordinating his efforts with others to attain certain ends. Group interests are recognized as superior to individual interests. Theoretically, the form of organization and the principles of operation preclude any individual from attaining these ends at the expense of a fellow member. Group action may result in progress, inertia, or regress, but the movement is always unified and each member shares in the fortunes of the association in proportion to his contributions. The general objective of association is to improve the status of mankind in a manner superior to that attainable under other economic systems. The plane of living is to be elevated through collective action and collective responsibility rather than through individual effort as laissez-faireism proposes. A few of the immediate problems which cooperators have sought to solve by association follow:

To harmonize production and consumption

To avoid duplication and waste of human resources

To prevent men from exploiting one another by directing their activities in such a way that each mutually improves the status of the other

To eliminate idleness and dissipation

To assure the benefits which result from combined effort for the general welfare of society

The manner in which the synthesis can be effected, its nature, scope and potentialities can be best understood by a study of the

principles of association. These form the subject matter of the next two chapters.

#### Questions

1. Summarize Adam Smith's plan for augmenting the wealth of the nation.
2. Do the doctrines of the Physiocrats encourage associated effort?
3. Define *produit net* and explain its limitations as a concept applied to agrarianism in America.
4. Enumerate the main points in the mercantilistic program of the eighteenth century.
5. Is there any need for a planned economy today?
6. Who was Robert Owen, and what did he contribute to the cooperative movement of the nineteenth century?
7. Describe Fourierism and evaluate its influence upon cooperativism in America.
8. What was Louis Blanc's criticism of the agrarian Utopias?
9. In what ways do the critics of the social and economic order of the twentieth century agree with those of the nineteenth century?
10. If cooperation is a synthesis, what are its components?

## VI

### *Principles of Cooperative Sales Associations*

*This nation is the experimental laboratory of the world for the cooperative movement. A combination of attributes—rich natural resources, a people imbued with the venturesome spirit of the frontier, and a government permitting and encouraging the organization of business—has contributed to this distinction.*

*Out of a maze of isolated trial-and-error experiments, certain laws become recognized as essential to the development of cooperative associations. These laws are called "principles," and principles differentiate the cooperative form of business from private enterprise. In order to grasp their full significance in relation to the cooperative movement one must distinguish between principles and practices.*

*The one thing that is certain in life is change, and changes affect the principles of institutions. The tempo of these changes at times is quickened and their effects are often profound and far reaching. Principles are affected by the social enterprises of a people, by their political alliances and actions, and by their strifes and struggles for economic power. Several of the most important principles are given in this chapter. This list is not to be regarded as conclusive, but rather as a starting point from which other principles may be recognized and used.*



CHAPTER VI  
PRINCIPLES OF COOPERATIVE SALES  
ASSOCIATIONS

Innumerable forms of cooperative organization have originated and thrived in American communities. The development has been entirely on a voluntary basis and for the most part spontaneous and sporadic. By complying with simple statutory requirements, any small group of individuals may form an association. During the past half century this freedom from restrictions upon group initiative has not been without its advantages. The heterogeneous groups attempting collective action in various branches of industry and agriculture have occasionally hit upon a plan, a method, or an idea of practical value. In the absence of a coordinating agency, however, many good ideas have not had as wide currency as they deserved. The rudiments of the movement are far from being universally known and understood.

A movement which advances by chance through the trial and error method may become self-centered in a coterie of professed practical managers. Often little toleration is shown for the introduction of ideas originating from theoretical speculations. This is expressed in the laconic assertion, "That may be all right in theory, but it won't work in practice." The relevant point is that an original idea probably will not work in practice unless it is all right in theory. One writer asserts that there is nothing so practical as a good theory and defends this point by stating that "the whole foundation of science and engineering, upon which our [civilization] rests, is simply well-developed, soundly analyzed, and carefully checked theory or generalization."<sup>1</sup>

If any of the subject matter on cooperation has suffered inattention, it is that part concerning the theory of the movement. Confusion has resulted from failing to recognize the principles upon which cooperative associations are founded. Just what

<sup>1</sup> Nourse, E. G., *The Evolving Idea of Cooperation in the United States*, "American Cooperation, 1928," vol. 1, p. 13, The American Institute of Cooperation, Washington, D. C.

constitutes a principle is not easily discerned, and principles are frequently confused with practices. The principles of cooperation are the basic concepts which determine the sphere of collective action. Generalizations as to the elements indispensable to a particular type of enterprise are drawn from a vast field of successful experiences in cooperative effort. Principles are derived from these generalizations by the process of logical reasoning and are verified through tests of broad application.<sup>2</sup>

The layman ordinarily thinks of practice as being the manner in which tasks are performed. All businesses, whatever their form of organization, may resemble one another in their accepted business practices.<sup>3</sup>

<sup>2</sup> Several encyclopedic sources show that the word "principle" has been broadened from its original meaning and has undergone changes in usage since the time of the Greeks. In their search for truth, the Greek Philomaths endeavored to trace things to their origin. To them the original term *ἀρχή* meant "the source of all things" and imparted the idea that everything emerges from a primary concept. The encyclopedist refers to this mental process as "the Grecian constitutive sense of objective reality." In later times the logicians used the term "principle" to connote a summary expression of their generalizations. Careful observations of phenomena disclosed certain similarities which in time were classified and interpreted into laws or principles from which deductive reasoning proceeded. Similarly the moralist derived laws which purported to explain the factors that control the conduct of human beings. This interpretation of the word "principle" might be referred to as "normative" in that it brings under one concept the effects of causal elements. In modern times the word "principle" has fallen into a general and indefinite use expressing a broad truth or apparent law.

The most common use of the term in the social sciences, however, is the metaphysical one. Here it has the advantage of combining the various meanings given it from ancient times to the present: the "primary element" idea contributed by the Greeks, the "determining cause" as conceived by the logicians, and the "regulating law" of contemporary usage.

<sup>3</sup> Note that some of the practices commonly used by American cooperatives are not distinguishable from those of private business corporations:

1. Building up efficient local units
2. Using business records and accounts
3. Commingling the products according to grade or other common characteristics
4. Encouraging products of better quality
5. Branding products with a trade name
6. Advertising when necessary to stimulate sales
7. Organizing sales areas and establishing representatives in the most important markets

Many of those who adopted the cooperative method of selling farm products prior to 1900 did so without knowledge of the experiences of existing cooperative groups. Some were also oblivious of the development of consumer societies in the Old World. Voluntary associations were precariously organized. In organization and management they had no special technique; they simply imitated the practices of private business organizations with the important modification that the gains or advantages should accrue to those who participated in the enterprise. Cooperative effort was confined largely to the performance of simple tasks within restricted areas of production. After a period of approximately 20 years of experimentation, accepted practices in the operation of local associations were quite generally understood.

Since 1915 the movement toward federation of local associations into district and central associations and the gradual integration of marketing services have made it necessary to experiment on a greater scale. Communication between cooperative groups in various parts of the country brought to light approved practices. After these practices had been generally applied under varying conditions in different parts of the country, they came to be recognized as fundamental to success and were analyzed for the attributes which would merit their recognition as principles. It is conceivable that certain practices inaugurated by cooperative associations may fall into a twilight zone between accepted principles and general practices, and in the course of time, what may now be considered a practice may become a principle. The effect of time, as well as other influences at work in society, must be taken into consideration in the evolution of principles.

Once principles are definitely established, they provide a base from which untried practices may be tested for potential possibilities. If a new practice is not contrary to any of the established principles, it may be subjected to trial, but if it is in direct violation of some established principle, an attempt to carry it out may be inadvisable except by associations favorably situated and capable of prosecuting an experimental program.

In any business the first principles that are established are most likely to be broad in their application, perhaps because they are the obvious and most easily discovered principles of



the business. When the list of principles is extended, however, their application may become restricted to specialized spheres of activity. As time passes changing economic conditions may cause some principles to be modified or discarded. The test of the validity of a principle is: (1) Does it describe and define the basic and essential characteristics of a particular system or type of organization? (2) Can any organization function more efficiently with a particular principle than without it?

Writers on the subject of cooperation usually present a list of principles which they regard vital to the movement and include a few or all of the original precepts of the Rochdale Pioneers. Some lists contain summaries of the aims, purposes, and objectives of cooperation as they are conceived by the particular writers. In appraising the cooperative movement here and abroad, we present as basic principles of *producers'* cooperative marketing associations:

1. Membership selection
2. Functional and commodity specialization
3. Democratic representation
4. Services at cost
5. Savings prorated to members on patronage basis
6. No unusual risk assumption
7. Attitude of nonpartisanship and nonsectarianism
8. Dissemination of information to membership
9. Control or ownership of marketing facilities and institutions

#### MEMBERSHIP SELECTION

To be most successful the sales type of cooperative association requires close coordination of the production and distribution of goods. Growers' responsibilities and risks are increased by cooperative undertakings. The satisfactions or sacrifices and the gains or losses, which may involve a large part of individual net incomes and returns on capital investments, may be in direct proportion to the participation of each member in the enterprise. For these reasons members must qualify as producers and cooperators, and membership selection is an outstanding principle of cooperative organizations.

The process of selection goes on even while an association is being formed. The producers become members either upon their own initiative or upon the invitation of fellow producers,

and the confirmed individualists elect to maintain their independent status. There are few cooperative organizations in this country that have as members all of the producers in the community. Although producers in the California citrus industry have, with unprecedented success, handled their own products since 1893, 15 per cent of the growers have not affiliated with either the California Fruit Growers' Exchange or the Mutual Orange Distributors. These individuals are undoubtedly happier on the "outside" and the associations may be fortunate in having them there.

The most ideal condition under which a cooperative may be operated is that of having an intelligent membership of efficient producers who recognize the need for organization, who have the patience to work out their problems, and who will give the necessary support to the employees and management of the enterprise. A selective membership policy does not make the individual the sole determiner as to whether he shall become a member. He must "pass muster" to those who are in the organization.

Not all men make good cooperators. It is only wise policy on the part of an organization to eliminate those who give trouble and cause the association unnecessary inconveniences. When the management has control over membership relations, it may for good reason call upon particular members to show cause why their connections with the association should not be terminated. This procedure usually has a wholesome effect on the morale of the entire organization. Membership in an association under these circumstances becomes a privilege.

When a new association is being formed, there is no formal means of selecting and excluding petitioners for membership. Many of those who assume the responsibility of forming new organizations visualize might in numbers and are prone to use the dragnet in their zealously to build a powerful organization. Especially is this true where professional solicitors are engaged to promote an association, with commissions based on the number of members obtained. An open-door policy is subject to criticism because it admits irresponsible individuals, chronic kickers, and agitators who disconcert the loyal members. Internal troubles break out sporadically and are a constant source of expense and destruction to associations.

Not all organizations can follow a selective membership policy, either because they lack the information necessary to make intelligent selections or because they require additional business to lower their marketing costs. The general procedure in the development of a cooperative is to begin with an open membership policy and to shift gradually to some plan for selecting and choosing new members. Limitations and qualifications for participation in going cooperative concerns are designed to give the association more complete command over its affairs.

Membership may be limited by receiving applications only during specified periods, prior to planting or harvesting, each year or in such years as the association may choose. This device is effective in that it prevents "fair weather" cooperators from taking advantage of an association by following an "in-and-out" policy, joining when conditions are favorable and dropping out when they are unfavorable. No cooperative could succeed with such opportunists.

Some associations control the influx and the exodus from their organizations by rules concerning withdrawals. The California Walnut Growers' Association requires that a member who has withdrawn legally must remain outside the association at least two years, when his readmission will be at the discretion of the directorate, and that one who has withdrawn illegally must remain outside the association three years or more. Everyone who withdraws may temporarily lose his equity in the reserves which he has helped create, because the welfare of the association is placed above that of any individual producer when reserves cannot conveniently be allocated and distributed.

The language of the membership agreement may be indicative of the policies followed by an association respecting the selection of members. In most stock associations the transfer of common stock is controlled by the board of directors. The directorate reserves prior option to buy for the association or the right to recall the shares of any stockholder, providing this right is exercised within a stated time and subject to conditions and limitations stipulated in the stock subscription agreement or the bylaws of the association. If an association has considerable control over the product handled and is relatively independent, it may permit members to terminate their connections with it easily but make access to the association difficult. This policy has the

psychological effect of attracting members and making them reluctant to sever their connections.

In the absence of well-defined policies relating to membership selection the group may resort to the undesirable practice of making distinctions between members in the organization. The management sometimes shows preferences in the services and considerations which it extends to certain members or groups of members. The personalities and counsel of some influential members may govern to a considerable extent the adoption of new ideas which affect all members. The control of minor offices may be kept within esoteric groups. These practices discourage rather than promote cooperation.

#### FUNCTIONAL AND COMMODITY SPECIALIZATION

In a simple economy, exchange was effected by barter between two persons without the assistance of a middleman or the use of money. When the use of money as a medium of exchange was introduced, the market for certain goods was enlarged and middlemen made their appearance to bridge the distance between producers and consumers. Subsequently new inventions and improved machines made possible greater divisions of labor and increased productivity. Each new advance in production required an extension of the market and a greater number of middlemen to perform the services of distribution. Improved roads and new vehicles of transportation permitted the sale of goods many leagues from their point of origin. The distance could no longer be traversed by one middleman, so the work of marketing was divided into stages comparable to some of the functions known today as country buying, wholesaling, jobbing, and retailing. As the problems of making sales became more complex, each of these major functions was divided and subdivided into more minute fields of specialization. The main problems that arose and still exist from this competitive system of marketing are the difficulties of coordination to prevent waste, duplication, and excessive charges. On the basis of private initiative middlemen do not seem capable or are not willing to specialize to the extent desired by large manufacturers. For this reason large industrial corporations have, in general, integrated the functions ordinarily performed by middlemen, and now provide

specialized services and control the distribution of their products from factory to consumer.

The limitations of the services by private middlemen have been even more striking in the marketing of agricultural products than in the distribution of industrial products. These are occasioned possibly by the nature of the products and their geographical distribution. Specialization in both production and distribution was late in making its appearance in agriculture. Where large corporations, such as those of the millers, meat packers, and cheese processors, have integrated the functions of marketing, the financial advantages have stopped short of the producers' pockets. Since the beginning of this century, farmers have developed a superior type of marketing technique, the cooperative organizations, which are the counterpart of the industrial corporations. Despite many failures the cooperatives' record of achievement often has surpassed all expectations.

Farm leaders have been divided in a controversy relative to the correct method of organization for marketing farm products. The theory of one group is that an association should confine its activities to one commodity or a group of closely allied commodities in order that all the advantages of specialization may be gained. The other group maintains that an association should handle a variety of commodities commonly purchased and sold in the community. The Oregon Cooperative Council was organized in 1921 as an outgrowth of such a controversy. Officials and directors of the commodity sales associations were apprehensive of a movement in the state which proposed to set up local cooperative exchanges dealing in various and sundry products. According to this plan the local associations were to be affiliated with a state exchange. The council went on record as opposing this plan because it feared that the whole scheme would fail, involve heavy losses, and permanently injure the cause of cooperation in the state.<sup>4</sup> The experience of various sales organizations to the present time indicates that associations confined to the handling of one commodity, or closely related commodities as poultry and eggs, apricots and prunes, oranges and lemons, have been most successful. The marketing of a single commodity presents an array of problems complicated

<sup>4</sup> MARIS, PAUL V., "History of the Oregon Cooperative Council," a mimeographed report.

enough to tax the ingenuity of an alert board of directors and an expert staff headed by a proficient manager.

In the diversified farming areas of the middlewest or the north-eastern states some of the possible combinations are two or more of the following enterprises: dairying, poultry raising, fruit growing, truck gardening, livestock feeding, and a number of supplementary enterprises such as bee keeping, fur farming, and ginseng growing. Like the farmers in Denmark, producers may find it necessary to belong to three or four cooperative associations, each handling a different commodity. Diversified farming requires the assistance of highly specialized marketing organizations which will provide technical information about production as well as market prospects for the various crops ordinarily grown in the area. Without market organizations, specialization in production quickly lapses into a quiescent state.

The single-crop farmers in the tobacco and cotton producing areas of the south, wheat areas of the northwest, or the grazing regions on the plains and plateaus adjacent to and in the Rocky Mountain Range stand in great need of organizations to reduce the risks, accurately grade, weigh and classify the products, discourage excessive numbers of middlemen, and reduce market costs by concentrating volume in a few associations. It is as necessary for the many producers to coordinate the sales of products for each specialized area as it is for the individual farmer to maintain the proper balance and relation between the different crop incomes on his farm. Specialization in agricultural production requires that market organization tend toward rather than away from specialized services.

#### DEMOCRATIC REPRESENTATION

No principle has the influence of time more clearly impressed upon it than this one. Its origin is political in nature. The revolts against monarchical despotism and rule by hereditary succession in the latter part of the eighteenth century resulted in the formation of new modes of government. Since the American Revolution the people of this country have been committed to the cause of democratic government, which grants all citizens equal privileges of participation in the affairs of state. Citizens reserve freedom of expression that they may defend themselves against oppressors, safeguard their rights, protect their property,

and extend to all citizens the security so necessary to the promotion of their peace and happiness.

The dependency of communities and countries upon commercial intercourse makes control and coordination in business almost as important as in government. Consequently, it has become the practice of government to gradually invade the economic field. The phenomenal growth of capitalism and the inevitable drift toward the concentration of wealth have resulted in the domination of capital over industry and laborers, from which the agrarian and working classes have sought to free themselves. They have found this freedom in the cooperative association.

The three barriers against capitalistic control in a cooperative are:

1. Limited voting power
2. Limited number of shares per member
3. Limited interest paid for capital

One or more of these is included in every enabling law. The Capper-Volstead Act provides:

First, That no member of the association is allowed more than one vote because of the amount of stock or membership capital he may own therein: *or*

Second, That the association does not pay dividends on stock or membership capital in excess of eight per centum per annum.

It is commonly thought that all associations must or should provide equal voting privileges. The cooperative statutes in thirty-five states provide that no member shall be given more than one vote, irrespective of his financial interest in the association or the amount of produce delivered.

In some cases the one-man, one-vote principle hinders the growth of cooperatives because large growers maintain that they are unwilling to grant small growers the right of fully controlling the handling of their own products together with part of the products of large growers. Other groups of producers do not regard differences in their economic status significant enough to require a departure from this principle. Consumer groups particularly may regard any changes affecting their individual rights as jeopardizing the whole cooperative movement. Those who justify the one-vote method of control in cooperative associa-

tions assume that it is man, not money, that is most important in the government of cooperatives, and they desire that personal rights be placed above property rights, as they are in all true democracies.

In some agricultural areas of the United States the variations in the size of farms, volume of products sold, or the economic status of individual farmers are considered so significant that members make special provisions for unequal representation. They choose the second alternative of the Capper-Volstead act which does not permit the stockholder to profit at the expense of patrons or dissipate savings by paying more than the necessary amount of interest on stock to cover the risk involved.

Stokdyk and Cerini of the Bank for Cooperatives in the eleventh district, including the states of Arizona, Utah, Nevada, and California, examined the articles of incorporation of approximately 100 cooperative marketing associations in that district and found that only 42 per cent of these associations provided for equal voting power. The remaining 58 per cent gave members unequal voting power which was generally based on patronage, 37 per cent being associations with a capital stock structure and 21 per cent being membership associations. In the association which permits its members to vote on the basis of patronage, representation is usually determined by the units of products delivered or dollars' worth of business, additional votes being given for each 10 units or \$10 worth of business, or multiples thereof. Some fruit associations provide additional votes on the basis of 100 packed boxes, and some wineries on the basis of 10 tons of grapes. Poultry associations use dozens or dollars as criteria for additional votes, either one vote per 1,000 dozen eggs delivered or one vote for each \$1,000 worth of eggs and poultry sold through the association. The majority of associations do not limit the number of additional votes given any one member, but a few associations take this precaution when it is feared that too much power may be given to the largest producers.

The California nonstock cooperative law passed in 1929 provided for unequal voting power and unequal property rights and interests of individual members in an association. The present law which is applicable to stock and nonstock associations, Sec. 1196, reads:



The articles of incorporation of any such association shall state:

*e.* If organized without shares of stock, whether the voting power and the property rights and interest of each member are equal or unequal; and if unequal, the general rule or rules applicable to all members by which the voting power and the property rights and interests, respectively, of each member may be and are determined and fixed; and provide for the admission of new members who shall be entitled to vote and to share in the property of the association with the old members, in accordance with such general rule or rules.

*f.* If organized with shares of stock, . . . If the shares are to be classified, a description of the classes of shares and a statement of the number of shares of each kind or class and the nature and extent of the preferences, rights, privileges, and restrictions granted to or imposed upon the holders of the respective classes of stock; and except as to the matters and things so stated no distinction shall exist between said classes of stock or the holders thereof. One class of stock shall always be known as common stock and voting power may be restricted to holders of common stock.

Legal sanction to abandon the one-man, one-vote principle has obviously met with popular approval in California because approximately 50 per cent of the associations in that state are now operating on the basis of unequal representation, and the probability is that this percentage will increase in the next few years. In addition to California there are 12 other states which permit the cooperators to modify this principle at their discretion.<sup>5</sup>

#### SERVICES AT COST

Cooperative business is conducted at cost and without profit; private business is dependent upon a margin over and above the costs of rendering sales services. This difference in the principle of operating a cooperative as compared with a private business is sometimes succinctly put in the assertion that "cooperatives always pay what they *can* but proprietary businesses only pay what they *must*." It is not implied in this statement that private businesses are not entitled to profits; they must make profits to offset the losses of buying and selling transactions, as well as to adequately compensate the entrepreneurs for their work and worries. "We're not in business for pleasure," is a current saying

<sup>5</sup> These states are Colorado, Delaware, Florida, Kansas, Michigan, Missouri, Nevada, New Hampshire, New Mexico, New York, Oregon and South Carolina.

among businessmen. In contradistinction to private business enterprises, cooperative services are rendered by a personnel receiving wages, not profits, and the cooperative has first claim to the proceeds from sales to cover its actual operating costs.

It is impossible, of course, to ascertain the exact costs of any transaction. The aggregate costs over a period, usually the fiscal year, are allocated to the different services. Many cooperative contracts specify what shall be construed as costs and limit the amount of the deductions. The power to arbitrarily allocate some costs is reserved for the directorate. This permits latitude in initiating needed programs of reform, in producing better quality, more scientific handling, or expert selling that might otherwise never be attempted because the members may lack the courage to make such changes in operating methods. It is imperative that the management charge an amount large enough to cover all costs and avoid the mistake of attempting later to collect the additional marketing costs from its members by making large deductions or levying assessments. The operation of a cooperative purchasing-type association, which buys and sells goods as differentiated from the sales type, is contrary to this procedure. Like private businesses, they must make profits to cover any losses. This mode of cooperative business is discussed in the next chapter.

In a new association where cost figures are not available, the manager should estimate as accurately as possible the volume of products to be handled and the costs that will be incurred. Information from membership agreements, the number of prospective patrons, assessors' reports, census data, or other acceptable sources may be used in judging the expected volume. On the basis of these figures an approximate unit cost can be determined and a flat deduction charged for services rendered. In established associations, the approximate unit costs of doing business are known from past experience, and larger initial payments or advances can be made to the grower members without assuming great risks.

In estimating the funds available for expenses, sources of incidental income may be ignored. Incident to the marketing of a particular product an association is wise to develop as many sources of income as possible so that its budget may be balanced. If the income from the various activities of an association exceeds

the amount anticipated, it is a pleasant task to distribute them to members or assign them to some needed reserves. The next principle, a corollary to the one of services at cost, deals with the general theory of distributing savings which may accrue in well-managed cooperative sales associations.

#### SAVINGS PRORATED TO MEMBERS ON PATRONAGE BASIS

The financial gains which accrue to cooperatives in the ordinary course of business transactions are variously termed profits, net earnings, surpluses, or savings. It may seem incongruous to refer to cooperatives as nonprofit in character and at the same moment be giving serious consideration to the problem of equitably distributing their savings. It is not what these financial gains are called but how they are apportioned among those who created them that is significant. The nature of cooperative savings becomes apparent when one considers some of their sources:

1. Delayed pool settlements. Frequently it is desirable to inventory goods and arbitrarily fix a settlement price on the quantity in order to avoid interminable delays and minute payments to producers. Later sale of the produce may net the association a surplus.

2. Unspent deductions for marketing. When a flat charge is made for each unit of the commodity handled, a surplus may accumulate over and above actual costs.

3. Opportunity transactions. Associations may stimulate sales beyond their capacity to fill orders. When this occurs, profitable purchases may be made in the open market to fill the orders they receive. Giving service and keeping the good will of customers may be the incentive rather than the pursuit of profits in transactions of this kind.

4. Recovered damages and claims on rejections. Surplus may arise from claims against railroads for damage to goods in transit or from buyers where adjustments on price have been delayed pending inspection.

5. Handling of supplies. The general practice of cooperative associations to engage in the business of purchasing supplies which are incidental to the processing, packing, and marketing of the commodity often provides a lucrative source of income.

The laws of various states provide methods of distributing earnings. The usual procedure is first to pay interest, limited by the Capper-Volstead Act and most enabling laws to 8 per cent, on the capital investments of members. A number of states provide that a given percentage of earnings must be placed in the reserves of the association until they equal a proportionate part of the capital investment. The association may next exercise an option to set aside a given percentage for an educational fund. Some states provide that part may be paid to the employees in the form of bonuses on wages and salaries. After these distributions, the remainder may be given to the patrons on the basis of business transacted, according to either the value of the products delivered or the number of units sold through the association. Whether nonmembers are to receive a patronage dividend is left to the discretion of the directors. If a cooperative wishes to qualify for exemption from the payment of federal income taxes, it is necessary to treat members and nonmembers alike with regard to patronage dividends.

It is of interest to note that emphasis was given to the importance of business surplus in sales cooperatives during the first two decades of the century. The Wisconsin cooperative law of 1911, which was used as a model by sixteen other states, included a provision which made it incumbent upon an association to realize a business surplus and distribute same:

If such association, for 5 consecutive years shall fail to declare a dividend upon the shares of its paid-up capital, five or more stockholders, by petition, setting forth such fact, may apply to the circuit court of the county, wherein is situated its principal place of business in this state, for its dissolution. If, upon hearing, the allegations of the petition are found to be true, the court may adjudge a dissolution of the association.

This section was omitted from the Wisconsin law when it was revised in 1921 because it was regarded as incompatible with the spirit of cooperative enterprise.

The distribution of savings concerns purchasing cooperatives more than it does marketing cooperatives. The reason for this is that more than 70 per cent of the large-scale marketing associations of the country use the agency-type contract and confine their transactions largely to those of making sales for growers. Products are not purchased and resold. The impact of competi-

tive force is more direct in cooperative sales associations, or producer cooperatives, than it is in consumer cooperatives because competition is focused upon each transaction. Very shortly after the transactions, when costs have been determined, returns are made to growers. Most cooperative sales associations find it necessary to make these returns as large as possible, after covering the costs of operation, in order to hold their patrons. Consequently, very little is left at the end of the year to be divided among the members. In some communities, however, where the cooperatives have considerable control, the management may set aside fairly large incidental earnings to be distributed late in the fiscal year. This is a desirable procedure from the standpoint of minimizing risk, maintaining membership morale, and creating general satisfaction with the services of the association.

#### NO UNUSUAL RISK ASSUMPTION

Many cooperatives, especially the local associations, do not build out of earnings large reserves to be used as protection against losses. They are not designed to assume risks other than those associated with the physical handling of the commodities. Many of the losses arising from the risks of transportation, industrial accidents, dishonest employees, explosions, fires, floods, and tornadoes might be covered with insurance.

Considerable risk is assumed by holding title to and financing goods during the period of time that elapses between transactions. In the past quarter century some cooperative associations have made the serious mistake of attempting to perform the service of risk bearing by making outright purchases from farmers and later selling the products on a declining market. Cooperative sales associations have found it advantageous to use the agency-type contract which relieves them from assuming unnecessary risks in handling agricultural products.

The assembling and wholesaling of agricultural products involve greater risks than those assumed in distributing most manufactured products. The reason for this is that agricultural products are perishable, bulky, and widely diffused in production; they lack uniformity in quality, size, and shape, and require considerable refinement before being presented to the consumer. The services of assembling and wholesaling involve the handling

of large quantities on relatively smaller margins than are customary in the retailing business.<sup>6</sup>

For centuries the farmer has relied upon middlemen to assume the ordinary risks of marketing his products. At first the quantities produced in excess of the needs of any local community were not sufficient to justify an elaborate organization for distribution. Marketing was a seasonal business of small proportions in which individuals found it relatively easy to establish themselves. As specialization in agricultural production spread, the function of risk assumption became indispensable. At first middlemen combined all the services of marketing including risk assumption. Later those who were more proficient in assuming risks, namely, speculators, began specializing in this function alone. Except in the handling of a few agricultural commodities the function of risk assumption has not been refined to any marked degree. In the highly organized produce exchanges, the function of risk bearing assumes a professional status and the traders are specialized to the extent that they may be classified as speculators, manipulators, or traders. Because the risks in handling agricultural products are great, the primary producers have been forced to pay rather dearly for the services of risk assumption. The risk bearers have always acted on an individual competitive basis, and their activities in the organized markets have been the most bitter bone of contention among agrarian reformers. The whole market system has been condemned because speculators were able to make profits without performing apparent services. Probably no single factor has furnished farmers a greater inducement for reform in the markets than this one.

Cooperative associations provide means for producers to assume the ordinary risks of marketing their products. They minimize the risks which the individual producers assume by reducing the number of transactions between the primary producer and the final consumer and attempting to stabilize the market. Where there are fewer transactions there are less

<sup>6</sup> In the operation of cooperatives the association imposes upon itself certain functions involving more than the usual risks of marketing, such as a grain elevator which does not hedge its purchases. Under good management and strict adherence to accepted principles, these risks need not be assumed.

opportunities for private middlemen to manipulate prices or "rig" the market. In pooling large quantities of produce, the cooperatives spread the risks that result from temporary inequalities in the markets and reduce the per unit costs of handling. Large sales associations have succeeded in spreading risks and minimizing the costs of this service appreciably.

#### ATTITUDE OF NONPARTISANSHIP AND NONSECTARIANISM

American cooperatives have generally tried to avoid taking a partisan stand on political and religious issues to such an extent that an unbiased view is generally considered one of the principles of the cooperative movement. *Esprit de corps* among members is essential for cooperation. In order to create and maintain a harmonious spirit, political and religious controversies cannot be permitted to cause dissension. The danger of taking issue on legislation affecting banks, internationalism, war debts, and other problems outside its immediate economic functions is that friction and division of membership may result. The sales-type associations are less likely to participate in political party leadership than the purchase-type associations. Because of their degree of economic specialization, cooperatives have a distinct economic objective which is not subject to compromise. A political party, on the other hand, can achieve success only with a constant give-and-take between the leaders of the party and its adherents. Its vacillating methods would be dangerous, if not fatal, to this type of movement.

It is almost certain that a cooperative will become subservient to the political party from which it seeks favors if it is definitely allied to it. It is, moreover, a foregone conclusion that if a cooperative binds itself to the losing partisan group, it will suffer through loss of prestige or adverse legislation.

Neutrality on the part of cooperatives does not suggest a lack of interest in the affairs of government. They fully recognize that economic activity is influenced either beneficially or detrimentally by political action. In accordance with this, the Danish cooperatives draw up a platform to be approved by candidates for political office. Each candidate is informed of the wishes of the cooperative movement, the legislation it desires, and the appropriations it needs. The greater the number of parties or candidates for office subscribing to these requests,

the greater is the likelihood that the cooperative will get such legislation enacted without itself taking a partisan political stand. As a result, candidates of all parties, anxious to obtain the support of the cooperative membership, readily endorse its proposals. The cooperative informs its members which candidates and parties approve of their program without presuming, however, to tell members how they should vote. A cooperative can be motivated by ethical idealism without resorting to denominationalism. It is a nonsectarian organization and should retain a neutral stand on all issues relating to religion.

#### **DISSEMINATION OF INFORMATION TO MEMBERSHIP**

The free and uninterrupted flow of information is vital to collective action. In any organized body where the optimum functional coordination is required, there can be no obstructions in the communication system through which directions are given to each related part. Whenever anything happens which seriously disrupts the transmission of intelligence from one mutually dependent part to another, it paralyzes or cripples those parts of the organism and may cause serious consequences to the whole. In marketing organizations it has been demonstrated that the best results are obtained when all available facts are collected without delay, properly interpreted, and quickly passed on to all those who may benefit from the information. Intelligent action on the part of any group is dependent upon its power to assimilate available facts. Without simplification and interpretation, some information concerning production, processing, or marketing may be difficult to understand because the individuals have had no previous experience. Intelligent action also depends on the total number in any group. It is more difficult to educate a large group than it is a small group of equally intelligent individuals. The difficulties of contacting a large number of people living in various communities retard the coordination of the group.

The government maintains a market news service which is intended to assist buyers and sellers with information that will result in the determination of prices which are consistent with conditions of supply and demand. Large market associations find it necessary, however, to supplement the news services of the government by collecting from various sources additional



information relative to production, consumer purchasing power, and existing and potential market supplies. Individual entrepreneurs and organizations with limited resources are usually unable to provide this service for themselves, much less for others. The market made up of private corporations and individuals is characterized by stages or independent segments for the performing of particular functions. It is almost impossible to arrange complete and free exchange of information between these units. The representatives in each stage, particularly the wholesalers, spend large amounts of money annually in the collection of information in order that they may reduce risks and conduct their business as efficiently as possible. Since the wholesalers and other large assemblers of information in the market system are not motivated by the same objectives as cooperative associations, they reserve the right to decide which information shall be communicated to and which shall be withheld from those with whom they are bargaining. The entrepreneurs assume no responsibility for educating producers to better assimilate the information they possess. When possible, they create a psychological situation favorable to the entrepreneur who has the information.

Since agricultural producers have learned to integrate marketing services, they appreciate the importance of the wholesaler's position in the market system. A great number of the cooperative associations of the country have not integrated their marketing system beyond the rendering of wholesaling services. The reason for extending their system through wholesaling services is to make it possible to pass information toward the producer or consumer and cooperative associations which are designed to render such services have generally followed the practice of interpreting data and providing information needed by producers. In some instances cooperatives have done much to facilitate distribution by informing consumers about producers' problems and commodity characteristics.

#### CONTROL OR OWNERSHIP OF MARKETING FACILITIES AND INSTITUTIONS

Although agricultural producers as a class are not reputed to be affluent, they are numerous and possess some capital which they are usually willing to invest in their own business

enterprises. If and when they choose to combine small amounts of capital contributed by a great number of individuals, the accumulated wealth may build institutions which provide services that compare favorably with those of any organization erected through the efforts of individual entrepreneurs or even those developed by private corporations. This is especially true when one takes into consideration the assistance which farmer groups may obtain from special credit institutions such as the regional cooperative banks, which assist cooperative members in acquiring ownership of marketing facilities. Agricultural producers generally have a larger proportionate share of their total earnings invested in their cooperative enterprises in the form of cash and commodities than individuals hazard in private corporations through investments in capital stock. The principle of democratic control invests producers with the right to direct the operations of their organization. These two conditions are of much import to producers because they provide the basis for setting up a powerful business organization. At the moment producers initiate a program for the ownership of their marketing facilities, they can act more securely in their own behalf. They develop an enclave within a competitive system. They use social capital to combat private capital.<sup>7</sup>

It is imperative that any group acting within a capitalistic system take the precaution to surround itself with the same protective devices used by the capitalists for their perpetuation and self-preservation, namely, the rights of property. An organization cannot under any circumstances make itself dependent upon its enemies for the very thing which gives it the freedom and power of an independent entity.

Once producers have decided to own their facilities an additional investment outlet is provided, where the surplus earnings of agriculture may be devoted to the services of agriculture. In the past farmers have been prone to re-invest their capital earnings in land, overcapitalizing it in anticipation of prospective future values or improved market outlets. The acquisition of capital goods in the form of operating capital and facilities gives the farmers economic power over the services of others. The

<sup>7</sup>The term *social capital* usually connotes the total of all products and services made available to a community within a given period. Here the term is used in the narrower sense of *within a cooperative group*.

personal services which are purchased may be directed in their interest and for the welfare of the group. This is in contrast to a market system which directs its employees as so many pawns against the interests of the producers.

The collective ownership of facilities may be properly regarded as control of social wealth to be utilized by any members of society who can meet the cooperatives' membership requirements. The main objective is to control facilities in order that the cooperative may fully and completely regulate all its activities and displace those who assume that they possess a vested interest in the markets through seniority rights.

#### PROBABLE TREND IN PRINCIPLES

It has been stated that the practices inaugurated by cooperative associations may be an indication of what principles will prevail in cooperative associations in the future. Judging from the present trend of affairs, there is in the offing the shadowy outline of a principle which seems to be taking shape in the idea of economic control or a planned economy. This supposition is grounded upon the apparent willingness of American cooperators in some quarters to voluntarily submit themselves to more control and direction than they have at any previous time in the history of agriculture. Agricultural adjustment of production is associated with the idea that something can be done in guiding the preference of consumers. The time is not propitious, however, for predicting that these significant experiments will culminate in widely accepted cooperative principles, because so much depends on the education of the masses and the attitudes of cooperative members as well as on many other influences at work in society.

#### Questions

1. Is an idea sound in theory if it cannot be applied in practice?
2. Enumerate the changes which the word "principle" has undergone in usage since ancient times.
3. Distinguish between the terms "principle" and "practice."
4. Critically appraise the following statements:
  - a. "The principles of cooperation are primarily socialistic concepts."
  - b. "The practices of cooperation are essentially capitalistic in nature."
5. Enumerate the basic principles of cooperative sales companies.

6. What are the various plans of membership represented in cooperative sales associations?
7. Make a list of possible sources of cooperative savings. How should these savings be distributed?
8. Under what circumstances should cooperative sales associations assume risks?
9. Define the term "social capital." Has it any significance for the cooperative ownership of facilities?
10. Is the above list of principles conclusive? Enumerate two or three cooperative practices that are, in your estimation, sufficiently universal to be regarded as principles. Do they meet the test of a principle?

## VII

### *Principles of Cooperative Purchasing Associations*

*“There are many ways in which to improve the conditions of mankind but the noblest of them all is through cooperation.” Holyoake could have added, there are many ways to cooperate. The principles of a particular type of cooperative association are basically similar, but in the past they have received various interpretations by people of different nations. The International Cooperative Alliance was formed to unify the activities of all cooperators and extend the influence of the movement everywhere. To achieve this end, delegates from all parts of the world meet in congress periodically to discuss vital issues, and lay plans for the future development of the movement.*

*In 1930, more than a hundred years after the first cooperative societies were founded in Europe, the Alliance instructed its central committee to make a thorough study of the principles of consumer cooperation. The brief preliminary report submitted by the committee included seven principles of which the authors present their own interpretation.*



## CHAPTER VII

### PRINCIPLES OF COOPERATIVE PURCHASING ASSOCIATIONS

To students of the cooperative movement, the differences in the principles of sales- and purchase-type cooperative societies are of greater significance than are the similarities. These differences may be traceable to the original concepts or to some singular interpretations of the principles. Whenever the relative merits of cooperatives of the producer and consumer types are discussed, the question invariably arises whether the two types are compatible within the same country or community. The impasse is an apparent conflict centered about price, because it is asserted that the chief interest of sellers is to keep prices up, and of buyers to bear prices down. The implications in this and similar assertions may be more readily comprehended after one has given consideration to the principles common to the major types of cooperative organization.

In American literature some descriptions of the consumer cooperative movement in Europe postulate that several infallible principles were suddenly discovered by the unlettered weavers of Rochdale, and not only that these principles have withstood the test of time, but that they are the primordials of all types of cooperative organization. These suppositions fail to note the evolutionary changes through which principles of the consumer cooperative movement have passed since 1800. The rate as well as the extent of change is affected by the diverse social, economic, and political conditions which, even within the same nation, shape institutions and determine their policies. On the numerous occasions when representatives from various parts of the world have been brought together for conferences, they have been impressed with the deep differences which develop in their discussions of the aims, arrangements, and accomplishments of cooperation. In 1930, more than a century after the first consumer cooperative association was formed in England, delegates

to the International Cooperative Congress meeting at Vienna requested that a study of the leading principles of consumer cooperation be made. It was the wish of many veteran cooperative leaders that such a study should define the principles of the Rochdale cooperative.

That the International Co-operative Alliance has the responsibility for upholding and safeguarding the standards of cooperation is beyond any doubt. That it has equally the task of determining what those standards are has been decided, by common consent, in the decision of the Congress to charge the Alliance with the enquiry now in progress. . . . The necessity for such an examination at the present time is, I think, beyond question, when in certain National Movements we see first the watering down, or diminution, of those standards in actual practice and now, still more, attempts to revise the standards themselves, to bring them into conformity with the vitiated practices that have been adopted for various sophistical reasons, but the plain facts of which are, to beat capitalist enterprise at its own game even if its methods have also to be adopted. Apart from the cooperative immorality of these courses, they are obviously doomed to eventual failure or to the transformation of the Cooperative Movement into an insignificant, if useful, department of the State instead of the world regenerating force which we believe it is destined to be.<sup>1</sup>

The central committee passed the task to an executive committee, which in turn selected a number of eminent men from various nations to serve as a special investigational committee. The special committee of authorities met on seven occasions in as many different cities of Europe to study the questionnaire reports submitted from all parts of the world. Four years later the committee gave a brief résumé of its findings to the Fourteenth International Congress meeting at London, but the work has not yet been completed. Another report is to be given at the meeting in Paris in 1937, and the Congress has been asked to continue its survey of the cooperative field to determine the organization, functions, and relationships of each type of association, giving attention particularly to cooperative activities under present economic conditions. The preliminary findings of the committee represent the accretions of a century of cooperative experience, and its conclusions on specific principles are presented as the most authentic list yet compiled:

<sup>1</sup> MAY, H. J., *The Significance of Co-operative Economy*, lecture given at Fifteenth International Co-operative School, Saltsjobaden, Stockholm, *Review of International Cooperation*, no. 9, p. 329, September, 1936.

1. Open membership
2. Democratic control
3. Dividend on purchase
4. Limited interest on capital
5. Political and religious neutrality
6. Cash trading
7. Promotion of education

#### OPEN MEMBERSHIP

The more members there are in a consumer cooperative, the greater will be the savings through collective wholesale purchasing, and the lower will be the costs of retailing. There is no need for distinguishing one consumer from another because their interests are generally similar in extent and intensity. Variations in the purchases of individual consumers are slighter as a rule, than variations in the patronage of members of a producer cooperative. Personal contacts and relations among consumer members need not be so intimate as those among members of sales societies, and it should be possible to admit all applicants without prejudice toward their personal characteristics, color, creed, or credentials.

Access to a consumer cooperative association should be made simple and direct. Contracts or membership agreements are not essential. Individuals should be free to patronize cooperative stores when and where they wish. The initial capital investment should be small so that everyone will feel that he can afford to become a member. Provisions are sometimes made whereby a nonmember may begin patronizing a cooperative store, with dividends earned on purchases accruing in the association until they aggregate an amount sufficient to buy a share of stock, the customer then becoming a bona fide member. Exceptions to the principle of open membership are made in some industrial productive societies, agricultural sales associations, and cooperative credit institutions in Great Britain and on the Continent.

#### DEMOCRATIC CONTROL

If liberty, equality, and freedom are indispensable in a democracy, they are equally fundamental for economic organizations in which masses have a proprietary interest. The realization of a democracy in the economic sphere is the aim of all cooperatives. The belief that each man has a right to participate in



government became the basis for extending voting privileges on an equal basis to all members of cooperative societies without consideration of sex or status. There are some individual members in consumer cooperatives who would hold a brief for representation on the basis of participation rather than on a one-man, one-vote basis, and contend that the principle of equality is not really violated. This interpretation of equality is most likely to be made where volume of trade is of vital importance to the organization. A vote on the basis of patronage is tantamount to a vote on the basis of proprietary privileges. Property rights are, temporarily at least, placed above individual rights. Those who adopt this point of view out of expediency should be reminded that in a true democracy there is no compromise between personal rights and property rights. Democratic control is always vested in men, not in capital. When any compromise is effected in which patronage or property is used as a measure of an individual's voting power in an association, several difficult questions must be considered. How much added weight should be given to a member's vote because he buys more merchandise or owns a larger number of shares of stock than a fellow cooperator? Which shall have jurisdiction over the affairs of the association, men or money? The business of an association might conceivably be classified in a manner which would permit, for example, one vote per member in the selection of the managerial personnel but unequal voting power upon questions relating to fiscal policies.

Large cooperative bodies formed by uniting many small associations find that only a rough approximation of a pure democratic procedure can be attained. In regional, national, or international organizations, the question invariably arises as to whether voting power should be granted the delegates in proportion to the number of members represented or whether the one-man, one-vote formula should be imitated by giving one vote for each association irrespective of the number of members in the association.

#### DIVIDENDS ON PURCHASES

Savings or surpluses accumulate in associations buying and selling as a result of adherence to a policy of charging more than is necessary to cover costs. The amount of the dividend may

symbolize efficiency and bargaining power in the consumer cooperative enterprise. Periodic distribution of savings or net surpluses reassures members that their cooperative unit is operating successfully. In some countries, as in England and Wales, no inducement has proved more effective in sustaining membership interest and loyalty than the dividend. In other countries or localities, as in Norway and Sweden, low retail prices are charged at the time of purchase and emphasis is placed upon price in appealing to member patrons.

The effect of the lower price policy generally followed by Swedish societies is described as follows:

A criticism might be lodged, from the cooperative point of view, against the price policy adopted by Swedish cooperation in that consumers who do not belong to the cooperative movement may enjoy the benefit of cooperation. It might thus be supposed that this price policy directly counteracts the aim of the movement, which is to enroll a larger and larger number of members within its ranks. This objection carries little weight, however. Experience in Sweden goes to show that the intervention of cooperation in different branches of industry has shown the general public that it possesses in cooperation its surest defense against monopolistic exploitation. This has been highly conducive to an increased membership in our societies.<sup>2</sup>

[About 52 per cent of the Swedish Societies representing 61 per cent of the membership did not pay in excess of 3 per cent dividend on purchases and only 6 per cent of the members belonging to 7 per cent of the societies received more than 5 per cent dividend on purchases.<sup>3</sup>]

The distribution of earnings in some form of extra payment has been systemized in well-regulated retail societies. Some stores pay a regular fixed percentage on purchases, however modest this percentage may be, and when net earnings warrant a more liberal distribution, a supplementary dividend is declared. Other stores offer their members bonus vouchers in addition to regular dividends. The bonus vouchers are redeemable only in departments of the store least visited by the members, or in a branch of retail distribution where a greater volume of trade is desired. Private competitive retail shops soon learn the dates

<sup>2</sup> GJÖRES, AXEL, Cooperative Development in Sweden, lecture given at Fifteenth International Cooperative School, Saltsjobaden, Stockholm, *Review of International Cooperation*, No. 10, p. 370, October, 1936.

<sup>3</sup> *Ibid.*, p. 371.

of regular dividend distributions and, during these periods, advertise special bargains in an effort to attract some of the cooperative earnings. Dividends are usually payable on a quarterly or semi-annual basis and are distributed at times when the drain on the family pocketbook is most likely to be the greatest, such as the due dates for interest, taxes, and insurance. Some families use the returns for travel or vacations, or as special holiday funds. So much significance has been attached to the dividend on purchase in consumer cooperatives that one might properly question whether the main object of collective action, namely, service, has not been subordinated to avarice for profits.

Theoretically, cooperatives might charge a price just covering the cost of the goods and the services rendered in their sale, but the price would have to be based on estimated costs because the actual costs are not easily determined. The retail price less dividends is of great significance to some buyers. These buyers are the bargain-conscious members who roughly calculate an approximate cost for each individual item while shopping. The price of goods at the cooperative must compare favorably with alternative opportunities in other shops or market places, because to these pecuniary minded members pennies are more important than sentimental loyalty to a particular cooperative enterprise. Cooperative purchasing, however, has a real appeal to such members, because it provides the means for accomplishing the same objectives which they strive to achieve by their own efforts at higgling and bargaining in the ordinary transactions of life. Owing to the influence of chain-store organizations in America, consumer stores may find it necessary to adopt the price policy followed by the Kooperativa Forbundet of Sweden rather than the more general policy of maintaining competitors' prices which prevails in many other countries of Europe.

There are some practical reasons for not adhering to the policy of handling retail merchandise at cost. All costs of buying and handling cannot be definitely allocated; shrinkage and spoilage cannot always be accurately estimated, and sometimes goods must be sold below cost to meet competitors' prices. A margin above costs is necessary to cover the ordinary risks assumed in purchase and sale transactions.

The cost basis of pricing goods to consumers is difficult to apply for another reason. Private enterprisers sell some items below

cost, making up the loss on other items where a slightly larger margin is not so apparent. No association would want to place itself in the position of losing business to competitors merely because these competitors temporarily resort to the use of price leaders. The Rochdale Pioneers early abandoned the cost-basis system of handling provisions and resorted to the prevailing market price policy because the advantages of cooperation were more clearly reflected by the size of the dividend paid periodically in lump sums than the small daily savings realized through the reduced prices of provisions. The results are the same, but one procedure has a greater psychological appeal to some people than the other.

Charging prevailing market prices is the most effective means of avoiding a direct conflict in the market because it does not induce destructive price wars. The marketing margin in industrialized countries such as England, Germany, and the United States, ranges from 25 to 35 per cent of the sales price of goods. Private merchants find it difficult to combat the cooperatives that adopt the policy of taking margins comparable to those of other merchants. They cannot graciously criticize the cooperatives for long margins, because long margins are the invention of private shopkeepers. Shopkeepers might comment unfavorably about the services given by cooperatives, but such comment would be without point if consumers could not be won over to their stores. They certainly would not be justified in disparaging the refunds and the dividend paid members because it would reflect on their own efficiency. It would seem uncharitable for them to belittle the social services which are provided out of cooperative reserves. As a means of defense against cooperatives, the merchants have learned that it is unwise to precipitate a price war unless their own resources are large.

#### LIMITED INTEREST ON CAPITAL

The reward for past labor is secondary in importance to that of immediate effort under this principle. The major emphasis in cooperative undertakings is upon present labor, in which it is implied that the greatest happiness abounds in a society where opportunities make it possible for everyone to be industrious and mentally alert. The Equitable Pioneers recognized in capital a powerful force which could be directed for good or evil. They

resolved to direct the meager sums which fell into their hands with an intelligence that should make capital serve all who became members of the society.

In one respect this principle suggests the medieval abhorrence for usury. It recognizes but places a limit upon the amount that shall be paid for the use of capital. Capital is subordinated in cooperative enterprises because it is thought of as noxious, bearing many seeds of injustice, if it is not kept under control. Some of the reasons for this attitude toward capital arise from the manifestations which appear when men suddenly acquire more than the amount which usually comes into individual hands. In direct utilization, the possession of wealth, to use the phraseology of Veblen, is placed upon invidious distinction, emulation, and conspicuous consumption. The use of capital in the business world, however, is sometimes abused by those interested in it because it can so easily be devoted to means of exploitation. It might be marshalled against that portion of society which is unfortunately in a weak bargaining position. The valiant pioneers of cooperation who struggled to reform the economic system by becoming masters instead of slaves of their economic environment laid down the principle of controlling wealth by limiting the amount of interest which should be paid for its use. They distinguished themselves by setting a higher purpose for the use of capital—that of alleviating the conditions of fellow workers instead of suppressing them. Their vision was one of harnessing and conserving wealth for the use and benefit of all members of society.

#### POLITICAL AND RELIGIOUS NEUTRALITY

Cooperative institutions may be of inestimable service to a community by maintaining a keen interest in social welfare and governmental activities. There are many undeveloped areas in both of these fields that do not encroach upon the jurisdiction of the church or upon political parties.

If the principle of open membership is acknowledged, the association embraces all members of society without prejudice, irrespective of their faith or political affiliation.

The basic concept of neutrality is tolerance, tolerance for differences in ideas and convictions. The cooperative is counseled not to meddle with affairs that are obviously outside its sphere

of business activities, because the schismatic influences which result from political issues and religious controversies tend to destroy relationships essential to trade.

This principle has always been an axiom of private business concerns, and its merits have been generally self-evident to the members and managers of producers' cooperative sales associations.

The cooperatives of most countries in the world claim adherence to this principle. A few notable exceptions, however, are the political connections of cooperatives in England, Finland, Russia, Italy, Austria, Belgium, Yugoslavia, and Czechoslovakia. Cooperatives in Italy are of necessity Fascist, in Russia Communistic, and others have relations with either the socialist or labor parties, or as in England where certain members have organized a Cooperative Party. Switzerland was the only country to report a regional cooperative organization not neutral toward religion. In Belgium the cooperatives are closely identified with the labor-union movement.

#### CASH TRADING

Under this principle members of consumer societies are required to pay cash for their purchases. Cash trading, which is most easily accomplished by budgeting the family expenses, forces people to live within their incomes. For the wholesale society, cash payments for goods make it possible to take advantage of special opportunities in large-scale purchases, to buy more economically at all times, and to obtain allowances as well as cash and quantity discounts. Allowances are made on purchases in large quantities for direct deliveries from local producers or manufacturers, reducing transportation and other distributive costs. Interest on capital is reduced to the minimum because the established cooperative usually has ample reserves and a good line of credit scheduled at low interest rates. The savings which can be made by the retail stores in making cash settlements for current purchases are appreciable during the year, especially on goods having a rapid inventory turnover.

A cash system effectively reduces the amount of bookkeeping that is necessary under the credit system and eliminates losses on bad accounts. The extension of credit particularly endangers those people who find it difficult to avoid the temptations of

overspending. They become hopelessly enmeshed in a web of debts from which it is very difficult to extricate themselves.

The great wholesale and retail societies have found that they cannot always adhere to a cash policy and still retain their patronage. Recently there has been a clamor for more liberal extension of credit. This tendency is not altogether a healthy one in that it endangers the reserves created by loyal members and encourages improvidence among others. Credit is being given by private retail corporations competing with cooperatives. Since rival organizations grant credit to their customers, it behooves cooperative societies to find some means of doing likewise. The rapid developments in the field of cooperative credit may be the solution to this problem. Those who do not have the available cash may finance themselves through a correlative institution specialized in rendering credit service. If such an institution finds that it cannot grant credit to a person, it is doubtful whether cooperative distributive societies can afford to assume the risk. In the absence of properly organized credit service, however, the management of cooperative societies must exercise care by limiting the amount of credit given to any individual member and by being judicious in extending credit to those who are doubtful risks. The experiences of those societies which have granted credit prove the wisdom of maintaining a policy of cash trading whenever possible.

#### PROMOTION OF EDUCATION

Madison once said, "to put the conduct of affairs into the hands of the people without first educating the people will prove to be the prelude either to a farce or to a tragedy." The first English and Scottish cooperators recognized that their efforts would be futile if the people were not prepared to assume the responsibilities of operating and directing their own businesses. Often the first step toward the formation of a cooperative was the establishment of a library or a reading room in which everyone interested in the subject of cooperation might find a congenial atmosphere and a place of comfort to spend their leisure hours in self-improvement. It has long been a custom for consumer societies to divert a small percentage of net savings to an educational fund. These societies have been inclined to expand reserve funds more freely for general educational projects than to encourage producers' associations.

The reason for this is that everyone is a consumer and, therefore, a potential member or customer of some retail society within a large system of cooperative organization such as the English, Danish, Dutch, or Norwegian wholesale societies. Some portion of the funds, of course, is used to stimulate sales and increase interest in the local societies, but on the whole, consumer cooperatives exhibit general rather than specific objectives in their entire program of education.

Cooperation among producers under American conditions of industry seems to require a more direct program of education. The propaganda in house organs, the subject matter discussed in special meetings, the brief radio talks, and the personal contacts made by expert field-service staffs are studiously directed toward the particular interests of the associations disseminating information and providing services. The expenditure of association funds for the promotion of cooperation in general is not common, because the various specialized cooperating groups are not bound by a common interest in integrated overhead organization. Many writers have planned educational programs which are more universal in scope, such programs resembling the one outlined in the next few paragraphs.

The cooperative movement needs intellectual centers where scholars might congregate from all parts of the world to exchange information and pursue research studies. These centers should be founded at favorable places in Europe, Asia, and North America where their influence would be a source of strength to the cause. They could be located near the particular types of associations to which scholars are devoting special attention. Every effort should be made to remove impediments to a better appreciation of cooperative effort and to promote good will among cooperators internationally. It is presumed that one institution on each continent might be easily financed to provide excellent facilities for investigational and instructional purposes. The files of the research laboratories and the libraries could be provided with accounts of the practical problems of cooperative enterprises as well as an unlimited mass of statistical data on the operations and transactions of the various associations. A system of exchanging literature between the centers and providing travel for visiting instructors and fellows would serve to stimulate interest in the diversified forms of cooperative enterprises



and promote a common understanding of their possibilities and limitations.

In some countries the educational and promotional agencies are departments of central wholesale societies, as they are in Sweden. In other countries, as in England, the promotion, education, and organization of new cooperatives become the work of a separate organization maintained by the operating cooperatives within the country. Comparable to the Cooperative Union of Great Britain is the Cooperative League of the United States. This league, organized in March, 1916, is the central unifying agency of the consumers' cooperative movement in America. It is now the pivotal educational force and general information bureau for the movement in this country. The increase in the number of consumer cooperative business organizations and the accompanying demand for promotional work and management guidance has resulted in the organization of three district leagues. Other district leagues for performing similar functions in the expansion of the consumer movement are in the process of organization. The Northern States Cooperative League of Minneapolis is one of the largest and most active of the three district leagues. A magazine, "Consumers' Cooperation," is published monthly by the central league and is one of the numerous media for circulating the philosophy of the movement and maintaining interest in its progress. Through the Cooperative League of the United States, American cooperatives are affiliated with the International Cooperative Alliance of London, which is the international clearinghouse of information on the consumers' cooperative movement throughout the world.

Whether the educational and promotional work of the cooperative movement should be vested in an organization established especially for that purpose, or whether it should exist as a separate department of a central wholesale society or central marketing association, is a point of contention. Many feel that the philosophy of the movement as distinct from its purely business aspects can receive just consideration if a separate agency is organized. It is also felt that an educational agency can be a unifying force within the movement by conjoining, on a basis of mutual understanding, cooperatives that would normally compete with each other to their disadvantage. An educational agency can devote time and energy to promote cooperation in places where separate

business institutions would find it impracticable, from a selfish standpoint, to spend money for organization.

Opposing these arguments in behalf of a central educational agency are the contentions of the advocates of a separate department of a central wholesale or marketing association to take care of educational work, as follows: Because the satisfactions which members are to derive from cooperative effort depend upon such tangible things as high quality goods, adequate service, and low prices, the central cooperative furnishing these should be the judge as to when and where cooperatives are organized. Since many problems of existing cooperatives are business problems, the central selling agency must be called in and may just as well provide the entire educational program for its constituency. Because the central association ordinarily benefits through new stores or local marketing associations affiliated with it, it should assume the responsibility and expense of securing the additional volume of business. The experience of Sweden's consumers' cooperatives and American farmers' cooperatives has proved that business concerns can discharge the educational function in a satisfactory manner. Mr. Howard A. Cowden, President of the Consumers' Cooperative Association, North Kansas City, Mo., writes, "The Swedish system seems to us the better, for it insures on the one hand that the educational work shall result in greater cooperative trade, and on the other that the business activities shall adequately finance the educational department."<sup>4</sup>

The general educational system including large and small universities, colleges, and secondary schools should continue to give, or be requested to offer, courses of instruction in cooperative principles, practices, and organization problems. The existing educational institutions provide the best means of diffusing among the masses information about cooperative philosophy. In 1935 a law was passed in Wisconsin requiring all common schools, high schools, and vocational schools to teach the elements of cooperative marketing and consumer cooperation. The state university, state teachers' colleges, and county normal schools are also required to provide in their respective institutions "adequate and essential instruction in cooperative marketing and consumers' cooperatives." Special schools could be organized to perform

<sup>4</sup> COWDEN, HOWARD A., *A Trip to Cooperative Europe*, p. 28, pamphlet published by the Consumers' Cooperative Association, N. Kansas City, Mo.

the more mechanical task of training a competent personnel for directing the business functions of associations. There are unfortunately in this general system of instruction at least two limiting factors: (1) a dearth of teachers who have received an adequate training in the social sciences to teach the subject with competence; and (2) only a few of those who have studied economics have formulated a philosophy inclusive enough to be consistent with the principles of cooperation.

Emanating out of an educational system, there may be any number of schemes and devices for propagating and promoting actual organizations. A comprehensive extension system of instruction with all its ramifications, such as that maintained by the federal and the state governments through the land-grant colleges, is an illustration of this form of disseminating information.

Cooperative organizations, since their inception, have assumed a major role in educating their own members, as well as liberally contributing talent and means to general educational programs. One of the first obligations of an association is to stimulate the intellectual interests of its members. Whatever sums are set aside from earnings in an educational fund should be used to raise the level of understanding within the organization until intolerance and ignorance from without do not hamper further progress. The advantage of this policy is twofold. It demonstrates that which it advocates, and it multiplies the possibilities of extending education to the masses through the influence and self-assumed efforts of its own enthusiastic members. The Danish folk schools which are separate from the cooperative system in Denmark, nevertheless, have proved to be one of the most creative forces in educating the Danes in the wisdom of marketing and purchasing on a cooperative basis.

Participation and self-education are the most effective means of conveying ideas to the uninitiated if leadership can be discovered to direct this system of informal education. Groups of interested people may arrange periodic meetings in their homes or community clubrooms to study and discuss phases of the cooperative movement. Great Britain and the Scandinavian countries have profited particularly from this type of spontaneous instruction. Interest in this kind of project may be stimulated, however, by constantly recruiting young members and injecting some order

into the system of providing literature, illustrative materials, and expert guidance for group discussions.

**THE LIST OF PRINCIPLES IS NOT CONCLUSIVE**

The above principles apply to agricultural purchasing associations as well as to consumer cooperative societies. In either case the objectives are similar whether the purchases are made for direct or indirect consumption.

Several other concepts were suggested for definitive analysis and inclusion in a list of principles, but none of them were accepted for the advisory committee's report. The inquiry included such questions as: Should consumer cooperatives:

1. Trade exclusively with members?
2. Hold surplus reserves indivisible?
3. Provide representation on basis of participation?
4. Permit employees to share in the earnings?

If trading was confined to those who are bona fide members in the consumer cooperatives, the most effective means for increasing the number of patrons and expanding the volume of sales would be eliminated. Members often receive substantial benefits from profits on the transactions of the casual customer in associations where nonmembers do not participate in the earnings. Adoption of this proposal would therefore decrease the savings now made available to members, and it would take away the most effective means of recruiting new members by permitting dividends on purchases to accumulate until a share of stock or membership is acquired.

The theory underlying the proposal that surplus reserves should be held indivisible is that a portion of the earnings of any cooperative association is the reward of collective activity and can neither be logically attributed to the actions of any individual member nor to the efficiency of the management. Therefore, it is concluded that the savings should be left to accumulate in a reserve fund to be held as common property by the association. This fund would serve to increase the prestige of the association and insure its perpetuation as a service institution to consumers of future generations.

The suggestion that representation be made on the basis of participation has been discussed in Chap. VI under the principle of Democratic Representation.

In the formative years of the Cooperative Wholesale Society, employees as well as patrons shared in the earnings of the society. This arrangement stimulated each employee to give the best possible service in order that the earnings would be larger. Employees' wages were low and the share in the earnings was considered a part of the compensation of the workers. In recent years, the C.W.S. has abandoned this policy to avoid compensating their employees in three different ways: (1) wages, (2) dividends on purchases, and (3) bonus on sales. Employees of the C.W.S. enjoy the same status as any other member who is gainfully occupied elsewhere. They participate as members in the society on an equal basis in the services and savings.

#### Questions

1. What are the most commonly accepted principles of "Purchasing Associations"?
2. Why do the principles of cooperative purchasing associations differ from those of cooperative sales companies?
3. Are any of the principles interpreted to be similar to those of cooperative sales companies? Which ones?
4. Which price plan is more desirable from a social point of view:
  - (a) The cost basis of pricing goods, or
  - (b) The prevailing price plan?
5. Why should interest on capital be limited in a cooperative society?
6. Give the advantages of cash trading.
7. Is the purchasing type of cooperative enterprises more aggressive in the promotion of education than other types of cooperatives?
8. Have European cooperatives conformed with the high purpose of maintaining political and religious neutrality?
9. Should the purchasing-type association permit employees to share in the earnings of the association?
10. Are the principles enumerated in this chapter arranged in the order of their importance?

## VIII

### *Formation of Cooperative Associations*

*Aside from the strictly business phases of a cooperative, the human relationships play an exceedingly important part. This elusive human element must be considered fully in organizing a cooperative. Since this human factor is so variable, the plan of organizing associations cannot be stereotyped—it must be arranged in such manner as to deal most effectively with this changeable element. Before a cooperative association is organized, it is well to have an economic survey made by a competent agency to determine the exact status of existing marketing practices, agencies, technique, and machinery; to ascertain the probable economies from cooperative action and the cooperative spirit among the producers in the rural community. This survey should show above all whether an economic need exists for the establishment of an association. If an association is organized, incorporation should soon follow to give it a legal standing. Central marketing associations are in a position to help solve certain marketing problems which local associations unaided cannot solve to best advantage. No rule-of-thumb formula can be set up for organizing large-scale central marketing associations. Some organizers prefer a bottom-up plan of organization, others a top-down.*

*The reasons for failure or cessation of cooperatives give clues as to the weak points in their organization and operation. Inefficient management, financial difficulties, insufficient volumes of business, and lack of membership support are the chief reasons for suspension. Certain practices, such as handling quality products, organizing producers having similar marketing interests, using marketing contracts, maintaining accurate records and accounts, and keeping an association producer owned and controlled, are not absolutely essential for success but contribute materially to the same. Since many cooperative associations, like private businesses, have failed because too little thought was given to details preceding organization, it is expedient to give considerable attention to this phase in the establishment of any association.*



## CHAPTER VIII

### FORMATION OF COOPERATIVE ASSOCIATIONS

There is no vest-pocket formula for organizing either cooperative sales or purchasing associations. No stereotyped procedure is practicable. There are, however, certain steps that may be followed which will give a more solid basis for organization. Too many cooperative companies, like private businesses, have failed because too little time was devoted to the details preceding organization. Too many are started on the basis of grandiose wishes—too few on the basis of practical reality. Before the depression of the thirties, approximately 11 per cent of the cooperatives annually ceased operations (11 per cent of private businesses also failed yearly).<sup>1</sup> Since such cessation is not only accompanied by heavy financial loss, but by caustic ridicule of cooperatives by its critics, and a breakdown of faith in cooperation as well, those who organize associations might well proceed scientifically rather than in a hit-or-miss fashion.<sup>2</sup>

#### ESTABLISHING LOCAL ASSOCIATIONS

In every community, persons may be found who wish to organize a cooperative. Some are looking for a job, others are vexed at the local dealers, some are merely fanatics on cooperation, and many have a sound basis for wishing to organize an association. Usually the county agent, or the state college of agriculture, or the local Grange, Farmers' Union, Farm Bureau, and Equity meetings, or a small group of farmers hears about the desire to start an association. Before calling a general meeting of all producers in the community, those who are interested should hold

<sup>1</sup> Cooperative Marketing, letter from the Chairman of the Federal Trade Commission, Senate Document 95, 70th Congress, 1st Session, pp. 300-301.

<sup>2</sup> For an excellent discussion and guide for setting up local cooperative marketing associations see Harry C. Hensley, Fruits and Vegetables—Guide for Setting Up Local Cooperative Marketing Associations, Federal Farm Board, *Bul.* 1, 1930. See also A. M. Eberle, Steps in the Organization of a Cooperative Marketing Association, *Extension Circ.* 317, 1932, South Dakota State College Extension Service.

an informal meeting, state their personal reasons for wishing an association, and resolve to make a general survey of the whole situation. On the basis of this survey the final decision should rest. Such a study should be made by a competent person or committee in analyzing a local marketing problem. What should this survey show?

**Is There an Economic Need for the Association?** The ostensible purpose for organizing a cooperative marketing association is to establish the most efficient agency to market farm products. Economy of operation and expertness in selling are the twin goals sought. With this in mind, all other purposes for an association become secondary or even illegitimate. Hence, the most important and first consideration before starting an association is the economic need for it. If honest, dependable, and efficient service is already present so that it would be impossible for an association to improve the marketing methods in any way, then there can be little reason for starting a local association. However, such a conclusion has one exception. Sometimes it will be found that local private marketing agencies are efficient but that they are simply a link in a system which can be greatly improved. The system per se may need overhauling. In such an event, it is usually necessary that local associations be organized so that these can make it possible for terminal marketing agencies or national cooperatives to function.

How is the need for a local association determined? This need is best discovered by analyzing the character of the local marketing service. Is there a lack of adequate facilities or of service? Is there an absence of competition and is the local operating margin apparently too wide? Is the service honest and dependable? Are excessive profits being made by the established concerns? Are the producers' best interests adequately served? What concrete savings or improvements can a cooperative effect? Will the improvement which is sought be commensurate with the risk, financial investment, and farmers' time and effort involved? Is the local association needed to such an extent that it will enlist the support of the best farmers in the community?

Industrial concerns, chain-store organizations, and other commercial organizations oftentimes spend months making preliminary surveys and analyses of all factors that bear upon the probable success of a business venture. Farmers will do well



to follow this precedent. The old adage—an ounce of prevention is worth a pound of cure—applies here.

**Is There Sufficient Volume for Efficient Operation?** The survey should also include an inventory of the potential volume of business in the community. If a local creamery is proposed, how many cows are there within a radius of 5, 10, or 25 miles of the prospective plant? What is the average production per cow? If it takes 1,000 or 2,000 cows to produce enough butterfat to operate a creamery economically, are there that many cows in the neighboring territory? The unfortunate experience of farmers in Kansas and Nebraska where cooperative creameries were established before sufficient butterfat was obtainable indicates the importance of ascertaining the present and potential supplies in advance. It is unnecessary to point out here that sufficient volume is essential for low cost operation, retention of capable managers, meeting of competition, and for obtaining minimum shipping costs as well as market premiums for volume sales. Although some large-scale regional sales associations have overemphasized volume at the expense of other equally important aspects of their business, it is, indeed, seldom that local associations have committed this error.

**Are There Sufficient Producers Interested in an Association?** It is one thing to have an adequate volume produced in the community, but quite another to know what proportion will be marketed through the cooperative. By means of a short questionnaire or personal interviews this information may be obtained. Some local associations using a contract require a minimum number of signers or a certain minimum volume of production before the contracts become effective. It is natural that many prospective patrons are not in a position to decide definitely at the time the survey is made or do not wish to commit themselves to a cooperative before they see how it functions. Hence, an association need not delay organization if 100 per cent of the members which it may easily have in a few years do not agree at once to become members. A sufficient volume should, however, be available to commence operations and there should be a fair assurance of an increasing volume for economical operations in the future.

**Can the Producers Finance the Association?** If the association requires no capital investments, such as a livestock shipping

association, no problem arises. But if land, buildings, and equipment are required the question of financing the venture is exceedingly important. What will the total investment amount to? How much will have to be supplied by the members? How much are members willing and able to pay at once and subscribe for to be paid later? Where can adequate loans be made? What will be the cost of such financial assistance? Knowledge of the amount that prospective members are ready to invest in the company can be gained from a questionnaire or from personal interviews.

**Can a Competent Manager Be Hired?** So much depends upon capable management that to overlook this feature is certain to invite trouble. An honest, dependable, capable and likable manager is the axis about which the association revolves. Can such a person be hired? Or, is some inexperienced but well-meaning retired farmer the only one available for the position? Operations might better be delayed until a qualified manager can be engaged than to go ahead with the cherished hope that the right man will pop up from somewhere.

**Miscellaneous Factors to Be Surveyed.** In addition to the above mentioned prerequisites, the survey should also inquire into the spirit of cooperation that exists among the residents of the community. Split communities are poor grounds for successful organization. Have the producers in the community shown their ability to work together on some major enterprise? Or has some previous disastrous experience with cooperatives embittered the farmers against the movement? What is the attitude of producers toward cooperative marketing?

Likewise, is there local qualified leadership that will assume the responsibility of setting up an organization and devote considerable effort to see it succeed? If the survey is made by a disinterested party, such as the college of agriculture, enthusiastic local leadership will be required to "sell" the idea to the community. Outsiders are often regarded apprehensively. After all, the association must be supported and run by local residents and it is essential, therefore, that the producers are convinced that the association is for their welfare alone and not for someone else's good.

The stability of the rural population is an additional factor to be considered. If the producers are predominantly renters who

care little to invest their small savings in a cooperative or who have short-time leases, the status of their association will be less secure than if the producers largely own their farms.

**Report of the Survey.** After the survey is made, the local committee should prepare a report to be submitted to the producers in the community. If the report indicates clearly that it is inadvisable to start an association, the matter may simply be dropped or reported to the growers. If, however, the report shows the opposite, then every effort should be made to secure a large attendance at a meeting where the committee can report favorably upon its investigation, answer questions, and propose plans for the new organization. Those in attendance should then vote upon the committee's report. If this is in the affirmative steps should at once be taken to elect an organization committee (preferably including members of the survey committee). If physical facilities are needed a building committee may also be elected. A third committee, the finance and membership committee, should also be elected to secure stock subscriptions or memberships in the association. The organization committee has the responsibility of drawing up the articles of incorporation and bylaws, incorporating the association,<sup>3</sup> and preparing the marketing agreement if such is to be used. The building committee must find a location for the plant, adopt plans for construction, secure bids from contractors, and decide upon the kind of equipment to be bought. At a second meeting the articles of incorporation and bylaws are adopted, permanent officers are elected, and committee reports are heard and approved. As soon as sufficient members have signed marketing agreements and after financial arrangements have been made, the cooperative can start building operations and become a going concern.

Knowledge of state laws under which associations are incorporated is important. In one state, for example, the cooperative law provides that not more than 5 per cent of the paid-up capital stock or membership fees may be used to pay promotion expenses. In this same state in a capital stock association, at least one-half of the authorized capital stock has to be subscribed and one-fifth must be actually paid for before the association can legally do

<sup>3</sup> Incorporation papers are secured from the Secretary of State or Commissioner of Corporations. Usually a small fee must accompany the papers when returned to the state office.

business with anyone other than its own members. The procedure in incorporating an association, number of days of notice before meetings can be called, and other legal matters should be ascertained from either the Secretary of State or Commissioner of Corporations.

#### ESTABLISHING REGIONAL OR LARGE-SCALE ASSOCIATIONS

There is no set way of organizing regional, or large-scale centralized or federated associations. The large successful cotton and tobacco cooperatives were organized in a different manner from that of the equally successful butter and livestock cooperatives. The best method for organizing a wheat pool may not be the most desirable for establishing a milk distributing company. No "hand-me-down" method is available, nor would it be advisable even if it were available, for the organizer.

The particular method of establishing a large-scale sales association is not so important as a full consideration of those important factors that will bear upon the success of the sales association. Here again such important considerations as the economic need for an association, the potential volume of business for economical operations, the support of individual farmers or local associations, the financial requirements and backing that may be secured, the experience which farmers have had with similar or other sales associations, the initiative and drive of local leaders interested in such a large-scale venture, and the possible advantages which a cooperative sales association would have over existing companies and methods of marketing are to be carefully surveyed, analyzed, and critically appraised. In addition to the factors that bear upon the success of the regional association itself, there is one other important consideration that may determine the establishment of such company, namely, the services that a central marketing organization may render to local associations to make them more effective and to assist them in coping with problems that they have been unable to solve satisfactorily alone.

Black and Price point out sixteen problems of local associations in the solution of which properly organized and managed central marketing organizations are either essential or could be of material assistance. Some of these are simply problems of the country market in general rather than of local associations in particular—therefore, regional associations have been found necessary and

effective in solving marketing problems in the country market as well as in the larger wholesale markets. The sixteen problems follow:<sup>4</sup>

- |  |                                      |
|--|--------------------------------------|
| 1. Control of quality                        | 9. Claims                            |
| 2. Standardizing production                  | 10. Selling                          |
| 3. Adjusting production to consumption       | 11. Financing                        |
| 4. Stabilizing production                    | 12. Bargaining and price policy      |
| 5. Controlling consumption to fit production | 13. Elimination of competitive waste |
| 6. Controlling the flow to market            | 14. Improving business practices     |
| 7. Distribution of product                   | 15. Utilization of by-products       |
| 8. Inspection                                | 16. Research                         |

Other problems could be added to this list, such as purchasing supplies, bookkeeping and auditing service, providing timely and accurate market information, and furnishing economical legal service.

**"Bottom-up or Top-down" Methods of Organization.** There are those who argue that a large-scale association serving an extensive region of the country should be the climax of an evolutionary process of organization. It is held that local associations should be organized first in many communities and that these local associations on their own volition, not that of some outside party, should agree to establish a central selling agency. This "bottom-up" type of organization method can be said to have many advantages: (1) The bulwark of the regional association is the established and operating autonomous locals; (2) since the central association is a response to the needs which the local associations feel, their loyal support of it is assured; (3) the expenses of "high-powered" organizers are saved since members of the locals do the work; (4) experience in Denmark and elsewhere has proved the soundness of this system; (5) a definite ascertainable volume of business is known in advance so that plans for the necessary facilities and sales forces can be intelligently made; (6) financing the venture is simplified since stock

<sup>4</sup>These problems are discussed in Co-operative Central Marketing Organization, *Minn. Expt. Sta. Bul.* 211, pp. 6-15, 1924. They are as apropos today as they were in 1924.

can be readily sold to the established locals desiring the overhead organization; (7) fewer errors will be made since the establishment of the central organization is usually a slow evolutionary process; (8) the regional association becomes in fact a farmer-owned and a farmer-controlled organization for it springs up from the "grass roots," rather than being the inspiration and concocted plan of some outsider.

In contrast to these arguments the advocates of the "top-down" method of organization (which is usually identified with the centralized type of associations as against the federated type) hold (1) that the "bottom-up" method of organization is too slow a process, and, if the initiative of local groups is to be depended upon, few if any large-scale associations would be organized; (2) that a definite plan carefully drawn up in advance constitutes a sounder method of building than if the organization has to be modified and changed repeatedly as other locals are added; (3) that the experiences of successful cotton, poultry and egg, and wool marketing associations demonstrate the feasibility of such procedure; (4) that for some commodities, local associations and local facilities for handling products are not necessary or economically desirable.

The so-called bottom-up type of organization is supposed to originate with already established prospective members of the central organization, whereas the "top-down" type is commonly thought of as being some outsider's ready-made plan of organization to which the farmers subscribe. Ordinarily the former is thought of as typifying the method of organizing the federated type of associations, the latter that of the centralized type since many centralized associations were organized in this fashion during 1921-1925. From a practical standpoint, however, it is found that large-scale regional associations, whether they be of the federated or centralized type, are the results of suggestions and proposals of both farmers, who may already belong to local associations, and of outsiders representing the colleges of agriculture, state departments of markets, federal departments and general farm organizations. Hence, the influence of outsiders in one type or another of regional association is a matter of degree. Whether the association is organized from the top down or from the bottom up is not nearly so significant as the fact that the prospective members feel a real need for it, that it be a response to

the cooperative spirit of its members, that it be economically sound in its organization, objectives and methods of operation, and that its costs of operations be so low as to effectively meet competition.

#### SPECIALIZATION OR INTEGRATION?

In forming a cooperative, decision must be made as to which steps of the marketing channel for a particular commodity should be covered by the association, *i.e.*, shall farmers perform the functions of middlemen in the country markets, wholesale markets, and retail markets or shall the farmers' company perform only a part of these services? The type of commodity handled very largely determines the answer to this question. Likewise, whether there is to be a change in the whole system of marketing a particular commodity or whether merely certain functionaries within the system are to be replaced by the cooperative association has a further bearing upon the answer.

Generally stated a cooperative association can succeed in any kind of business in which private corporations can prosper. This, however, does not suggest that it is expedient in all cases for a farmers' company to carry its members' products along the entire channel of distribution. Private corporations and many cooperative companies handling only one or only a few related commodities have found it economical to go no farther than the wholesaling step in distribution. Others have found it most economical to use certain private agencies in the wholesale markets of the country—such as brokers, auction companies, and commission firms—to supplement their own wholesale distributing department. Few, if any, private or cooperative business concerns that handle one or a few allied commodities engage in the retailing function, except only in an incidental manner resulting from over-the-counter sales to consumers who call for products at the plants. The usual retail store handles a variety of products—its stock is not limited to the one which a particular group of farmers wish to sell. Meat packers, soap manufacturers, millers, spinners, vegetable packers, and hundreds of other specialized processors fully realize the inadvisability of retailing their particular products.

Established retailers can perform the retailing function, perhaps, in a more satisfactory and certainly more economical

fashion than each individual processor can. The same applies to the majority of farmers' cooperative companies.

For some commodities, chiefly dairy products, farmers can set up a cooperative that will perform all functions of distribution between producer and consumer. Farmers' cooperative milk-distributing companies, some cooperative creameries, and some cheese factories have such large sales direct to consumers as to require almost the entire production of the plants. But it is doubtful if it is wise to carry some products more than a few steps in the marketing channel. For certain commodities such as livestock, wool, rice, tobacco, and cotton, it is most practicable to carry the products to the processors.

It is well to observe at this point that greatest possibilities of improvement in the marketing system for the cooperative lie between the farm and the retail market. The chance of bettering the variety, grade, and pack of products on the farm, or local processing and packing plant, of narrowing margins and raising the standard of service of country market operators, and of effecting economies in transportation, market distribution, and utilization of by-products and cull products promises more tangible accomplishments for the cooperative than the savings which can be made from cooperative effort in the wholesale distributing, jobbing, and retailing fields. Margins of most wholesalers and jobbers are already narrow and those of retailers have been narrowing considerably since the advent of chain-store distribution so that it would be difficult for a cooperative to make a "showing" in these fields. But in the fields of processing, ginning, packing, and handling of farm products in the country markets where so often the uninformed producer becomes an easy prey of the shrewder and better informed local buyer considerable "showing" can be made. As the cooperative livestock commission firms have repeatedly shown, certain types of functions in the wholesale markets can also be carried on cooperatively at costs considerably below private companies' charges.

But the opportunity of influencing prices and lowering costs of marketing is also partly dependent upon the existence of a so-called "perfect" or an "imperfect" market. A perfect or organized market is one in which both buyers and sellers are well informed respecting prices, sales, supplies, consumption requirements, and other factors bearing upon prices and the



movement of products, one in which facilities for the rapid exchange of title and possession of goods exist and in which competition acts freely. The large grain exchanges in the commodity field most nearly approach this concept of a perfect market. In this type of market a cooperative has less opportunity to effect any favorable influence on prices or to decrease operating costs than in an imperfect or unorganized market. It is for this apparent reason that terminal cooperative grain-marketing associations the world over have not been able to achieve so remarkable a success as have the regional fruit and vegetable, livestock, poultry and egg, walnut, and dairy cooperatives. This statement suggests, therefore, that, in a perfect market, operations by private agencies are already transacted on a high level of efficiency which cannot be changed materially, if at all, by a cooperative; in an imperfect or unorganized market in which market news is not common knowledge and, therefore, wide differences in bargaining exist, a cooperative representing a substantial proportion of the producers is in a position to exert considerable market influence to the benefit of its producer-members.

It is evident from these remarks that no dogmatic statement can be made concerning the number of marketing functions which a cooperative should undertake. Here again the criterion is the economic possibilities of such undertaking. What may be unwise at its inception may prove expedient when the organization has gained more experience, established a well-known branded product, and has financial reserves to venture farther into the distributive field. Thus, some large-scale cooperatives were content for years to act as wholesale assemblers of their members' products and use existing wholesale distributing agencies for market distribution; however, after they were well established and had gained considerable market experience, they placed their own sales representatives first in one market and then in another to take over the functions previously performed by brokers, jobbers, or wholesale distributors.

#### ELEMENTS OF SUCCESSFUL OPERATION

A cooperative association may be organized according to cooperative principles, have ever so fine a membership contract, articles of incorporation, bylaws and office building, and have well-known men on its board of directors and still not succeed.

These things, to be sure, are important but in themselves do not assure success. They simply constitute the framework of a possible going concern—the energy, the spark, and the power of the concern are a composite of other factors which will now be examined.

Why do commercial businesses fail or cease operations? The answer to this question is an indirect way of discovering the vulnerable phases of a business and those things that must be guarded against if success is to be gained. In a study of 1,500 cooperative associations that failed or ceased operations prior to Dec. 31, 1926, the United States Department of Agriculture found that the causes given by the associations were the following:

TABLE IV.—REASONS FOR THE FAILURE OF COOPERATIVE ASSOCIATIONS

Cause*	Per cent† of associations reporting	Cause	Per cent of associations reporting
Inefficient management . . . .	72	Dishonest management . . . .	8
Insufficient working capital . . .	24	Acts of providence . . . . .	6
Insufficient business . . . . .	23	Unfair competition . . . . .	2
Too liberal credit to patrons . . .	17	Miscellaneous causes . . . . .	8
Voluntary dissolution . . . . .	12		

\* ELWORTH, R. H., *Agricultural Cooperative Associations—Marketing and Purchasing 1925*, U. S. Dept. Agr. Tech. Bul. 40, pp. 65-66, 1928.

† Many associations gave several reasons for their cessation which explains why the percentages exceed a total of 100.

Chief reasons for suspension of 404 associations investigated by the Federal Trade Commission were:

TABLE V.—CAUSES FOR THE SUSPENSION OF COOPERATIVE ASSOCIATIONS

Cause*	No. of associations	Cause	No. of associations
Voluntary dissolution . . . . .	90	Competition . . . . .	14
Financial difficulty . . . . .	65	Acts of providence . . . . .	7
Insufficient business . . . . .	59	Miscellaneous . . . . .	121
Mismanagement . . . . .	48		
		Total . . . . .	404

\* Cooperative Marketing, letter of Chairman of Federal Trade Commission, Senate Document 95, p. 302, 70th Congress, 1st Session.

After investigating the failures of both large and small local and regional associations, the Federal Trade Commission concluded that the failures were due to one or more of the following causes:<sup>5</sup>

1. Organization mistakes: (a) Failure to study the needs of an organization and the problems to be met; (b) creation of an organization out of proportion to the business to be handled; (c) organization extravagance in the matter of equipment needed, promotional expense, and initial salaries paid.

2. Mismanagement: due to (a) lack of understanding of local conditions, (b) marketing problems, (c) financial requirements, and (d) inexperienced officers and managers.

3. Lack of membership support: due to (a) dissatisfaction with results obtained, (b) loss of interest, and (c) failure of association to establish local points of contact with members, all of which result in an insufficient volume of business.

4. Economic conditions: such as price declines and falling off in demand either in domestic or export markets.

5. Internal dissensions: due to selfish motives and the playing of politics on the part of officials.

Besides examining the causes for failures of defunct organizations, the reasons for the successful operation of going concerns may also suggest the elements that pave the way to success for other companies. It is impossible to determine to what extent success is dependent upon any particular reason or combination of factors, hence the following necessary operating features for successful operation are not necessarily listed in their order of importance.

#### ESSENTIAL OPERATING PRACTICES

1. An association must be efficiently managed. Whether or not a manager is capable, honest, and likable very often determines the success or failure of an association. The manager should be adequately compensated for his services, receive the cooperation and assistance from a capable board of directors, and be in sympathy with the cooperative movement.

2. An association must have sufficient volume of business for economical operation. Insufficient volume is a serious handicap.

<sup>5</sup>Cooperative Marketing, letter of Chairman of Federal Trade Commission, Senate Document 95, p. LI, 70th Congress, 1st Session.

Unit costs can be reduced with volume. One of the main reasons for a cooperative is to lower the cost of marketing—this requires volume.

3. An association must have the loyal support of its membership. In this respect a cooperative is quite distinct from a private business. Without the loyal backing of its membership, a cooperative is doomed for it cannot depend upon nonmember business for its success. Hence, well-informed, satisfied members are indispensable to an association.

4. An association must be soundly financed. This means in most cases that at least half of the fixed capital should be provided by the members. It means further the efficient use of adequate capital, building up of reserves, and intelligent budgeting. All members should have a financial investment in their company. It is one of the ties that bind members to their organization. It is evidence of the faith that members have in their company and has a stabilizing influence.

5. An association must serve an economic need. The justification of any association rests in the fact that its members achieve more satisfactory results from collective effort than is otherwise obtainable through individual effort. Therefore, a more satisfactory service must be rendered by the association. Merely duplicating existing agencies is insufficient reason for commencement or operation of a company. The greater the need and the more satisfactory the service performed, the more lasting the association will be.

In addition to the above features which are considered absolutely essential to successful operation, factors that contribute in varying degrees to success may also be listed. Some associations may place major importance upon certain of these factors as being the primary reason for their particular success.

#### FACTORS CONTRIBUTING TO SUCCESS

1. An association should handle high quality products. In order to establish itself firmly an organization should strive to place uniform, high-grade, well-packed products on a market. It is often said that "good products sell themselves but poor products can't be given away." Quality products get the premium prices in a market—poor ones do not. Without exception

the best known and most successful cooperative sales associations are scrupulously careful in placing only the highest grade products on the market under their brand names. All emphasize and re-emphasize quality production, careful grading, and standardization.

2. An association should consist of producers with similar interests. Producers having production and marketing problems that are alike cooperate much better than producers with divergent interests. This suggests, therefore, that local associations be established whenever possible. Farmers living close to each other and knowing one another can cooperate more easily than if farmers of one part of a state or region are to associate with farmers from another section.

3. An association should be organized on a commodity basis. Organization on a geographical basis, *i.e.*, having one association in a locality handle all of the farmers' products produced in that locality, is often economically unsound. The great divergence of producers' interests, the difficulty in allocating costs between the different products, and the task of intelligently marketing each of many different products create far greater problems than those brought about in single commodity marketing associations. Marketing of single commodities, or of closely allied commodities, enables the association to use the same facilities, methods, equipment, and trade channels for all products. In addition, the association embraces farmers with similar marketing and production interests.

4. An association should have an organization suited to its needs. It should be flexible enough to meet changing conditions, representative of all its members, and not burdened with exorbitant costs. Facilities and equipment should meet the needs of the association and not be for show purposes. Extravagance has no place in a cooperative. The association should be incorporated, have suitable bylaws, and adopt operating policies designed to achieve the immediate objectives of the membership.

5. An association should keep records and accounts. Careful bookkeeping is an even more important requisite of a cooperative than of a private business. In order that patronage dividends may be correctly disbursed, it is necessary that a record be kept of each member's business. The fact that patronage and membership are linked together in a cooperative makes it expedient that records be kept in a careful manner. Likewise,

the management is the hired agent of the association answerable to all the members. Therefore, proper records are essential.

6. As nearly as possible an association should conduct its business like that to which the members have been accustomed. This does not mean to operate at high cost, unethically, or to furnish poor services, all of which the association wishes to correct. It does mean to prevent delays in payment, to provide marketing facilities of the kind with which members are acquainted, and to deal with brokers, jobbers, and other market agencies in a manner to gain their confidence. Cooperative marketing succeeds best when it is an evolutionary process instead of a revolutionary one. The cotton cooperatives learned the sanity of this observation 10 years ago. Today, optional pools, which involve cash selling, supplement the former seasonal pools; interior classing offices take the cooperative to the growers in place of requiring the producers to ship their cotton to distant central classing offices; and flexible, revocable contracts have taken the place of the long-term, ironclad five-year contracts. The objective of a cooperative marketing system is difficult enough for some to perceive without complicating matters with many new innovations in methods of handling and pricing policies.

7. An association should remain cooperative in spirit and farmer owned and farmer controlled at all times. Producers should retain control of their organization. Their interests as producers desiring a more efficient marketing system should not give way to an interest in the association as an investment medium. The object or purpose for which the association was established is to return the highest price possible to the producer for his product—not as high a dividend upon capital as possible. If members feel that the association has slipped out of their hands into those of a minority clique, failure will soon follow.

8. A large-scale association should establish means and methods of contacting its membership. In a federated association this is done rather easily through local associations, but in centralized associations some kind of local group action is essential. Having members in a community buy stock in a local warehouse or processing plant controlled by the centralized association is one way to maintain interest. Establishing local receiving stations where the overhead organization can be constantly in touch with its membership, such as the interior

classing offices of the cotton cooperatives, has done much to keep the members' loyal support.

9. An association should use membership contracts. The contract is especially valuable in the early years when an association is the target of severe and oftentimes ruthless competition. Most associations have found that a flexible contract gives the association a measure of stability otherwise unobtainable. By no means is a contract to be considered a substitute for voluntary cooperation.

10. An association must pay its members as much for their products as its competitors do. An occasional unfavorable price comparison will not break an association but repeated unfavorable comparisons will. Members belong to a cooperative to improve their marketing, which means for most farmers to get better prices. An association may render better service to producers than they formerly received, yet, if improved services are not accompanied with prices equally as high as could be received from outsiders, the association will constantly have difficulty. Even though price comparisons are generally meaningless and often erroneous, members will continue to make them and behave accordingly. Competition must be met if success is to follow.

The late George O. Gatlin prepared a list of factors which he believed led to failure of an association. This is a negative way of pointing out the road to success just as was the listing of the reasons for failures and suspensions earlier in this chapter.

#### FACTORS CONTRIBUTING TO FAILURE

1. An organization should not admit as members men with conflicting business interests. It is difficult to maintain harmony and singleness of purpose when nonproducers, buyers, and men of contrary or conflicting interests are grouped with bona fide producers of identical interests.

2. An organization should not conceal from its members facts regarding its operations. Misleading statements, juggling funds, secret contracts, and similar practices undermine confidence. The organization belongs to the membership, not the officials and employees. There cannot be proper cooperation where there is suspicion.

3. An organization should not permit the engineering of elections and the appointment of officers by a self-perpetuating group. Democratic control must be more than a promise. Those elected to represent the members must represent them in fact, if the association is to be cooperative.

4. An organization should not rely upon force to maintain member cooperation. Threats, lawsuits, and coercion break down rather than

build up the support of the growers. Coercion is the opposite of cooperation.

5. An organization should not sacrifice cooperative principles to obtain volume of business. Encouraging its members to purchase products for delivery, admitting buyers to membership, selling for non-members, and buying for its own account to increase volume tend to eliminate or minimize cooperative features.

6. An organization should not maintain an overhead expense out of proportion with the service required. Salaries should be commensurate with service rendered. Jobs should not be provided as rewards to organizers or bribes to commercial interests.

7. An organization should not attempt arbitrary price fixing based on monopoly control. A price that does not reflect supply and demand conditions brings about an economic readjustment that reacts upon the organization. No cooperative association can "fix prices" successfully over a period of years unless the price fixed is the "right price."<sup>6</sup>

#### Questions

1. If some producers of livestock, wool, or cotton were anxious to organize a local cooperative marketing association, what should be ascertained before a cooperative is started?

2. What should be considered by farmers before a cooperative supply-purchasing association is established?

3. Why is it essential that an "economic need" for a cooperative association exist before operations are started?

4. What problems of a local association are solved best by a central marketing association?

5. Critically appraise the bottom-up and the top-down methods of organizing a central marketing association.

6. What various committees may be used to advantage in setting up a cooperative association? What functions would each serve?

7. "The greatest possibilities of improvement in the marketing system for the cooperative lie between the farm and the retail market." Evaluate this statement.

8. What conclusions were arrived at by the Federal Trade Commission regarding the causes of failure of cooperatives?

9. Find out from your secretary of state what papers must be filled out and filed, on what dates meetings must be held, length of time that notices of meetings must be given, amount of fees, and the differences in the incorporation papers for a nonstock company from a capital stock association.

10. Are cooperative associations more easily organized during periods of depression than during periods of prosperity in agriculture? Or, does the economic condition of agriculture have no bearing upon the time when marketing and purchasing associations are organized in largest numbers?

<sup>6</sup> GATLIN, GEORGE O., Elements of Cooperative Marketing, Oregon State Agricultural College, *Extension Bul.* 429, p. 3, 1930.



## IX

### *Types of Cooperative Associations*

*There are four main classes of cooperatives—sales associations (also called “marketing associations”), purchasing associations, service associations, and workers’ cooperatives. In the sales associations and most purchasing associations only farmers are members. Consumers’ cooperatives in America have chiefly farmers as their members. The service associations provide their members with services rather than with commodities and are found in both urban and rural centers. Workers’ cooperatives do not supply their members with services or commodities, but provide associations through which workmen can pool their labor.*

*The cooperative sales organizations may be either local or regional in scope. They may consist of only independent local groups or of a federation of local associations. For some commodities a number of federations have been united into national marketing associations. The centralized association, a regional marketing association whose membership consists of farmers directly, differs from the federated association in that autonomous locals are omitted in the scheme of organization.*

*Not all cooperative marketing associations render a complete marketing service. Some, the bargaining associations, chiefly bargain over prices with the buyers of farm products; others, the sales agencies and cooperative commission firms, render primarily a selling service but do no storing, packing, advertising, financing, and other marketing services such as the usual marketing cooperatives perform. Most associations are single commodity organizations, but some are multiple commodity associations. There is no rule-of-thumb method of determining which structural form of organization should be used.*



## CHAPTER IX

### TYPES OF COOPERATIVE ASSOCIATIONS

Individuals constitute the membership of cooperative associations. The objectives of these individuals differ considerably, however, and for that reason different types of associations are organized. There is no uniformity of opinion regarding their classification. Some think of only two main divisions, namely, agricultural producers' associations which sell farm products and which buy farm supplies, and consumers' cooperative associations which handle commodities and provide services. The following terminology and the types in the order of their importance are suggested.

#### I. Cooperative Sales Associations (also called Farmers' Cooperative Marketing Associations)<sup>1</sup>

1. Commodity marketing associations
2. Collective bargaining associations
3. Sales agencies

<sup>1</sup> Marketing in its broadest meaning embraces both selling and purchasing. Buying and selling are integral parts of every transaction and since the transaction is a vital part of all that constitutes marketing, it is evident that buying as well as selling falls under the generic term "marketing." Marketing, besides including the transaction, embraces all of those production activities that give time, place, form, and ultimately possession utility to an article. From common usage the term marketing has been applied to all of those functions necessary to sell an article, *i.e.*, assembling, grading, packing, packaging, inspecting, storing, financing, transporting, bearing risk, advertising, and selling. Thus, when the manufacturer and farmer speak of their marketing problems, they refer to the problems incident to the distribution and sale of their products. It is in this narrower sense that the term "cooperative marketing" has been widely applied to farmers' cooperative sales associations and not to the agricultural cooperative purchasing associations. Though the correct term for farmers' cooperative associations engaged in selling farm products is "cooperative sales associations," long-time and widespread usage of the term "cooperative marketing associations" may be considered as synonymous with it. For those sales associations that also handle farm supplies and sell these to their members the latter term would be eminently correct.

- II. Cooperative Purchasing Associations
  - 1. Agricultural purchasing associations dealing in producers' goods.
    - a. Retail associations
    - b. Wholesale associations
  - 2. Consumers' cooperative associations dealing in consumers' goods.
    - a. Retail associations
    - b. Wholesale associations
- III. Cooperative Service Associations
  - 1. Finance associations
    - a. Credit unions
    - b. Cooperative banks
    - c. Production credit associations
  - 2. Insurance associations
    - a. Farmers' mutual fire insurance companies
    - b. Mutual insurance companies—automobile, life, etc.
  - 3. Mutual telephone companies
  - 4. Electric associations
    - a. Rural electrification associations
  - 5. Drainage and irrigation associations
  - 6. Truck associations
  - 7. Medical and hospital associations
  - 8. Miscellaneous associations, such as restaurant, housing, recreational, dry cleaning, bakery, burial, fuel, garage, laundry, publishing, etc.
- IV. Workers' Cooperative Associations
  - 1. Labor associations or labor unions
  - 2. Agricultural laborers' associations
    - a. Threshing rings, shredding rings, spraying rings
    - b. Collective farming
  - 3. Industrial workers' associations
    - a. Workers' self-help cooperatives

#### WORKERS' COOPERATIVE ASSOCIATIONS

Workers' cooperatives are sometimes called "producers' cooperatives."<sup>2</sup> In these associations the *labor* of workers is

<sup>2</sup> The authors suggest the more definite term "workers' cooperative associations," in preference to the broader term "producers' cooperatives." The term "worker" refers more especially to a laborer, a wage earner, a toiler, and a nonsalaried employee. The broader term "producer" includes the entrepreneur, employer, and capitalist as well as the laborer. Both, employers and laborers, produce. The type of cooperative referred to here, however, includes only those that labor rather than those that manage and direct industry. Hence, the narrower term is more definitive and preferable. The term "producers' cooperatives" is used by some writers in contrast with consumers' cooperatives to denote agricultural cooperative sales associations. In view of such varied uses of the different terms the reader is advised to note texts carefully to observe what precise meaning the different authors ascribe to the terms used.

pooled. In the labor union, which is one type of workers' association, workers depend upon collective bargaining with employers to determine the wages and conditions of employment under which such collective labor will be rendered. Agricultural laborers also pool their labor when they organize threshing rings, shredding rings, or spray rings to accomplish certain farming tasks. They might go even farther, as in Russia, and organize collective farms where many laborers cooperate to perform all farming operations on a collective basis. During the depression years, numerous self-help cooperatives were organized throughout the United States by unemployed workers. At first the workers made many different things and exchanged these with one another on a barter basis. Later, however, production was specialized and the proceeds from the sales were divided among the laborers.<sup>3</sup> Although the self-help cooperatives were liberally financed and aided by government relief agencies, it is apparent that workers could own and operate the plants in which they work and receive sufficient income from the products produced to support themselves without governmental aid. Hall and Watkins refer to these industrial workers' associations as "cooperative copartnership productive societies." The Franklin Cooperative Creamery Association of Minneapolis is an illustration of an employees' and consumers' cooperative. To quote from the 1930 *Yearbook of the Cooperative League* (page 165), "It was a wise thing that the men organized the Franklin as a consumers' cooperative, instead of a producers' cooperative owned and controlled exclusively by creamery workers, as the original plan had been."

#### COOPERATIVE SERVICE ASSOCIATIONS

Cooperatives that render services rather than provide commodities for their members are called "service associations." These may be organized by city folks to be of special services to them or by farmers for their special needs. The most important are the finance associations which pool the savings of the members. The credit unions, cooperative savings banks and banks for cooperatives are illustrations of the finance associations. The cooperative insurance companies pool the risks of its policy holders

<sup>3</sup> Self-help Cooperatives, bulletin by Division of Self-Help Cooperatives, Federal Emergency Relief Administration. See also March and August, 1936, issues of *Monthly Labor Review*, Bureau of Labor Statistics.

whereas the electric and telephone associations provide utility services on a cooperative basis. Most of the service associations of today are organized by farmers with the notable exception of the credit unions and some of the types falling in the miscellaneous class. Both the cooperative financing associations and cooperative insurance companies named in the above classification are today so prominent that some writers list them as distinct types of cooperatives, but important as they are, they logically fall as subclasses under the heading of Service Associations. Service associations may consist of either *local* associations, as a local credit union, or of *regional* associations, as the cooperative automobile and life insurance companies.

#### COOPERATIVE PURCHASING ASSOCIATIONS

A cooperative purchasing association combines the purchasing power of buyers and aims to provide its members with high quality products at the lowest possible prices and with services that are essential and gratifying. These objectives are sought by members whether the associations sell producers' goods, as in the case of farm supply companies, or consumers' goods, as in the case of consumers' grocery stores, meat markets, department stores, or urban filling stations. Irrespective of the use to which the product is put the objective of pooling the purchasing power of the buyers is identical in either case. In each type members are buyers and as such are influenced by motives affecting buyers. For sheer practical reasons and for the purpose of identifying one class of purchasing associations from another, it is desirable to distinguish the consumers' cooperative associations dealing largely in consumers' goods from the agricultural purchasing associations whose membership consists of farmers and which deal almost solely in producers' goods. Whereas the Banks for Cooperatives are permitted, under the interpretation of the Farm Credit Act, to lend to associations that purchase farm supplies, they cannot lend to associations that buy household goods as the consumers' cooperatives ordinarily do. Reasons for this separation into these two subclasses will become apparent in subsequent paragraphs.

The term "consumers' cooperation" is not correctly used as synonymous with "cooperative purchasing associations" as

some would like to have it used. It is more apropos to confine it to the cooperative purchase of goods which consumers usually wish to consume directly. "Buyers' cooperatives" would be a more fitting term to encompass all cooperative purchasing if a synonym were to be named, but it is preferable to adhere to the broad term "purchasing associations" as was used in the classification on a previous page. When individuals purchase collectively they do not act as consumers, but as buyers. If they buy for immediate consumption then their interests as consumers predominate, but if they buy for the purpose of furthering production, then their interests as producers receive uppermost consideration. In the former case personal gratification from consumption is sought, in the latter, economy in production is aimed at.

**Scope of Consumers' Cooperatives.** The object of a consumers' organization is to advance the interests of individuals as consumers, not as producers. From a strictly practical standpoint, it proposes to increase the purchasing power of its members' incomes, not the incomes themselves. These are derived from many different sources or occupations. The interest of the member in such an association is that of a consumer, not that of a workman, and emanates from the home, not from the workshop, the mine, or the farm. The objective is not to change the conditions of employment, but to raise the plane of living. In other words, this type of cooperative does not presume to enlarge a member's money income, but it does propose to increase his real income. Members hope that their incomes will be spent in such a manner through the consumers' cooperative that the best service and the largest quantity and highest quality of products can be obtained for the money. A consumers' commodity association buys commodities for consumption purposes for its members. It handles consumers' goods, not producers' or capital goods if the economists' classification of goods is used. Groceries, clothing, and furniture are consumers' goods. Consumption credit as provided by a credit union, electricity for the home, telephone service for domestic purposes as against business purposes, housing in cooperative apartments, recreational facilities, and cleaning and dyeing services are consumers' services which consumers' cooperative service associations provide.

Cooperative retail grocery stores serving *local* communities are the most common type. Such locals are owned and operated by the member-patrons. They are autonomous and may or may not be affiliated with *regional* wholesale societies. Cooperative wholesale associations serving local associations within a region may pool their purchases and maintain a *national* wholesale. Thus, the local cooperative retail store at Cloquet, Minn., is a member of the Central Cooperative Wholesale at Superior, Wis., and the latter association derives some of its products (automotive) from the National Cooperatives, Inc. Some cooperative wholesale associations have sufficient volume of business to warrant the establishment of factories or processing plants. Such cooperative production, usually carried on by a subsidiary corporation of the wholesale association, is not nearly so extensive in the United States as in England, Scotland, Sweden, and Norway. Cooperative bakeries, coffee roasting plants, and oil blending plants are, however, run by cooperative purchasing associations in this country.

**Scope of Agricultural Purchasing Associations.** The chief purpose of an agricultural cooperative is to advance the interests of its members as producers. In the economic sense a product is not fully produced until it has the form, time, place, and possession utilities which a consumer demands. Before a farmer can be a consumer, he, of course, must be a producer, and the amount of consumption goods and services he can command is governed by the extent of returns he receives from his production operations. Hence, the cooperative sales association is considered by him as the instrument to enlarge his gross sales returns and increase his productive operations by adding utilities to his product over and above those they had when they left his farm.

Farmers' purchasing associations are likewise designed to advance the producer interests of its members. These associations handle producers' or capital goods—seeds, feeds, fertilizer, fencing materials, farm machinery, tools, insecticides, paint,—and not consumers' goods. As a buyer and a producer, a farmer desires to obtain these production goods at the lowest possible cost and of the best quality in order that his net returns from his productive operations may be as high as possible. The same logic applies to the purchase of different services. Electricity

to operate electric motors, fire insurance on his farm buildings, cooperative credit to finance his fixed investment and current operations, mutual ownership of irrigation and drainage projects, and trucking of his farm crops and farm productive supplies are producers' services he hopes to obtain at reduced costs in order that he may enhance his net returns from his farming operations.

It is true, however, that there is an overlapping of both a producers' and consumers' interest in those agricultural purchasing associations that carry consumption goods as well as production goods or goods which may be used for either purpose. Farmers, like city folks, have interests as consumers in certain cooperative organizations. There is no reason to suspect that this interest is any less for farmers than for urban dwellers. When a farmer buys household necessities or consumption goods from an agricultural purchasing association, his interest in such purchase is that of a consumer. In many cases there is a complete overlapping of these interests. For example, gasoline bought for a farm tractor is capital goods, but for the family car used on a pleasure jaunt is consumer goods. Here, the cooperative oil station serves both interests. Rural cooperative grocery and general stores which handle essentially consumers' goods fall, of course, into the category of consumers' cooperatives.

#### COOPERATIVE SALES ASSOCIATIONS

The cooperative sales association, as distinct from the purchasing association, markets the products of its members who produced the same on their individual farms. Since the cooperative marketing associations have been organized by farmers for the purpose of selling their products, they have been called cooperative sales associations, farmers' or agricultural cooperative marketing associations, and agricultural producers' associations. This last term, however, is vague and misleading since it may refer to cooperative production on farms. Although common usage applied the last term to farmers' cooperative sales associations and although no cooperative production on collectively owned farms is common in the United States, therefore, not imputing an erroneous meaning to the term for many, still it may create confusion and suggest a type of cooperative practice not engaged in if we persist in the usage of such misleading nomenclature.



Marketing associations, like the purchasing associations, may engage in production operations where goods are manufactured to be used by the cooperative or sold to the cooperative's members. Thus, a manufacturing plant run as a subsidiary of a cooperative may make boxes, baskets, or berry crates which are sold to the members or used by the cooperative sales association itself. Approximately 2,400 agricultural sales associations also purchased supplies, equipment, and other farming necessities for their members although their chief business is that of selling members' farm products. For the remainder of the chapter the special types of agricultural cooperative sales associations and purchasing organizations will be discussed.

#### TYPES OF COOPERATIVE SALES ASSOCIATIONS

It is possible to point out many types of cooperative sales associations depending upon the basis of classification used. From the standpoint of structural setup, certain types of organizations are more important than others. The outline below indicates the basis of classification and types of associations under each.

##### Basis of Classification of Associations

1. Size of territory or area served
  - a. Local associations—members reside in local areas
  - b. Regional associations—members reside in a region of the country
  - c. National associations—membership resides throughout the nation
2. Membership affiliation
  - a. Local associations—farmers are members of locals
  - b. Federated associations—farmers are members of locals which are members of a central organization
  - c. Centralized associations—farmers are members of a central organization
  - d. Combination association—has elements of federated and centralized associations.
3. Nature of operations
  - a. Marketing associations—perform a series of marketing services
  - b. Collective bargaining associations—essentially, bargain for a price without handling the products
  - c. Sales agencies—operate according to commission method
4. Financial form
  - a. Capital stock associations—sell shares of stock to members
  - b. Nonstock or membership associations—issue membership certificates

5. Legal form
  - a. Unincorporated associations—not incorporated under any state or federal laws
  - b. Incorporated associations—incorporated under some state or federal law
6. Commodity handled
  - a. Single commodity associations—handle one or a few closely allied products
  - b. Multiple commodity associations—handle a number of unrelated products
7. Method of handling farmers' products
  - a. Associations purchasing farm products upon delivery
  - b. Associations selling each farmer's products on private account
  - c. Associations pooling products, sales receipts, and expenses
8. Contractual arrangements
  - a. Contract associations—use membership contracts
  - b. Noncontract associations—no membership contracts used
9. Volition
  - a. Voluntary associations—farmers choose to be members or not
  - b. Compulsory associations—farmers are required to market through the associations

Any particular association may fall under some or all of the above classifications. Thus, the California Fruit Growers' Exchange is a regional, federated, marketing, capital stock, incorporated, single commodity (citrus-fruit), pooling, contract, voluntary association. A local milk-bargaining association is ordinarily a local, collective bargaining, nonstock, incorporated, single commodity, contract, voluntary association. The differences between the major types of associations named will follow.

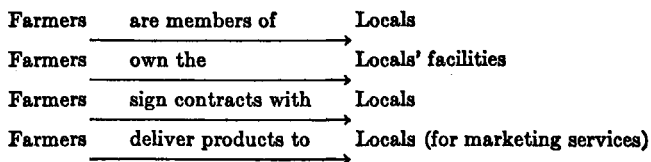
#### LOCAL ASSOCIATIONS

Farmers are the members of local associations. Membership is obtained by purchasing a share of stock, or a membership certificate, or by signing a marketing contract. The name suggests that the membership resides in the usual trading area about some small town or village. It is essentially a neighborhood enterprise, composed of producers with similar interests in production and marketing. The cheese factory with its two dozen members, the creamery with its 100 to 300, the livestock shipping association with its 75 to 200 members, the fruit packing house with its 25 to 100 members, the local elevator company, the local potato warehouse, and the local egg-auction company are illustrations of local associations. More than 90 per cent

of all farmers' cooperatives are local associations. Farmers own and operate their local marketing facilities, products are delivered to the local association's processing plant or warehouse in the case of marketing associations, and contracts, if used, bind the farmers and the local association. A local collective bargaining association does not handle the members' products but acts as the bargaining agent for the farmer in the sale of his goods to regularly established private dealers.

The services which a local association performs depend upon the kind of commodity handled or the purpose of the association. A local cheese factory, creamery, and condensery are primarily engaged in the efficient processing of milk and cream into finished dairy products; a local cotton gin renders essentially a ginning function; a local grain elevator purchases grain and stores and loads it into cars to be sent to terminal market dealers; a local milk bargaining association bargains with private milk dealers over the sales price and conditions of sale, and checks weights and tests. The functions are limited to those ordinarily found in the country market—no comprehensive sales or advertising program is carried on. The purpose of the locals is to lower the costs of handling collective lots of products and to obtain if possible some price advantage by offering carload lots to terminal market operators. Usually someone from the local community acts as manager, farmer-members are on the board of directors, and members finance the company, assisted at times by loans from local credit institutions. The associations are autonomous and may or may not be affiliated with an overhead organization for the purpose of marketing their members' products or purchasing their supplies. Locals may be incorporated or unincorporated, may or may not use marketing contracts, and may handle only one or several commodities. Many not only handle the products which farmers have to sell, but the products which farmers buy for their farming operations and household economy.

Diagrammatically the relationship of the farmer to his local can be shown as follows:



What are the strength and weakness of a local association? Its strength rests largely in that (1) members know each other; (2) all have the same marketing and production problems—therefore, a unity of interest; (3) the business is usually easily understood and conducted by the farmers; (4) members have confidence in the local manager whom they know and regularly meet; (5) the association is the basis of the democratic federated type; (6) it is an effective medium for extending marketing and production information to the members; (7) if successful, marketing services, known to be inadequate, are improved and as a result the members' whole-hearted support and loyalty are enlisted.

The weakness of a local association rests chiefly in its inability to perform marketing services beyond the local market. It does not go farther than the first step in the marketing channel, hence its influence is greatly restricted. It has in fact very little bargaining power. Unassisted by other locals, it cannot possibly cope with dealers in the terminal markets. Consequently, problems of major marketing significance that were listed on page 192 would go unsolved unless a regional association of the federated or centralized type were established. In recognition of this weakness, private dealers in terminal markets have not discouraged local cooperation so that the local associations may be excellent sources of supplies for them but have looked askance at any regional marketing associations with which they might have to compete. This is simply a recognition of the fact that local associations had no influence in any other than the country markets and that much of the benefit derived there may be nullified by dealers in terminal markets "as these interests through understandings, sharp practices, and many other sometimes questionable competitive methods were able to destroy in a large measure whatever advantage had been gained through these local organizations." A more complete control of the marketing operations was imperative. Regional associations filled this need.

#### FEDERATED ASSOCIATIONS

The federation is one of three types of large-scale regional associations. The other two are the centralized and combination form of associations. It was recognized long ago that the influence of a local association was limited to marketing at coun-

try points and that, if the gap between farmer and consumer were to be bridged more completely, large-scale marketing associations that operate in the wholesale assembling or wholesale distributing markets would be needed. The federation is one type of the central market organization that performs this function. As the name suggests, a federation is a cooperative organization of existing local associations for the purpose of selling the products which the member locals receive, grade, pack, and prepare for shipment. The federation goes farther along the marketing channel than the local association can. It copes with problems of selling, advertising, merchandising, pricing, transportation and claims, financing, collections, quality improvement, controlling the flow of products to markets, adjusting production, utilization of by-products and cull products, production and marketing research, and such other industry-wide problems that only a large-scale association can possibly solve. A federation has the dual task of assisting its local associations in their production and local operating problems and of conducting its own affairs as a terminal marketing association in the most efficient manner. A federation may be a regional *marketing* association in that it handles its members' products and performs such services as terminal assembling, grading, standardizing, processing, packing and packaging, branding, storing, selling, financing, and pricing of the products (*e.g.*, California Walnut Growers' Association); it may be a regional *bargaining* association in that its principal function is to bargain for a price, terms, and conditions at which its members will sell to established local dealers who perform the necessary marketing functions (*e.g.*, Interstate Milk Producers' Association, Philadelphia); or it may be a regional *sales agency* which merely sells its members' products on a commission basis but does not otherwise perform a whole series of marketing functions for the product (*e.g.*, Producers Livestock Commission Association, East St. Louis).

The military plan of organization is a distinctive feature of a federation. Farmers are members of local associations, locals are members of district associations, and district associations are members of the central overhead association. If no district associations exist, then the locals are members of the central association. This structural arrangement can be illustrated in the California Fruit Growers' Exchange—13,300 fruit growers

are members of 200 autonomous local packing associations, these locals have membership in twenty-six self-governing district exchanges, and finally these district exchanges are federated into one central organization that has headquarters in Los Angeles. Farmer members elect from five to seven directors in each local association making a total of about 1,400 directors in the entire exchange system; the locals that belong to a district elect directors to govern the district exchanges; and each district exchange elects a director on the central board—twenty-six in all—which manages the affairs of the central organization. Farmer members sign contracts (usually a 5-year, annually revocable) with the local associations. The locals sign long-term revocable contracts with the district exchanges and the latter sign long-term contracts with the central exchange.

The local associations of the exchange receive, sort, grade, and pack the oranges and lemons in the local packing houses. Sometimes the locals also fumigate and prune the orchards and pick the fruit for their members. Each local pools its members' fruit by variety and grade in pools that are semimonthly, monthly, or seasonal. Although each local may sell its fruit independent of the central sales organization, very little of such selling is actually done since the district exchanges are in a much better position to advise the locals when, where, and at what price to sell. The costs of operating the locals are distributed among the patrons.

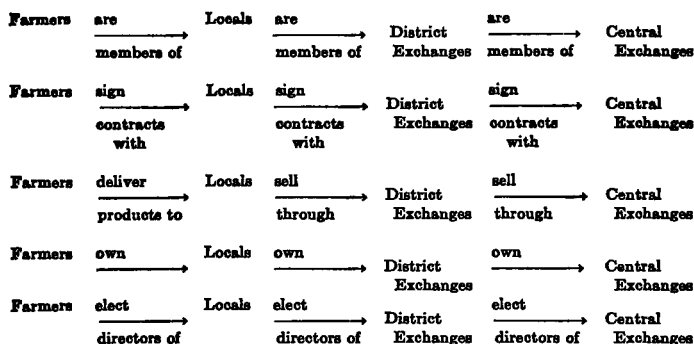
Each district exchange consists of a number of locals varying from two to twenty-two. Some district exchanges include in their membership individuals who are not affiliated with any local association. The district association acts as advisory agent for the locals, as sales agent, disseminator of market news, and as a general intermediary between the locals and the central exchange. Unless a purchase order specifies that fruit is to be shipped from a certain local packing house, the district exchange manager apportions the orders between local associations. Cars are ordered and sales remittances are made by the district association to the locals. Sales cannot be made by the central exchange or its representatives at prices that are not approved by the district or the local associations.

The central exchange is organized on a nonstock basis and is the coordinating unit of the entire system. Its principal function

is to sell fruit for the 13,300 growers. For this purpose it has established definite grades, a popularly known brand, Sunkist, and sales representatives in about fifty leading wholesale distributing markets. It spends millions of dollars advertising its members' fruit, develops new markets, and through research discovers new uses for fresh fruit and processed fruit juices. It deals directly with brokers and auction companies and with sales agents in foreign markets. In order that fruit may arrive in the best condition at different markets, inspectors are stationed at strategic points to inspect cars of fruit en route as well as at destination. While in theory the district exchanges sell the fruit with the authority of the locals, in practice much of the selling is actually done at the suggestion of the central exchange. Here is an integrated system of marketing that, through a delegation of duties, places the individual fruit grower in touch with the entire national market for citrus fruit. Special departments of the central exchange deal with problems of transportation, orchard production, field service, and legal matters. Besides these matters relating directly to the sale of fresh fruits, the central exchange has established three subsidiary companies—one to utilize cull oranges for the manufacture of marmalades, orange juice, and other processed products, one to utilize cull lemons in a comparable manner, and one to secure orchard and packing-house supplies for its members. In the exchange's lumber mill and box factory, packing boxes are made from lumber produced in its own forests.

The California Fruit Growers' Exchange is one of the best known of the federated types of marketing associations. Other federations may not carry on so many functions or integrate their operations so well as the citrus exchange. But the difference in structural organization and function is one of degree and not of kind. Diagrammatically the federated type may be as shown at the top of page 219. Modifications in certain organizations are found.

Ordinarily it is the custom of a federation to be established after local associations have been operating for some time. The federation is, therefore, considered as being built from the bottom up. But it is not uncommon to find successful federations that were conceived and established at the same time that local associations were fostered. Several general farm organizations



that set up new systems of marketing farm products proposed a federated system and established local associations and a federated sales organization at the same time. Many federations have been the chief organizing agent of local associations which become affiliated with the central organization. Thus, the fieldmen of many federated cooperative livestock commission firms have taken a lead in organizing local livestock shipping associations that become members of the cooperative firms. In 1936 there were about fifty active large-scale *marketing* federations and an equal number of federated *sales agencies*.

The strength of the federation rests on (1) its democratic form of government; (2) upon the authority, control, interest and responsibility that rest in the members at all times; (3) on the fact that the federation is built from the ground up in which the importance of self-governing local associations is recognized; (4) upon the relatively greater ease of keeping contact with the membership than in the centralized association through the long established local and district associations; (5) upon the fact that through experience gained in operation of locals the federated association has learned that it can have more beneficial influence on prices through improving the quality of products, rendering better marketing services, and working with the established dealers in the market than through attempts at controlling or fixing prices following the control of a major portion of a crop.

CENTRALIZED ASSOCIATIONS

A second type of regional organization is the large-scale centralized association. It became most widespread from 1920 to

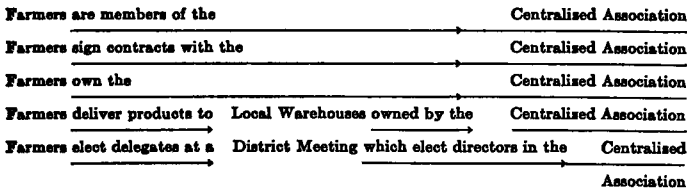


1925. Starting on the Pacific Coast, it soon spread to all other sections of the country, particularly throughout the South. Most important commodity associations organized according to this type are the cotton and tobacco associations, but such commodities as wool, rice, grain, poultry and eggs, nuts, and fluid milk were also organized in this manner. Unlike the federated associations, autonomous local associations are dispensed with. Most of the centralized associations organized during 1920-1923 came into existence after high-pressure promotional campaigns had stirred farmers to sign long-time marketing agreements with the central association. Usually a large proportion of the crop had to be signed up before the association started functioning. Farmers became members directly of the centralized association through purchase of membership certificates, or shares of stock and through signing marketing contracts. In this type of association control and authority are centralized in the headquarters organization whereas in the federated association control is decentralized in the autonomous local associations. In many respects the structural organization of the centralized association has certain features of a local association. Instead of having the membership within a small trading area about some local shipping point as the local association has, the centralized association has its membership spread over a part of a state or over one or more states. As a result, members may live several hundred miles from headquarters. This necessitates districting of the association in order that contacts may be made between the central headquarters and the membership, and in order that the members may elect their own representatives on the central board of directors. Such informal, unincorporated local associations within the centralized organization are for the purpose of maintaining a cooperative spirit among the membership, of providing a governing unit to elect directors, and of providing a center for information between the membership and the distant headquarters of the company.

Members' products are received, sorted, graded, pooled, and prepared for sale to market operators at warehouses or local packing houses operated, owned or leased by the central association, not by the farmers who deliver to them. The central organization also has charge of all functions incident to the market distribution of its members' products. In fact it has

charge of the functions both of locals and of the central exchange of a federated association. Most of the associations organized in 1920-1923 aimed at controlling such a large proportion of the market supply in order that the association could have monopoly power in the market. This object of price fixing is no longer considered vital to the success of centralized associations by their leaders and managers. Today many centralized associations in their method of conducting their sales operations are no different from federated associations.

In actual practice varying degrees of market integration, and of structural organization are found among the hundred large centralized associations with a membership of somewhat less than a half million producers. Diagrammatically the association and its relations to its members can be shown as follows:



This type of association has certain laudable features: (1) it is usually organized in a relatively short time, (2) it is particularly valuable in those cases where a strong central control is advisable (sometimes dominant central authority can accomplish things in a quicker and better fashion than decentralized management can); (3) it recognizes that volume is essential to reduce costs, insures more economical use of by-products, and is an important factor in the determination of market prices.

One of America's most successful centralized marketing associations is the Washington Cooperative Egg and Poultry Association with headquarters at Seattle, Wash. Organized in 1917 as a capital stock company with a membership of 117 producers, it has expanded in 19 years to a point where it now has nearly 18,000 members. Commencing with \$473 of working capital, it had \$1,516,125 of common stock and \$1,304,817 of preferred stock outstanding on Dec. 31, 1935. On this date it also had \$1,005,302 in reserves and surplus. Members own stock in the central association and irrespective of the number of

shares of common stock held, each has but one vote. A board of trustees consisting of sixteen members, fifteen active poultrymen and one selected by the State Director of Agriculture, directs the affairs of the company. Under its plan of financing, a deduction of 1 cent per dozen eggs and  $\frac{1}{2}$  cent per pound of poultry is made from each members' sales receipts which pays for additional shares of stock. After all authorized stock has been issued, the stock will be redeemed in the order of its issuance from the revolving fund created by the deductions. In this manner the control of stockholdings rests with the active members. Patronage dividends accruing from the feed department are paid to growers in the form of preferred stock bearing 8 per cent interest. The earnings are retained to provide working capital, but, when sufficient capital has been accumulated, the oldest preferred stocks are retired from the revolving fund.

The association operated twenty-six branch stations in 1935 in all of the principal egg producing sections of the state at which eggs and poultry were received and at which feed and supplies were sold. A fleet of 120 trucks was used to assemble eggs and poultry from its members' farms and to deliver feed and supplies. Nine mills at which feed is ground and mixed are in operation. In 1935, 1,043,167 cases of eggs, 3,589,501 pounds of poultry, and 177,062 tons of feed were handled.<sup>4</sup> Nonmerchtable eggs (eggs of good quality but with shell defects) are converted into frozen eggs, egg albumen, powdered yolks, and other processed products. A nutrition committee to test and improve feed formulas and a laboratory to test commercial feeds and ingredients are maintained.

When the association began its operations, it sold eggs only in the Seattle market through a commission agent. It soon established its own sales representatives on the Pacific Coast markets to sell its eggs directly to the retail trade. At first, eggs that were sold in the Eastern markets were handled by commission men, but after 1922 the services of the Pacific Egg Producers Cooperative, Inc., New York City, of which it is a member association, were used.

<sup>4</sup> For an interesting account of the increase in the membership, volume of business, and net worth of this eminently successful cooperative see tables on p. 11 of the June, 1936, issue of *News for Farmer Cooperatives*, Farm Credit Administration.

**Difference between Federated and Centralized Types.** In the early twenties the most important differences between these two types of organization were in purpose and scope of operation, but many of these differences are now eliminated. Inasmuch as the early plan and concept of organization have molded the two types of cooperatives, it is well to point out the differentiating features.<sup>6</sup> Some federations are models of organizational and operating efficiency while some are the exact opposite. The same is true of centralized associations.

A fundamental difference between the federated and centralized type of association is that the former starts from the bottom up, decentralizes authority to its constituent members (district exchanges and/or locals), and is democratic throughout, whereas in the latter, authority is highly centralized in a central governing board and all operations work from top down. These and other differences may be shown in the diagram on page 224, but it is to be remembered that the differences are largely a matter of degree not kind.

It should be reiterated that many of these differences are a matter of degree and not kind, that since 1925 many centralized associations have undergone considerable reorganization, that pooling areas have been adjusted to meet the needs of growers, that pooling periods have been shortened in many cases, that contracts are as flexible in the centralized as in the federated type of association, that emphasis on market control has given way to more emphasis upon marketing services, that the primary importance of a sound legalistic structure has given way to the concept of a smooth working effective marketing system that will work with and through established tradesmen in an efficient manner, that a 100 per cent grower sign up is not indispensable to success, and that the existence of some kind of organization to take the place of local associations in the federation is important to maintain membership contacts and sustain loyalty. In scope and method of operation the new centralized association of the thirties is different from the old centralized association of the twenties. In fact, it is difficult to tell whether certain

<sup>6</sup> BLACK, J. D., and H. BRUCE PRICE, in *Cooperative Central Marketing Organization*, *Minn. Agr. Exp. Sta. Bul.* 211, pp. 27-35, point out at some length the principal differences between these two types of regional marketing organizations.

Differences in	Federated	Centralized
1. Membership	Farmers in locals, locals in districts, districts in central associations	Farmers directly in central association
2. Primary objective	To lower costs of marketing and obtain best market prices through efficient marketing services and quality products	To control prices through control of major amount of market supplies (policy is changed today)
3. Methods of achieving objective	Render most efficient marketing services	Gain control of the bulk of the crop and use such control as an effective bargaining weapon
4. Authority	Rests with local associations	Rests with central headquarters
5. Voting	Farmers vote in locals, locals in district associations, districts in central associations	Farmers vote in voting districts and district delegates in the central association
6. Contractual arrangements	Contracts not considered absolutely essential. Farmers sign contracts with locals, locals with districts, districts with central. Contracts are flexible	Contracts are a vital part in scheme of organization. Only one contract is used and that from farmer member to central association. Long-term non-revocable ones were first used
7. Title to products	Farmers generally retain title. Contracts commonly used are agency contracts	Usual type of contract is the purchase and sale, vesting title of commodities in the association
8. Pooling arrangements	Most pools are local area pools ordinarily of short duration	Pooling area ordinarily co-extensive with entire membership area. Long-time seasonal pools were first considered absolutely essential, and were necessary considering the price policy that was adopted
9. Price and sales policy	Usually emphasises market service, development of markets, quality improvement, orderly flow of products into markets to obtain best possible market price. Locals often select their own markets and determine time of sale	Greater emphasis placed on monopoly control of a large portion of the crop in order to be in a position to dictate prices at which products will be sold (this policy is considerably changed today)
10. Control of volume	No set percentage of crop was deemed necessary to start operations	Usually a high percentage (75 per cent or more) of the crop had to be signed up before operations began
11. Marketing practices	Much of the grading, packing, storing is left to the locals. Supervision and advice from central association	Central association establishes grades, pack, time of sale, prices, and all marketing functions
12. Nonmember business	Many locals handle nonmember business	Since the contract is so vital a part of the association, non-member business is not handled
13. Financial form of organisation	Favors capital stock associations	Partial to nonstock membership associations
14. Ownership of facilities	Locals own local warehouses, processing plants; districts may own warehouses; central owns central office, central storage plants, central processing plants. Subsidiary corporation plants operated through central's supervision	Centralised association owns or leases all facilities in either country markets or terminal markets

commodity organizations are of the federated or centralized type if they are to be judged by the mode of conducting their business operations. In many federations the local units are manned today by personnel hired by the central exchange in order that grading, packing, and market preparation of produce may be uniform throughout all locals. Likewise, many federations strive just as hard as centralized associations to get such substantial control of the crop as to be a significant factor in the trade.

#### COMBINATION FORM OF ORGANIZATION

Not all regional associations follow the pattern of either the centralized or federated type, but a few have found it expedient to combine certain features of each type in their structural setup. Such organizations may be called combination-type regional associations. An illustration of the combination that was worked out in one organization follows. Farmers were organized into local associations for the purpose of owning and operating local assembling units. The local units were federated into a central sales organization and had signed a contract with it. To this extent the association was of the federated type. A second contract was signed by each farmer-member directly with the over-head central organization. The central association placed its own grader in each local unit receiving plant and completely controlled the grading, packing, shipping to market, market selection, and time of sale, thus removing nearly all authority respecting the marketing of the commodity from the local units. This procedure would indicate practices characteristic of centralized associations.

#### SALES AGENCIES

Another type of regional cooperative organization is the terminal sales agency. It differs from a regular marketing association in that it conducts essentially a commission business, selling whatever livestock or produce is consigned to it. (In this sense it is a marketing association, but one performing a limited number of services in only few markets. It does not store, brand, advertise, or perform marketing services offered by such marketing companies as the American Cranberry Exchange.) The consignors may be local associations or individual farmers that

ship their livestock or produce to the terminal markets to be sold for whatever the market price may be. The cooperative livestock commission firms, the cooperative fruit and vegetable commission houses, and the cooperative firms that sell eggs and poultry, butter, grain, and cotton on a commission basis are the kinds of companies that are classed as terminal sales agencies. About 50 of these central market sales agencies are in operation. These agencies generally receive shipments from members or nonmembers residing in country markets, sell the consignment to the best advantage as soon after arrival as possible, and remit to the shipper the gross proceeds less the customary commission and other market charges. At the end of the year any excess of commission receipts over expenses is returned as a patronage refund to the member shippers.

The sales agencies may be set up as federated associations or as centralized associations although the former are by far the usual type. In the case of cooperative livestock commission companies, the most important of the sales agencies, farmers are members of local livestock shipping associations which in turn have membership through the purchase of stock in the terminal selling agencies. In some agencies individual farmers who may have full carloads or truckloads of stock may also obtain membership on an equitable basis with local livestock shipping or trucking associations. No contracts are used between the sales agency and the local shippers, although it is not uncommon to find a local association using contracts with its members. Each local association is an autonomous unit and may or may not consign livestock to the sales agency. Although a sales agency may be a federated type in structural organization, it differs from the ordinary marketing association in that a limited number of services are performed in the market place. In the terminal grain markets, the early sales agencies handled grain on a consignment basis only and sold it for country elevators at regular commissions. During the past 5 years, however, these terminal sales agencies have bought and sold increasingly larger amounts of grain and handled proportionately smaller amounts on a commission basis. They have thus assumed other than the usual functions of a sales agency.

The Central Cooperative Association at South St. Paul, Minn., illustrates a sales agency in the terminal livestock markets. This

cooperative commission firm started operations in 1921. Previous to commencing a commission business at South St. Paul, livestock shipping associations shipping to this market organized in 1918 a federation, the Northwestern Cooperative Livestock Shippers Association, which for several years dealt with general problems confronting country shippers, such as transportation rates, claims, terminal market charges, terminal services, and legislation affecting the interest of the livestock shippers. The commission firm was incorporated as a capital stock company, \$25 shares of common stock being sold to livestock shipping associations, and \$1 shares of preferred stock to individual producers who shipped directly. Each association holding one or more shares of common stock has one vote and each individual producer holding preferred stock has one twenty-fifth of a vote. Between 500 and 600 shipping and trucking associations holding common stock and nearly 11,000 individual carlot shippers holding preferred stock constituted the membership in 1935. Like other federated associations, this sales agency is primarily built upon local associations and obtains the bulk of its business from them. According to its own statement it proposes (1) to establish better service at the terminal market, (2) to reduce marketing costs, (3) to create wider outlets for livestock arriving at the market, (4) to eliminate as far as possible the speculation on livestock at the terminal market, (5) to bring about an orderly system of livestock marketing throughout the country and by accomplishing these purposes to make livestock production more profitable.

This association operates on commissions which are approximately 15 to 20 per cent below regular rates (on other markets, cooperative firms usually charge rates that private firms charge) and at the end of the year refunds net earnings to the members on a patronage basis. Besides selling livestock for its members or nonmembers, it also purchases stockers and feeders for its patrons through a special department. No contracts are signed by the central association and its members. Through its fieldmen and its house organ, the *Cooperative Shipper*, it keeps in contact with its members and carries on its educational activities.

Since the sales agencies are limited very largely to the performance of a commission business, selling whatever livestock or produce anyone wishes to send to them at any time, it is apparent



that the effect of such agencies upon production practices, upon the general market price, and upon developing and expanding new markets is more restrictive than that of a marketing association which establishes grades and brands, advertises, stores, and follows a program of orderly market distribution. Sales agencies do not advertise the products which they handle in order to increase their sales outlets as regular marketing associations do, but they do advertise the commission services which they render in order to attract more business. It is one thing to advertise Eatmor cranberries, Diamond walnuts, Sealdsweet grapefruit, Sun-maid raisins, Pep eggs, and Land O'Lakes butter, but quite another to advertise the services of the Pacific States Livestock Marketing Association, the National Fruit and Vegetable Exchange, Inc., or the Northwestern Turkey Growers Association. Although sales agencies have quite generally accomplished considerable in the field of their limited operations, it is doubtful that they have made as important inroads in the marketing channel as have the federated or centralized commodity marketing associations.

#### COLLECTIVE BARGAINING ASSOCIATIONS

According to the outline on page 212 collective bargaining associations are the second type of association listed under the classification "Nature of Operations." They are contrasted with marketing associations and sales agencies which already have been described. A collective bargaining association is either a local or regional association that negotiates with private market operators over the price, terms of sale, and other business arrangements involved in selling the products of its members. In the strictly bargaining association, members' products are not handled by the cooperative but deliveries are made directly to private buyers. The association acts as a sales agent or broker in bringing buyer and seller together. The dealer either pays the full price to the farmers directly for the product less such deductions as are taken out by the association, or remits to the association which, after making its deduction, pays each farmer. In many ways this type of cooperative association resembles a labor union, the former negotiating with the buyer over the price and terms of sale of the farmers' products, the latter doing the same for the labor of a workman. This type of association is a response

to a particular situation in which marketing facilities and business methods are already carried on successfully by private agents but in which the individual producer has little bargaining power over the price of his product. It has likewise found favor among the producers who deliver their products directly to processors.

Most common use of the collective bargaining association is made by fluid milk producers around city markets. The greater share of fluid milk is sold by farmers on the basis of bargained prices between associations and milk dealers. Most of these milk bargaining associations were organized after 1914 although some date as far back as 1883. In the purely bargaining association, the producers sign contracts with the association in which they agree to market all of their milk to buyers and dealers designated by the association at prices agreed upon between the association and the dealers. Officials of the cooperative meet monthly with distributors and bargain for prices, base and surplus considerations, and other matters arising between dealers and producers. A price schedule involving the prices of "basic" and "surplus" milk is agreed upon. The bargaining association does not physically handle the members' products, but in addition to negotiating a price, it may hire testers to check weights and butterfat tests, and to inspect farms so as to advise members in producing high quality milk. The association may also act as arbiter between individual members and dealers in the settlement of differences, may make adjustments if errors in payments, weights, and tests occur, and may provide considerable marketing and production information for its members. Thus, the Sanitary Milk Producers, a collective bargaining association of milk producers around St. Louis, Mo., organized in 1929 for the following purposes: (1) "standardization and improvement of milk and dairy products; (2) collective bargaining in selling; (3) control of surplus and supplying milk as the market demands; (4) checking weights and tests; (5) watching credit ratings of buyers; (6) issuing truthful market information; (7) advertising milk and dairy products to broaden the outlet."<sup>6</sup>

During the past 10 years there has been a pronounced tendency for many milk bargaining associations to take over many of the regular marketing functions and to own and operate their own

<sup>6</sup> Reported in *Illinois Agricultural Association Record*, April, 1929, p. 1.

facilities. Some take title to the milk of their members, own and operate processing plants where surplus milk is converted into manufactured products, and sell to regular milk dealers such amounts as are required for fluid-milk use. The history of the Dairymen's League Cooperative Association of New York illustrates such change. Starting out as a bargaining association in 1907, it reorganized in 1921 and became the largest milk marketing association operating in the country. Confronted with large surpluses of milk at the close of the World War, the League decided to begin operating country plants in April, 1920. By 1929 it was operating 238 plants, some being owned, others leased, and was serving 37,000 members. In 1934 it was running 119 country receiving plants, had 40,000 members residing in five states and distributed directly to consumers a portion of the \$40,000,000 worth of milk that it handled, the rest being either sold to private dealers or processed into manufactured products in its own plants. The Twin City Milk Producers Association of St. Paul, Minn., is a collective bargaining association which also owns facilities to convert surplus milk into processed products. Other bargaining associations that handle only "surplus" milk as a supplement to their regular bargaining functions could be named.

The bargaining type of association is not restricted to fluid milk producers only. Patrons of condenseries, sugar-beet growers, and peach, pear, and cherry growers have sold their products through bargaining associations to processing plants. It is estimated that there are more than one hundred active bargaining associations at the present time. In the fluid milk markets the influence of bargaining associations has been checked somewhat since marketing agreements under the Agricultural Adjustment Act have been in effect and since in some states the department of agriculture and markets fixes the retail and farm price of milk. To cite only two of the many states that have fixed milk prices since 1930—in 1936 the price of milk to producers was set in Pennsylvania by the Pennsylvania Milk Control Board, and in Connecticut by the Connecticut Board of Milk Control. In the hearings at which milk prices are determined by dealers, government agents, and producers the collective bargaining associations as the representative of a large number of producers have an important voice in price determination.

From the standpoint of its structural organization, the bargaining association is either a local association or a regional centralized association. Farmers hold membership directly in the bargaining association, sign contracts with it, agree to accept the prices arrived at by the association and the dealers, and become patrons of local receiving plants that the central association may own or lease. The Sanitary Milk Producers of St. Louis is a regional association of about 10,000 members (1934) who are organized into 112 local units and who reside in about 40 counties in the two states of Missouri and Illinois. In contrast to this large-scale association, a local association, whose members live in one or a few counties about a small city market, may be pointed out to show the variations in size which the bargaining associations may assume.

#### NATIONAL MARKETING ASSOCIATIONS AND SERVICE AGENCIES

In 1929 and 1930 the Federal Farm Board set up six national commodity *marketing* associations and one *service* agency for the purpose of coordinating the sales activities of competing cooperatives, of preventing duplications, and of concentrating sufficient volume under one management so as to be an important factor in the market. Members of these national associations are local associations, centralized associations, regional sales agencies that have as members local associations and carlot shippers, and federations of local associations. Of the seven that were created those for the marketing of grain, livestock, fruits and vegetables, pecans, cotton, and wool are still functioning. In all but one (livestock) of these the nationals actually sell the products of their member associations. The functions of the six active nationals vary considerably from being national clearinghouses of information for their members to exceedingly large marketing companies. Such services as relate to sales policies, price policies, membership relations, financing, trade relationships, research, publicity, and legislation are performed for the member associations.<sup>7</sup>

<sup>7</sup> For a pro-and-con discussion of these national associations see "American Cooperation 1932," pp. 77-143, The American Institute of Cooperation, Washington, D. C.

As an illustration of a national *marketing* association the organization of the National Wool Marketing Corporation, Boston, may be described. This National was organized as a capital stock (\$1,000,000) company in 1929 under the laws of Delaware. Stock was originally sold only to district or state wool marketing associations that handled at least 500,000 pounds of wool or mohair. In order to give associations that were too small to qualify as stockholders in the National an opportunity to have a voice in its affairs, a Central Wool Marketing Corporation, Boston, was organized to handle wool for such small associations. Farmers sign contracts with their respective state or regional wool pools, and the latter in turn sign contracts with the National Corporation making it the exclusive sales agent for the member associations. Twenty-six wool and mohair marketing associations representing between 30,000 and 40,000 farmers located from Texas and California to New Hampshire are active members of the National—sixteen are located in the range states handling "territory" wool and ten in the midwest and eastern states marketing "fleece wool."

The state wool pools chiefly assemble wool for shipment and render a field service to the members, while the National attends to the selling. Preshearing advances (chiefly in the range states), as well as advance payments made to growers by the state associations at the time wool is received, are made possible through financing arrangements with the National Wool Credit Corporation, a subsidiary of the National Wool Marketing Corporation. Assisted by graders of the National, the fleece-wool associations grade their members' wool in warehouses owned or leased by them. The wool is sold for the member associations according to their choice of several methods; namely, (1) the so-called "unit marketing plan," chiefly for territory wools; (2) growers' original-bag lots for large individual range producers; and (3) separate state pools, chiefly for the fleece-wool associations. Between 200 and 300 mills and manufacturers buy from the National.

The National Livestock Marketing Association (Chicago) is also a national association, but, unlike the National Wool Marketing Corporation and the other nationals, it does not act as selling agent for its members. Instead it is a *service* agency to "develop unified cooperative control in selling meat-producing animals." Organized in 1930 through the efforts of the Federal

Farm Board, the association has today 22 cooperative commission firms and regional livestock marketing agencies as its members. These member associations signed contracts with the National and own stock in proportion to their volume of business. Several subsidiary corporations to finance the purchase of feeder stock and to publish a livestock marketing journal have been created. Economic research in livestock marketing, representation before legislative bodies on behalf of livestock producers, and coopera-

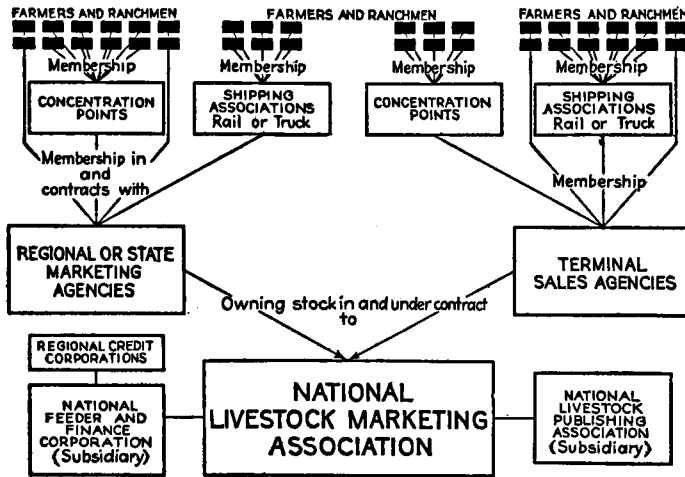


FIG. 6.—National Livestock Marketing Plan. Farmers and ranchmen have several ways of marketing their livestock cooperatively through the various agencies affiliated with the National Livestock Marketing Association, as indicated on the above chart. They may market through local, county, state, regional, or terminal cooperative associations. Terminal, regional, and state marketing agencies own stock in and are under contract to the National Livestock Marketing Association. (*Cooperative Marketing Makes Steady Growth, Federal Farm Board Bul. 8, p. 32, Washington, D.C.*)

tion with other agencies in creating a wider market for meats are some of the other functions of the National. The actual selling of livestock, and purchase of feeder lambs, hogs, and cattle are carried on by the separate member agencies of the National. The above figure indicates the plan of organization from the livestock producer to the national organization—a plan that brings together in one organization the Texas cattlemen, Iowa hog producers, Montana sheepmen, and Minnesota veal-calf producers.

The structural organization of the national associations discussed above should not be confused with large-scale regional associations that enjoy a national distribution of their products. Although the California Walnut Growers' Association of Los Angeles distributes its Diamond walnuts throughout the nation, it is a regional federated association confined to walnut growers on the Pacific Coast. It should also be mentioned that attempts to organize associations on a national basis antedated the Federal Farm Board's activities. The National Wool Growers Association organized a storage and warehousing company in 1909 which stored and sold wool for regional associations of numerous states. In 1923 the Federated Fruit and Vegetable Growers, Inc., began selling produce for individual growers, local associations, and federations of local associations located in more than fifteen different states.

#### SINGLE COMMODITY AND MULTIPLE COMMODITY ASSOCIATIONS

From the standpoint of number of commodities marketed, most of the successful cooperatives in this country handle only one or a few closely related commodities. The large-scale regional associations of both the federated and centralized types were organized in most cases on the *commodity* basis rather than on a *geographical* basis.<sup>8</sup> The advantages of organizing on the single commodity basis are:

1. Common interests of the membership are recognized. Problems of production, marketing, legislation, pricing, and other economic considerations differ for producers of unrelated products. Hence, it is more difficult to obtain a unity of interest if heterogeneous products are handled. G. Harold Powell wrote in 1913, "The members must be well acquainted with each other, their aims must be similar, and they must grow products of similar quality and character if they are to succeed when asso-

<sup>8</sup> By the commodity is meant the article *sold* by the association. In most cases the product delivered by the farmer is the same as that sold by the cooperative. But in the case of a raw material, such as milk, the commodity that is processed from it, namely, butter, cheese, canned milk, is considered as the basis of organization. If milk is sold as fluid milk, then this product is thought of as the basis of organization.

ciated with one another.”<sup>9</sup> Even though producers of unlike commodities live in the same community and have certain problems in common, they may not be the best cooperators in a marketing association if there is a great variance in the technique of handling, in costs, in market outlets, in sales promotion policies, and in numerous other matters relating to the different commodities. Divergence of interest in the marketing of the separate commodities tends to split the membership into factions. “A house divided against itself cannot stand.”

2. Handling unrelated commodities requires additional facilities, additional specialized labor, and greater capital investments than does the marketing of commodities using the same equipment and kind of labor. Whether or not an additional commodity shall be handled depends upon the extent to which the labor, capital, land, and management of one article may be used to economical advantage by the other. If the fullest use of these factors of production can be made by handling several commodities, then the unit cost of operation for each is lowered. If they do not supplement each other, then from the standpoint of internal operations of the company it would be unwise to combine them under one association.

3. There are limits to the capacity and efficiency of the management. The intricate marketing problems that arise for each commodity in a large-scale association require well-trained specialists. However, if the marketing operations and problems are not greatly dissimilar for a variety of products, then handling several commodities may enable a manager and his department heads to utilize their abilities to a fuller capacity and efficiency than if only one commodity were marketed. The issue centers about the economics of specialization and diversification.

4. The problem of equitably allocating the cost of handling several dissimilar commodities is not encountered in the single commodity association. If, for example, honey and apples were marketed by one association, the sheer difficulty of apportioning the costs of operations between the two commodities would be sufficient, no doubt, to create dissension between the members marketing the different products. The fact that a number of multiple commodity associations handling dissimilar commodities

<sup>9</sup> POWELL, G. HAROLD, “Cooperation in Agriculture,” pp. 19-20, The Macmillan Company, New York, 1913.



had to be re-organized on a single commodity basis due to internal dissensions indicates the seriousness of the complications when they do arise.

Therefore, whether it is unwise to organize on a geographical basis depends a great deal upon the kinds of commodities produced in a given area. If country operators and wholesale market dealers individually have successfully handled a variety of products and if the farmers produce on their respective farms some or all of the kinds of products of the territory, then a cooperative may find little trouble in uniting and harmonizing the interests of its producers as well as keeping its costs of operation at a minimum. The Eastern Shore of Virginia Produce Exchange, Onley, Va., has been in operation since 1900 and has successfully marketed a variety of commodities—white potatoes, sweet potatoes, strawberries, onions, cabbage, beans—for 5,000 to 6,000 growers living on the peninsula between the Atlantic Ocean and Chesapeake Bay. Another multiple commodity marketing association is the Yakima Fruit Growers' Association which handles apples, pears, peaches, plums, cherries, and asparagus. It will be observed that the products handled by these companies fall into the general category of "fruits and vegetables" and constitute the "line" handled in many instances by regular market operators.

There are many cooperative sales associations that commence operations as a single commodity association but gradually expand to include a variety of products. Thus, the Land O'Lakes Creameries, Inc., began as a butter marketing company but has extended its operations to include a "full line" of dairy products such as cheese, cream, powdered skim milk, and buttermilk, and casein, as well as eggs and poultry (including turkeys). In Denmark where the single commodity basis of organization has been adhered to very closely, the principle is being modified by cooperative packing plants which today handle a sizable volume of eggs for their members. The advantages of handling a variety of commodities in one organization are: (1) it obviates the necessity, expense, and effort of setting up several marketing associations; (2) it increases the volume of business of the cooperative without necessarily increasing its overhead costs; (3) it facilitates continuous operations if the marketing seasons of the respective crops are consecutive—the reverse would be true, however, if

the peak delivery period for the several commodities should come at the same time; (4) it enables the cooperative to deal in a "full line" and thus attract certain types of buyers. These advantages depend upon how well the products supplement each other in the full use of the land, labor, capital, and management of the concern.

Other types of associations listed under the classifications on page 212 are discussed in the chapters on financing, pooling, and legal background of cooperatives. In this country all cooperative associations are *voluntary* organizations. No one is forced to join an association. In some countries, Australia for instance, farmers are compelled to market certain products through a cooperative company if a vote of all producers is predominantly in its favor. Compulsion is the antithesis of cooperation.

#### FACTORS AFFECTING CHOICE OF FORMS

There is no rule-of-thumb method of determining which structural form of organization is to be used. A number of factors must be considered:

1. The task to be performed. If the association is designed to improve certain marketing operations at a given country point, *e.g.*, by establishing a better local egg market, a local association will suffice. If, however, the object is to revamp the entire system of selling eggs in both country and wholesale markets, then a centralized, federated, combination, or national association is needed. If the existing agencies are well managed and operating concerns, so that a cooperative would have little opportunity to effect greater economies or better sales, then instead of establishing a rival, duplicating marketing association the greatest good may be achieved from organizing a local *bargaining* association.

2. The stage of development of an operating cooperative. Many milk producers' associations have started as bargaining associations but have become operating-marketing associations as well in order to strengthen their bargaining position. Their experience in the market, increased membership, greater financial resources, larger volume of milk, greater surplus, and expanded opportunity of usefulness for the membership have made it expedient for the erstwhile bargaining associations to revamp

their structural organizations from local to regional associations and from price bargaining units to operating-marketing ones. In somewhat similar fashion single commodity associations have been transformed into multiple commodity organizations as sales experience and market outlets have increased.

3. The nature of the market for the commodities handled and the characteristics of the commodities themselves. Many commodities require grading, packing, and storage in order that a successful selling program may be carried on for them. Hence it is not uncommon for associations to acquire title to such goods. Other commodities cannot be stored but must be processed by firms with large amounts of capital. Thus, livestock is handled successfully by cooperative sales agencies which do not take title to the livestock, but tobacco and cotton are marketed by associations that usually have title to the products. The market for most tobacco is also limited to a handful of large tobacco manufacturers whereas the distributors of fruits and vegetables, nuts, dairy products, and grain are legionary. Consequently, a high degree of centralized control is often considered more advantageous for products having relatively few outlets than for products having very many market outlets. To the extent that this is the case in any association, a preference for the centralized association will be exhibited.

4. The speed with which a cooperative is to be organized. Organizers of regional associations have found that it usually takes less time to organize a centralized association than a federated one. With a preconceived plan of organization and with a rousing membership campaign put on by high pressure propagandists, it has been possible to put thousands of producers under marketing contracts within a few months. Most federated organizations are not established that quickly. Therefore, if *time* is the factor of greatest importance a centralized association will be selected ordinarily in preference to a federated one. Likewise, if a preference for the features of either the federated or the centralized association shown on page 224 exist, selection will be influenced accordingly.

5. The preference of leaders for particular types. The dominant leaders of cooperatives during 1920-1923 preferred the centralized to the federated type and as a result centralized associations were organized in many places. Some of the general

farm organizations, as well as the Federal Farm Board, sponsored national associations.

6. The financial requirements. Whether or not large capital requirements are necessary is an important factor in determining organization on a capital stock or on a membership basis. Even in this case certain leaders of cooperatives prefer organization under all circumstances on a noncapital stock membership basis. At times re-organization from a membership to a capital stock basis has been urged by credit institutions.

There are successful federated associations which, no doubt, would be equally successful if organized on a centralized basis. The reverse is also true. This merely suggests that the structural form of organization, which is largely a matter of organizing the membership, keeping membership relations at a high pitch of loyalty, and of cementing the relationship between an association and owner-patrons, is not the most important factor bearing upon the successful conduct of the business operations of a cooperative. The purpose of the association and the singleness of interest of the membership must be kept in mind in selecting a particular type of association.

#### AGRICULTURAL PURCHASING ASSOCIATIONS

The structural organization of farmers' cooperative purchasing associations does not differ materially from the marketing associations. The classifications on page 212 are applicable except those numbered, 3, 7, and 8. On the basis of territory served there are *local* and *regional* associations. The local association may be an informal buying club comparable to an urban consumers' buying club, or it may be a regularly organized local association having a place of business where it sells daily to its members. The informal buying club does not have a place of business—a purchasing committee pools the members' orders, places the order with some wholesale dealer, collects the money from the buyers, and has each buyer call for his goods at the car door when the car arrives. Usually such informal buying is among members belonging to local chapters or societies of the general farm organizations. The regularly organized local purchasing association, such as a farmer supply company, a feed store or an oil station sells shares of stock to its members, is

incorporated, provides facilities, and hires a manager and assistants, if necessary, to conduct a rural business catering to the needs of the farmers it serves. The members elect a board of directors who engage the manager of the company. Besides this local warehouse type of association, there is also the bargaining type. The latter is incorporated but operates much like the informal buying club mentioned above.

The regional purchasing associations may be of the *federated*, *centralized*, or *combination* type. Under the first, farmers are members of local associations which in turn have membership in a central purchasing association. Under the second, farmers are members of the central association which owns or leases and operates country warehouses or stores. Under the third, features of the first two are combined. The voting control in the central association of the federated type rests with the local associations, in the centralized type with the farmers organized into voting districts. The Indiana Farm Bureau Cooperative Association, Inc., is a federated type of organization, the Eastern States Farmers Exchange, Springfield, Mass., a centralized. The latter organization has thirteen regional service warehouses and approximately 600 local representatives who assemble orders and attend to the business details of distributing supplies to more than 50,000 farmer members of the Exchange. Only a small number of the local representatives have complete storage facilities since practically all feed and other supplies are trucked directly from the car to the farms on orders previously obtained. The combination type of association is illustrated by the Cooperative Grange League Federation Exchange, Inc. Autonomous local associations, G.L.F. local agents, and retail supply stores owned or leased and operated by the G.L.F. constitute three important outlets for products distributed to more than 100,000 patrons of the Exchange. The regional purchasing associations serve the same purpose for the local associations that a wholesale grocery company does for retail grocery stores.

The activities of these central buying associations are not restricted to buying for local associations—their operations include manufacturing as well. Large mills in which feed is ground and mixed, seed is cleaned, and grain is elevated and stored are maintained by several of the companies. Other

services including laboratory testing of seeds, feeds, fertilizers, and other farm supplies and accounting are provided.

Questions

1. What four main classes of cooperative associations are listed? Why not group all cooperatives into only two classes, namely, consumers' and producers' associations?
2. What are "service" cooperatives? With what types of cooperatives are they to be contrasted?
3. In what respects does a centralized cooperative differ from a federated?
4. How do marketing, collective bargaining, and sales agencies differ from one another? Give illustrations of each kind.
5. Show by illustration the plan of organization of the National Livestock Marketing Association.
6. What is meant by a "commodity basis" of organization? A "geographical basis"?
7. If the tobacco growers of Kentucky or the cotton farmers in Georgia were to organize new tobacco or cotton marketing associations what arguments would you advance for a centralized association? a federated association?
8. What types of farm supply purchasing associations are there?
9. It is held that "we are consumers by nature and producers by necessity." If this were granted, is it an indication that all cooperative associations—production and distribution societies—should be organized from the standpoint of consumers' interests?
10. What does J. P. Warbasse mean by a "Cooperative Democracy" as a system of organization of economic society?

## X

### *Membership Relations*

*He who possesses the charmed key to those inner recesses of the human mind has access to an inexhaustible source of wealth. An understanding and an appreciation of the latent forces, which impel individuals to action and to effectively combine and coordinate their creative powers with those of other men, permit the use of these energies for the greatest social good. Man alone can create values. His mastery over material things in recent times has done much to release him from mean tasks and the drudgery of common labor. Even now he is not far removed from barbarism in his relations with other human beings. If his relationships can be so ordered that he can harmoniously work with and not against his fellowmen, his second triumph will be the attainment of peace, happiness, and finer cultural values. Proper membership relations in cooperative enterprises may be the socializing influences that will avert disasters and chaos that always appear in the wake of a conflict that results from competition and internal strife.*



## CHAPTER X

### MEMBERSHIP RELATIONS

The influx of members into a newly organized cooperative venture is in many respects analogous to the settlement of pioneers on the frontier. The successive migratory waves of humanity originating in different countries and merging in a common region present many problems of adjustment caused by widely divergent cultural backgrounds. Fusion of the different customs, ideals, and standards brought to the new environment may result in the formation of a new society wholly different from any of the contributing cultures. Likewise, the bringing together of many people from different regions, districts, and communities into one business enterprise, such as a cooperative venture, calls for innumerable adjustments in the opinions and actions of those comprising the new organization. They must reconcile themselves to the fact that they will have to conform with the standards of the newly founded business society just as realistically as if they were members of a frontier civilization.

When cooperative organizations are hastily and imperfectly formed, as many of them are, the persons who become members cannot be expected to fully appreciate the underlying economic implications. Many of them will be slow to grasp the significance of the principles involved. They do not perceive the necessary adjustments in personal conduct that are required, or understand even the simplest routine tasks that are sometimes put into effect to improve physical operating conditions. If no provision is made to help those who want to understand and to be understood, the greatest possibilities of coordination will not be realized. The success of any business venture, if the common fundamentals of business organization are observed, rests with the persons who are identified with it. It is the common fault of many established associations to be so deeply absorbed in the problems of assembling and handling the physical commodities that they overlook the far more vital function of the association—the question of developing human relationships. This limitation



in management may be attributed in part to the failure of directorates to recognize the importance of developing favorable membership relations; in consequence thereof they provide no funds for administration, nor do they make policies relating to the cultural advancement of association. No definite pecuniary measure can be attached to the intangible "gospel of good will," and dividends on the investment of time and expense may be slow in materializing. The chief reason for inattention to membership relations, however, is easily surmised—they are abstract and abstruse.

Those who prize association as a means of production and distribution are greatly concerned with understanding and acquiring a philosophy relating to the forces which govern men's actions. Economists have rarely ventured over into the field of psychology to observe some of the forces of life that vitally affect economic activities.

#### MOTIVES FOR ECONOMIC ACTION

Adolf Wagner, a German economist, listed five leading motives which influence man's economic actions. These are positive and negative in nature. They are:

- I. The striving for personal economic advantage and the fear of want.
- II. The hope of recognition and the fear of punishment.
- III. The sense of honor and the fear of ignominy and disdain.
- IV. The urge to action and the joy in being active. Also, work for work's sake and for the sake of its results, as well as fear of the consequences of inactivity.
- V. The impulse for ethical action and the fear of self-reproach (conscience).<sup>1</sup>

NOTE: The authors have inverted the order within the motive under II from Wagner's version, "the fear of punishment and the hope of recognition," because they believe the hope for recognition is more dominant as a force for good than the fear of punishment. Wagner labels the first four motives as egoistic and the fifth as nonegoistic.

A thorough appreciation of the powerful incentives which flow out of the motives enumerated by Wagner may form the

<sup>1</sup> WAGNER, ADOLF, "Die Wirtschaftliche Natur des Menschen Grundlegung," 3d ed., Book I, part 1, p. 87, 1882. Also see pp. 83-121.

basis for scientific approach to shaping and directing membership policies. His theory is that man ascends from the first or baser motive toward the last and noblest aspiration, the moral command, or impulse for ethical action.

#### I. STRIVING FOR PERSONAL ECONOMIC ADVANTAGE

This motive is universally common to all men. It is based on a natural law which requires that our elemental hungers must be satisfied. The instincts of acquisition, sex, migration, and appropriation manifest themselves most frequently under this motive.<sup>2</sup> It varies in intensity as the individual senses his needs. This motive is not strictly confined to the selfishness of the individual, for he may broaden it to include those near and dear to him whom he considers dependent upon him.

When men become members of a cooperative association, they take a long transitional step from an organized capitalistic state in which economic activity is characterized by free competition, private property, and the profit system. The individual participants in this state develop habits of thought and modes of action that are often incompatible with the methods and objectives of cooperation. The task of directing the activities of men "en masse" is doubly difficult when reform is prerequisite to a system of effective coordination. The obstacles to harmonious collective effort are many, and a few of them are especially pertinent to the functions of marketing.

What are the modes of appropriation and exploitation? Under the capitalistic regime, the individual is compelled to adopt the principle of self-interest solely as a means of defense in the absence of any other motives. He uses his powers of persuasion and coercion to drive hard bargains in all except those fields of endeavor specifically shielded by the protecting hand of the government. The strong exploit the weak. The aggressive appropriate the unclaimed fruits of nature and the windfalls of society. No fine distinction is drawn between acquisitions from legitimate services rendered and incomes from

<sup>2</sup>The terms "instincts" and "innate qualities" are merely used to designate certain human characteristics in a language most commonly understood by the layman. The authors recognize that this terminology is regarded by some psychologists as obsolete and inadequate because the terms simply name and do not explain the actions of men.

conjunctural gains. In the cooperative association, incomes from personal services, interest upon a limited amount of capital, incomes from personal and certain classes of real property, members' ownership in tools and machines, copyrights, and patent rights, are recognized and approved. In contrast, however, the returns resulting from vested interests arising from monopoly profits, land rents, royalties, and conjunctural gains, may be considered in some instances inconsistent with the best interests of society. The main emphasis in a cooperative society is given to those earnings which result from some form of personal services. Under capitalism one may gain prestige if he is able to acquire wealth irrespective of how it is gained as long as it is within the law. Some writers on the subject of membership relations have lamented the fact that such personal traits as avarice, selfishness, greed, and general low standards of ethics should be manifested in the price bargain, especially by members who have been tempered long and severely in the individualistic discipline.

**The Demand for Cash.** A corollary to the problem treating of the legitimate sources of income and the correct use of property is the problem of determining the method and time of making payments. In one study of four cotton and tobacco associations 33 per cent of the members claimed that they were handicapped by the cooperatives' methods of making settlements for produce delivered to the associations.<sup>3</sup> Some of the reasons for dissatisfaction with the method of payment indicate that an appreciable number of farmers need immediate cash settlements in order to carry on farm operations. They do not have adequate reserves to participate in a program of spreading the risks of marketing by pooling their products and projecting the time of final settlement. Some members have financial obligations that must be met on due dates. Others object to the payment of interest on loans even though the increased returns from pooling may far exceed the amounts paid in interest during the waiting period. In all probability there are others who may offset losses from sales by gains through advantageous purchases in making cash payments at the time goods are delivered.

<sup>3</sup> JONES, J. W., and O. B. JESNESS, *Membership Relations of Cooperative Associations*, U. S. Dept. Agr. Circ. 407, p. 15, 1927.

Cooperative managers have been harassed by the complaints of members because settlements are delayed. They are often confronted with the dilemma of complying with the demands of the members as to payments and at the same time of excelling other sales agencies in the returns made for the products delivered to the association. To avoid gluts and demoralized markets, they induce the directorate to gamble on the trend in prices and assume unusual risks in withholding products. Simultaneously, they may yield to the pressure from members for liberal cash advances thereby endangering the reserves of the association. During the depression (1930-1934), many associations experienced financial difficulties because of a policy in making liberal advance payments. Often the declines in market prices were so abrupt that the association received less for the product than had been advanced to the producers. Although members may have no legal right to withhold funds rightfully belonging to the association which has made advances prior to the final settlement, it is an insurmountable task to collect overpayments from members. Any reasonable claims which the association may have are beset with legal complications, and any strife between an association and its members is liable to have serious repercussions on the social and economic relationships of the community. In the case of *Neith Cooperative Dairy Products Association v. the National Cheese Producers' Federation*, the court inquired into the customary procedure in making payments for cheese, and the language of the contract relating to the method of settling its monthly pools. On the basis of the court's findings, it was decided that the association had no recourse against its members because the settlement was construed to be a final payment.<sup>4</sup> This decision was disastrous for the prestige and financial status of the federation. Many unreasonable demands which members make for prompt settlements have originated from the habit of completing transactions on definite terms as they are ordinarily consummated in the private marketing system. Cooperative leaders should profit by exploring the possibilities of more adequately meeting the elemental needs that provide for the basic creature wants of their members. The solution of the problem is more likely to

<sup>4</sup> Supreme Court of Wisconsin (1935) 217 Wis. 202, 257 N.W. 624.

be found if the investigator is sensitive to the ordinary needs of men and is sympathetic in his business relations with them.

**The Effect of Indirect Benefits.** Cooperation is a means for eliminating harmful forms of competition within its sphere of business activity, but, unfortunately, it arouses external competitive forces and lashes them into violent activity against itself, producing effects which may completely obliterate any evidence of cooperative superiority over rival systems of economy. The full significance of this fact is not always apprehended by the lay cooperator, and thus it becomes one of the most common sources of unrest and discontent among members.

They fail to understand that competitive organizations must compare favorably with the cooperative association in business results to prevent a mass movement away from their enterprises. Reserves are thrown into the price bargain to impress cooperators and noncooperators of the efficacy of private enterprise. Favors are granted, additional services are given, and any reasonable concession is made to hold regular patrons and win new customers.

About 50 per cent of the members of the cotton and tobacco cooperatives interviewed by Jones and Jesness admitted that their main reason for joining the association was to get better prices, and another 37 per cent believed they could improve their status by cooperative organization. After obtaining experience with their association, however, 40 per cent claimed that they had been disillusioned in that they achieved no advantage over nonmembers by selling their crops collectively. Less than 9 per cent asserted that they had gotten better returns than nonmembers. One possible way of demonstrating the financial benefits of cooperation is to make a careful statistical survey of market prices measured against some accepted standard which prevailed before and after organization, other things remaining equal. This device, however, will not convince all members, for some will be piqued at their neighbors because they receive favorable prices from private marketing agencies. Price comparisons have their greatest value when they are based on a large number of transactions for like commodities of similar qualities at particular periods of time. Members are prone to focus price comparisons upon too few transactions and, from simple analogy, reason that all prices paid bear the same relation-

ship. Two general observations which characterize the farmers' mode of thought have been drawn from the experiences of making price comparisons. They take success for granted without offering a few kind words of encouragement to those who have probably sacrificed much to make success possible. They are easily displeased, however, if the trend of events is unfavorable.

There is a peculiar quirk in human nature, not alone common to the agrarian class, which tends to retard progress. Man would rather continue living in mediocrity than to permit his fellow worker and neighbor to rise above his own level. For this reason it is difficult to keep an organization intact if those on the outside enjoy the same economic advantages as those on the inside. It may be freely conceded that the status of everyone in the community has been improved, but to those who have assumed the responsibilities of creating and projecting changes this is only a hollow victory unless they belong to that rare group of socially minded individuals.

Personnel in charge of membership relations have too often stopped short in their analysis of the limitations of human nature. They have simply classified particularly troublesome members as possessing more than the usual portion of malicious qualities such as pride, jealousy, egoism, fear, suspicion, and irascibility. The remedy commonly prescribed for counteracting such limitations in individuals is more education to enlighten the ignorant and the indifferent.

## II. THE HOPE OF RECOGNITION

Since man has always feared punishment, Wagner emphasizes the negative side of this motive. The use of membership agreements by cooperative organizations to enforce loyalty may be said to be based on the negative side of this motive, in that various devices at law are provided to give the group recourse against the delinquent party to the agreement. Such devices are: the injunction, the right to collect liquidated damages, and the decree of specific performance.

Students of the cooperative movement, however, are inclined to deprecate the fear motive because it implies compulsion and an encroachment upon personal freedom. A much more effective force is found in praise and approval. Man strives for recognition. This trait is so prominent in the child that in the

presence of his superiors he will act in the most unusual manner to attract their attention. Industrial organizations, fraternities, honorary societies, universities, and innumerable other organizations and institutions create standards which must be attained by the individual in order to receive recognition. The attainment of these standards gives man a self-respect which satiates the desires of his spiritual cravings, as food allays physical hunger. There is a line in "Reunion in Vienna" which reads, "There is nothing I need so much as nourishment for my self-esteem." Under this motive the instincts of emulation, ostentation, and liberty of action appear. William James once said "nine-tenths of the world's work is done by emulation." The various contests that are sponsored by cooperative associations for excellence in production, beauty of farm or factory surroundings, speed in output, number of new members signed up, etc., are illustrative of the manner in which an organization may capitalize on the urge that man possesses to be recognized.

### III. THE SENSE OF HONOR

Under certain conditions the sense of honor motive provides a fairly satisfactory substitute for the desire for material wealth or at least supplements it. Men feel honored when their names are remembered by others. The hierarchies of rank, orders of distinction, and methods of recognizing individuals who have excelled in some field of endeavor have spurred individuals on to great feats in human prowess and perception in order to win the coveted prize of renown. So strong is this desire for praise that it has a wide range of application as a means to stimulating interest and activity in any mass movement. "The attainment of pleasurable conditions in mind or soul," which is the ultimate objective of economic man, is what Fetter calls psychic income.<sup>5</sup> The honor may or may not be accompanied by an emolument. The annual nationwide pulchritude contests which are sponsored by the different communities throughout the country create an intense rivalry among those vying for local, state, national, or even international honors. This rivalry reveals itself in dazzling dress and magnificent social events for

<sup>5</sup> FETTER, FRANK A., "Principles of Economics," p. 43, D. Appleton-Century Company, Inc., New York, 1911.

the purpose of creating favorable impressions and winning influential friends.

Cooperative organizations have frequently resorted to this device to raise the general standards of quality. Every producer who attains certain prescribed standards in the delivery of eggs, cream, nuts, wool, or tobacco from his farm is awarded an attractive plaque to be hung at the farm gate, on the barn, or in some other conspicuous place where neighbors can see it and he can be apprized of his attainment. Likewise diplomas are given to buttermakers and cheese makers for a sustained record of unexcelled skill in processing efficiency, plant management, or quality output. Thus, it is possible for an organization to build up an *esprit de corps* which will yield unexpected returns considering the small cost of obtaining it. The main difference between the two motives, the *hope of recognition* and the *sense of honor*, is in the degree of achievement. The former inspires men to bring themselves up to an accepted level of conduct or performance; the latter causes them to exert their faculties in such a way that they will demonstrate their superiority by extraordinary achievement. The awarding of honors to a limited number of winners in any instance does not limit the effectiveness of this motive. On the contrary it is a most efficacious means of impelling the restless souls on and upward to new goals of accomplishment, not merely because of personal ambition but for the good of society.

#### IV. THE URGE FOR ACTIVITY

The hypothesis that men are animated by a creative bent that causes them to work for the sheer joy of working was late in making its appearance in economic literature.

Since Wagner there had been no important additions in this branch of theory—in fact, few economists took notice of it until the recent vogue of the “creative instinct” doctrine. This supposed instinct has been thought by many writers of some standing to promise a radical reform of our ideas on work and to point the way toward a great reduction in industrial discontent, . . . <sup>6</sup>

Dickinson goes on to point out that the various writers include under this hypothesis different ideas about human behavior when influenced by the creative impulse.

<sup>6</sup> DICKINSON, Z. C., “Economic Motives,” p. 276, Harvard University Press, Cambridge, 1924.



In Veblen, it is a war against waste, a passion for doing whatever the other instincts want done, in the most efficient possible manner. With Taussig, it is simply invention of a new as well as a more efficient way of doing whatever is to be done. Marot and Hobson emphasize the human craving for novelty, which is supposed to be "creativeness." But all agree that the impulse makes at least some kinds of work intrinsically attractive to most men if not to all, that it takes no thought of the morrow, and causes its possessors to do good work without regard to pay.<sup>7</sup>

Probably no one has given us greater insight into the understanding of this trait of human nature than Veblen. He considers the instinct of workmanship, which expression is "taken to signify a concurrence of several instinctive aptitudes, lack of which might or might not prove simple or irreducible when subjected to psychological or physiological analysis," to be almost as important as the *instinct of parental bent*.<sup>8</sup>

It "occupies the interest with practical expedients, ways and means, devices and contrivances of efficiency and economy, proficiency, creative work, and technological mastery of facts."<sup>9</sup>

"The instinct of workmanship brought the life of mankind from brute to the human plane, and in all the later growth of culture it has never ceased to pervade the works of man."<sup>10</sup>

Man is naturally industrious, not lazy, and if the proper environmental and inspirational conditions are provided, it will liberate his latent creative faculties in an inestimable number of ways. Cooperative organization can be made to provide some of the facilities which may release the human talents and thus promote art, science, literature, and industrial development. This refined motive is worthy of more attention than has been given it as a means of furthering the welfare of society.

#### V. THE IMPULSE TO ETHICAL ACTION

A person's ego causes the individual to be subjectively minded and self-centered. It might be possible for man to live wholly for himself roaming about as a savage in a forest, appropriating

<sup>7</sup> *Ibid.*, p. 277.

<sup>8</sup> VEBLLEN, THORSTEIN, "The Instinct of Workmanship and the State of the Industrial Arts," p. 27, Viking Press, New York, 1922.

<sup>9</sup> *Ibid.*, p. 33.

<sup>10</sup> *Ibid.*, p. 37.

the fruits of nature to satisfy his most elemental needs. But man is a social being! His life is made richer by association, and, in order to enjoy the advantages of it, he is required to subordinate some of his selfish impulses and contribute something toward the welfare of the group. Other members of the group forego immediate personal desires in order to give talent or wealth to some social cause. Thus they gradually learn that the result of combined effort often exceeds their expectations. The greater the extent of cooperation the higher is the state of civilization.

Out of the combination of circumstances involved in living and working together, man is able not only to satisfy a larger ego, but also to accumulate surpluses that permit him to indulge in the rare extravagance of endowing humanity with thoughts and ideals that will ennoble the race. Those who are born into a superior culture are fortunate, because their original equipment of inherited instincts is supplemented and enriched by the products of a complex, contemporary, social life in which there are sympathetic responses of the conscience among individuals composing the group. This reliance on one another keeps associations intact in times of stress. It is this sensitiveness to justice, as well as respect for the rights of others, that is productive of agricultural and industrial reform. What are the ethics which landowners should follow in dealing with the three-fourths million share croppers in this country? What is a fair wage for the industrial worker who has small reserves and even less bargaining power? Should a cooperative association doing business with nonmembers discriminate against them in every possible way? The sense of decency and fairness alone condemns usury and attempts to define the *just price*. Wagner's view was that the impulse of ethical action and the fear of self-reproach are things to be striven toward but never fully realized. It would be difficult, indeed, to cite a case in cooperative experience where it could be claimed that the cooperators were motivated by an altruism free from all stains of avarice. Some doubting soul might sacrilegiously demand proof that the individual or groups performing a commendatory act did so without thought of reward. Who can authoritatively assert that the southern cotton growers were prompted purely by selfish motives, when they formed large-scale state and regional marketing associations? They continued

to patronize these associations through good and evil times, as described by Herrmann and Gardner.

Hundreds of growers, however, believed in cooperative marketing and joined an association because of this belief. This group formed the nucleus around which the present system has been built. Many of these loyal members have delivered cotton to their respective organizations every season without fail. Many times they have overlooked immediate monetary returns because of their belief in the cause of cooperation and its ultimate benefits.<sup>11</sup>

What are the ultimate benefits that the cotton farmers hope for? Can these benefits be measured in terms of money and fame? If so, are they inadvertently throwing up barriers against their own progress?

One observation relative to the social consciousness of groups within a society can be made, namely, that they acquire a finer sense of social obligations as their organizations mature. This is manifested by the extent of the services that are rendered to members and nonmembers and by the general educational programs that are gradually evolved to maintain membership morale and induce intelligent understanding.

#### EXPERIENCE TEACHES THE IMPORTANCE OF MEMBERSHIP CONTACTS

One of the oldest cooperative associations in America follows a policy of disseminating information directly to its growers by a personal visit, at least once a year, of executives from the central sales office. The California Fruit Growers' Exchange has approximately 13,300 members. These members are affiliated with twenty-six district exchanges representing more than 200 local associations. One director is elected for approximately every 9 members in the organization.

In order to get information to the 1,400 directors who in turn convey the information to the growers, the general manager and the sales managers attend at least one district meeting each week throughout the year. These meetings are informal gatherings which start early in the evening with a dinner. The representatives from the Exchange make it a point to meet and visit with

<sup>11</sup> HERRMANN, O. W., and CHASTINA GARDNER, *Early Developments in Cooperative Cotton Marketing*, p. 28, Farm Credit Administration, Cooperative Division, Circ. C 101.

as many directors as possible. After the dinner the group usually retires to another room where they may sit about a fireplace, smoke, and discuss the association's affairs. The local district manager announces that there will be no speeches, that several representatives from the Exchange are present to answer questions and to hear suggestions and criticisms, and that everyone is expected to participate in the discussion. These meetings invariably continue late into the evening and thus afford every director ample opportunity to express his views. This type of field service has been most effective in keeping the members informed about the problems of handling and selling fruit. The arrangement is an ideal one since the members, officials, and employees can mutually assist and counsel one another.

The business policies of the California Fruit Growers' Exchange are established in open meetings convening once a week. The directorate is made up of 26 members representing district associations. The weekly board meetings attract 200 to 500 members who may listen to the reports and advice of the department heads. They hear various policies discussed, and they can ascertain the results of ballots taken on questions vitally affecting the organization and industry. This association spends about \$20,000 annually on advertising media in local papers which circulate throughout the citrus producing district for the purpose of giving the members definite information about the Exchange.

#### EXPERT ADVICE ON MEMBERSHIP RELATIONS

The larger associations of the country should employ someone who is fully qualified by scientific training to direct the field-service department and expertly solve the troublesome membership problems. Proper technique in dealing with members can change the membership morale and eliminate friction and clashes which sometimes strain and aggravate the whole network of relationships within the association and throughout the community. Such an expert would undoubtedly determine some standard procedure that would prove helpful to smaller associations within the same region handling other commodities. If his services begin with the inception of an association, he can anticipate some of the common difficulties and avoid them by inducing

the organization committee to adopt a selective membership policy.

In a going concern, however, he would have no initial opportunity to select the individuals whom he must serve. In the average association the membership may be considered as representative of all the members of the community since organizers of cooperatives have not concerned themselves much about membership qualifications. The effort to obtain a sufficient volume of business has generally eclipsed all other considerations. The only requirement that is prescribed at times is that the member must have some connection with farming in order that he may direct a flow of products to the association. The next step has been that of making the growers' connection with the new association permanent for a period of time by contractual agreement.

#### HOW SHOULD PRODUCERS QUALIFY FOR MEMBERSHIP

Let it be assumed that a procedure is adopted which will require a prospective member in a cooperative organization to pass a comprehensive examination either written, or oral, or both, as well as to be recommended by several neighbors. The qualifications for membership might be based upon his ability as a producer and his attitude toward other people. This plan very likely would not be received favorably in many places. (1) It would be held that an examination would be an unsatisfactory method of determining personal qualifications. (2) It would limit the volume of products received and, therefore, increase the unit costs of cooperative selling. It is strange, nevertheless, that more failures and social disorders have not occurred in cooperative enterprises when the campaign for members has been so inclusive.

**The Economic Status of Individuals.** The movement often has its impetus among the classes in distress or during periods of depression. Consequently, the question is rarely raised concerning the desirability of taking into consideration the economic status of individuals. Laborers and agriculturalists have experienced difficulties in financing their cooperative enterprises. They have never been averse to admitting individuals who are in more comfortable circumstances than themselves because the most pressing need has been working capital and volume of sales. Indeed the instigators of cooperatives have generally been

flattered by the application of the wealthy for membership in their humble organizations. It is only after the association attains some maturity that serious attention is given to the ways and means of avoiding difficulties with members and of barring those who would be undesirable from membership.

There is another aspect to the relationship between the economic status of individuals and willingness to cooperate. It is a generally accepted fact that it is more difficult to organize associations in old established communities where some of the process of a stratification of society has taken place than upon the frontiers where the community is new and its members are struggling for position and recognition. The sociologists explain this by observing that the latest arrivals in the field of organization are the most aggressive in clamoring for a cause and in assuming a part in the functions of the society. Some of these groups will become exclusive, if the law permits, in order that their members may perpetuate their place in the sun. Such an instance is given in the early history of the labor trade-union movement of this country. Professor Commons points out that industrial cooperation was limited by the unwillingness of the workers to admit new members to their circle.<sup>13</sup>

The petty officers of local associations arrest expansion in cooperative activity sometimes because they resist any movement toward federation. They fear a diminution of their own importance by being subordinated to higher officials in the district and central exchange offices.

**Age Groups.** Allegorically the composite life of a community is like a flowing stream. It is constantly varying in temperament and character as it is influenced by the vicissitudes of time. Now, it is a pure stream flowing along with ripples here and eddies there; nevertheless, it flows serenely on to the sea. Again, it is but a silver thread tortuously winding through the countryside. At times it is swelled into an angry torrent. The heavy rains pollute it with the silt of the land and debris jauntily rides its crest only to clutter the landscape at some distant place when its fury is spent. The composite life of a cooperative association is like that—as is life in a country community, no better, no worse. Those who control the flood gates of admission into an associa-

<sup>13</sup> COMMONS, JOHN R., "Institutional Economics," p. 757, The Macmillan Company, New York, 1934.

tion, however, find it within their province to guide it to success by determining its cast. Many factors aside from any efforts at membership selection will affect the distribution of age groups in an association. The constituent elements of the community may be relatively unstable owing to the uncertainties of harvests, the status of industries, or the seasonal nature of production. Economic opportunities in other areas may attract the young and adventurous members away from their home communities, thus causing marked changes in the population, character, and life history of the forsaken neighborhood. The outflow of people from a community may create an undercurrent which will cause residents of other areas to move in and fill the vacated places. These immigrants will in all probability possess different ideals and standards. Their customs, laws, habits, traditions, and mores will color and change the cultural and economic institutions of the community. In instances where the soil is depleted, and the community begins to dwindle in population because it is devoid of natural advantages, opportunities diminish and a cooperative desert is created. The existence of a cooperative is, thus, closely interwoven with the fortunes of a community and the life of its constituents.

Cooperative memberships in the aggregate tend to age rapidly. No data are available on the average length of cooperative memberships, but it is brief compared to the productive life of farmers. It is a general complaint of cooperative executives that it is difficult to keep the associations youthful by bringing young men in as rapidly as the old take leave. If an association fails to keep the rank and file of its membership young, it begins to drift down the stream into oblivion as its members age and make way for another generation. Perhaps, the objective of the membership relations personnel should be that of reducing the average age of its membership in order to assure perpetuity to the organization it serves. The younger generations will add life and vitality to an association by their zeal and aggressive energy. It is sometimes feared that too many young men will run an association amuck, but the older and more experienced members are usually on hand to prevent a catastrophe. For example, the California Fruit Growers' Exchange requires that all important questions of policy be first considered by committees of the board of directors with the executive head of the depart-

ment. Questions may be referred to an advisory committee consisting of *seven veteran directors*.

The real bulwark of a cooperative, with all due respect to youth and age, is embodied in the men who are in the prime of life. They should comprise the largest, most productive and stable element among all members. The ideal situation is to have a proportional distribution of the age groups in the cooperative association consistent with the age groups representing the active producers in a community. The same scheme of distribution would be most desirable in sharing the offices and association's responsibilities among the adults.

#### SOCIAL AND ECONOMIC DEPENDENCE

The life of agricultural communities is close knit, and its residents are dependent in numerous ways upon one another to make life pleasant and profitable. There are many farm tasks even in this age of improved machines that require more hands than are ordinarily available on a single farm. The easiest and most expeditious way of performing these tasks is to call in one or two neighbors. The topography of an area can limit communities within narrow confines and make close coordination necessary. Local cooperative enterprises may be dependent upon the support of nearly every farmer in the community in order to receive, grade, and store grain; to gin and class cotton; to segregate, mark, and ship livestock; to pool, test, and manufacture dairy products; or to select and order purchases of farm supplies. All these services and many more must be performed without entailing prohibitive costs. "The pack is the strength of the wolf, and the wolf is the strength of the pack." To assure harmony and good will, each individual must fully realize his own dependence upon the other members of the group and must respect their right like his own. Unless there is this high-minded appreciation and understanding, life will become miserable and unbearable in a compact community. The valley hemmed in by a wall of hills or the altitude which isolates life on a high plateau might easily become a prison of dissension. The affairs of business are often carried over into the social, educational, and political organizations. Schisms breed in this culture and each organization forms a battleground for the factions to renew their



warfare at any provocation. Under these circumstances, questions can rarely be solved according to their merits.

After Minnesota farmers had been swept into cooperative organizations by the 1921-1923 wave of enthusiasm led by Sapiro and others, a sociological study of their marketing attitudes was made.<sup>13</sup> It was a critical time to make observations of various groups that had been sobered from their economic spree by disappointments and failures. In this study emphasis was given to the importance of social and geographical distances, environmental and cultural influences, experience and education as factors affecting business organizations. Farmers will more readily follow the leadership of other farmers than of individuals outside their own social pale. Therefore, it was concluded that the sons and daughters of farmers should be trained to assume leadership in the agricultural cooperative movement. The field service agents of cooperatives learn to recognize innate qualities in individuals, and they claim that biological differences are important. The direct descendants of one people may possess a background and training either congenial or hostile to the ideals of cooperation. Peoples of northern Europe have long been accustomed to the adjustment and dependence upon each other necessitated by the niggardliness of nature in extreme northern regions. As a result of this they combine in collective undertakings more willingly than peoples of southern climates where life is made easier by the generosity of nature. This theory finds support in the conclusions of the Minnesota study.<sup>14</sup>

Education is another outstanding factor contributing to the promotion of cooperative ideals. Generally, the more education an individual has the more responsive he is to plans for collective effort.<sup>15</sup> Long experience in the associated effort, such as is common to educational programs, is itself a good foundation for further collective effort.

The Jones and Manny studies are mainly subjective observations of the behavior of agricultural producers as members of an association. Their investigations are confined to a small

<sup>13</sup> ZIMMERMAN, CARLE C., and J. D. BLACK, *The Marketing Attitudes of Minnesota Farmers*, *Tech. Bul.* 45, 1926.

<sup>14</sup> *Ibid.*, p. 50.

<sup>15</sup> MANNY, T. B., *Farmers' Experiences and Opinions as Factors Influencing Their Cotton-marketing Methods*, *U. S. Dept. Agr., Circ.* 144, p. 7, 1931.

number of associations and are concerned with prices, outside interference, management and service costs, contractual relations, and educational influences. They present some statistical measurements of these influences and appraise their relative effects upon the social and economic status of particular organizations. The numerical evidence presented is not intended to be regarded as typical of all organizations. These sociological studies thereby indicate a procedure that may be followed in determining specific difficulties.

#### DISSEMINATING COOPERATIVE IDEAS

Ideas are transmitted from one person to another chiefly by three methods:

1. Demonstration or example
2. Through the spoken word
3. The use of mechanical means

Ideas form the material of judgment, and judgment is complete when contrasts are made between different ideas. Every idea finds its way into the mind through one or more of the five senses: seeing, hearing, feeling, tasting, and smelling. The most direct and efficient means of conveying thought is by the first method—demonstration, because it usually involves more than one of the senses, possibly all five of them. Persons who have not been subjected to a strict mental discipline or have not had the advantage of a formal training in thought as is afforded in an educational institution are apt to rely more upon combinations of their senses.

Occupations that require physical as well as mental exertions, such as farming, mining, and fishing, require the individual to formulate his ideas by bringing into play all of his senses. A more complete use of the senses of taste, feeling, and smelling is closely related with the physical welfare of the individual, and such an intense use of the senses tends to make one subjectively minded. The senses of sight and hearing are, however, more completely developed in objective thinking.

On various occasions cooperative leaders have contrasted ways and means of disseminating information and appraising their relative merits. They direct considerable attention to the technique of editing house organs. The subject matter of these publications is selected with the view to make the farmer mem-

bers receptive to new ideas by giving them information which relates directly to their specific problems in production and distribution. Whenever possible, it is desirable to supplement the printed page with pictorial descriptions of these ideas. Farm folks find it difficult to master technical details. They do not study so thoroughly as would be desirable the bulletins issued by research organizations, agricultural colleges, and industrial concerns. The contention is that since farmers receive their impressions and ideas through a more complete utilization of all their senses, the method of disseminating information must be modified to take this into account. The nature of one's occupation affects the distribution of the time that one can devote to reading, attending meetings, and listening to the radio. Oscar Wilde once said, "In the country people get up early in the morning because there is so much to do, and they go to bed early in the evening because there is so little to think about." Wilde does not do justice to the country people in his witticism, for there is much to think about and still more to read, but the individual is so physically exhausted at the end of the day, that he finds it difficult to think; also the lights are often so poor that it is impossible to read without injuring the eyes. In order to maintain membership morale, it is essential that the larger cooperative sales associations give close attention to the development of expert field service and to the methods of relaying information by actual demonstration or example. This is one important reason for advocating the federated type of association, since producers are better able to form judgment from the experiences derived by operating local associations than from reports submitted by a central office.

The second method is the use of the spoken word. The individual who transmits information thus may, through his personality as well as his attitude toward his listeners, favorably prepare them to receive the ideas which he expresses. Frequently, the manner in which he states a fact may be as important as the fact itself. The system of representation in cooperative organizations, as well as the nature of the business, requires that much of the information relating to business operations be conveyed to the members through personal contact and concrete illustration. The management of such concerns is reluctant to

publish certain information about the nature of their business operations, not because they desire to withhold this information from their members, but because they run the risk of inducing unfair competition through misrepresentation which will unfavorably affect the consumers' demand for the commodities which they merchandise.

The third method is the use of mechanical means, such as the printed word, telephone, telegraph, and radio. In many instances this is the most economical way of transmitting ideas to large numbers of people. Most of the large-scale cooperative organizations maintain a publicity and advertising department whose function it is to keep the organization in close contact with consumers on the one hand and producers on the other. Some of the rules which have been laid down for editing cooperative house organs are summarized as follows:

1. Print market information on front page.
2. Make all articles and news items seasonable.
3. Confine circulation to growers.
4. Give information that is absolutely reliable and without bias.
5. Make no reference to association troubles in the house organ.
6. Do not allow income from advertising to influence editorial policies.
7. Publish no articles that are advertisements in disguise.
8. Answer growers' technical questions.
9. Use no space for casting aspersions.
10. Word headlines so that the interest of the readers may be stimulated.
11. Use editorial notes of explanation.
12. Do not publish articles contributed by members that will lead to controversy.
13. Delete items praising the management.
14. Accept only fair advertising that is of interest to the members.
15. Enliven the publications with many illustrations.

The essential point in the dissemination of information is to utilize the various methods in such a way as to get maximum results.

## PROGRESS OF MAN IS SLOW

"The mills of the gods grind slowly, but, ah, they grind exceedingly fine." The progress that mankind is making towards creating a better society in which to live is so gradual that it aggravates the impatient social reformers. They may console themselves, however, with the fairly certain fact that there is a constant moral force exerted by intelligent individuals in society towards cultural advancement of the human race.

The most crude, barbaric traits are being suppressed by a rationalization process. The motivations of self-interest, jealousy, fear, and vanity are being modulated and refined from a lower to a higher order by the introduction of new customs, laws, and modes of human conduct. The objective for some distant period is the organization of human activity so that the culture will reflect the higher impulses for ethical action, the result of which will be mutual trust, cooperation in social and economic activities, and a kindred spirit for the general welfare of man.

None of the inclinations toward rivalry and competition for the nourishment of the individualistic ego need be destroyed; these are simply projected into fields that will direct their force toward the betterment of all society. They are lifted above the common level of being directed against the economic interests of some unfortunate individuals or weaker groups.

Mankind has enough innate qualities to create a higher civilization through a full development of its intellectual powers. Every new idea passes through at least four evolutionary stages: origination, perception, dissemination, and assimilation. (1) An idea is conceived; if it is in the field of mechanics, it is an invention; if in the field of social science, it may be referred to as a mental concept. (2) Someone must appreciate the worth of the new concept—they perceive its value as applied by humans in their relations to one another. (3) After a person originates a new idea and it has been tested in the judgment of associates, it may be pronounced worthy of adoption by society. When this decision is made, it becomes necessary to disseminate information relative to its application and possibilities in alleviating the conditions of man. (4) The judgment of those who foster the new idea may be confirmed by popular recognition. At this point man

is ready to assimilate the next suggestion conceived by his leaders for improving his economic and social status.

It is the responsibility of this generation not to live in the trough of regression, but to rise toward a higher plane. The relationships that are spontaneously developed between individuals and between cooperative groups indicate the cultural advancement of mankind as well as the progress made.

#### Questions

1. Is it necessary that an individual be socially conditioned for membership in a cooperative association?
2. Enumerate several motives for economic action.
3. Are the motives positive or negative?
4. Which motive is the dominant economic force affecting membership relations?
5. Differentiate between the motives "hope of recognition" and "the sense of honor."
6. Critically appraise this statement: Man is naturally industrious and will work for the sheer joy of creating things.
7. Can an economic motive be nonegoistic?
8. Should individuals be required to present certain qualifications for membership in a cooperative enterprise?
9. What methods may be used in disseminating information to members of a cooperative association?
10. Trace the course of an idea through its evolutionary stages of development.
11. In what ways are cooperative associations affected by the rate of turnover in membership?

**PART III**  
**LEGAL CONSIDERATIONS OF THE COOPERATIVE**  
**METHOD OF MARKETING**

## XI

### *Legal Basis of Agricultural Cooperative Associations*

*Under the dictum of the common law, it was lawful for farmers to sell and buy collectively. Some courts, however, adjudged such associations as illegal combinations restraining trade. Prior to the passage of enabling legislation in the separate states, producers were compelled to either keep their associations unincorporated or to incorporate them under the general corporation laws or under laws legalizing religious, fraternal, educational, and benevolent societies. This proved to be highly undesirable.*

*The first law legalizing cooperative associations was passed in 1857 in New York; Michigan passed a law in 1865, and a few other states enacted enabling statutes before the turn of the century. The Wisconsin and Nebraska laws of 1911 and the Kentucky Law of 1922 became the prototypes for laws in most other states. The federal law—the Capper-Volstead Act—was passed in 1922 legalizing agricultural cooperative associations engaged in interstate commerce. This law is the Magna Charta for cooperative marketing associations in America. Supplementary legislation, such as the law that created the Division of Cooperative Marketing in 1926, the Purnell Act of 1925, the Act to Prevent Discrimination by Boards of Trade against Cooperatives of 1927, and the Agricultural Marketing Act of 1929, has expressed public policy in favor of farmers' cooperative associations.*

*Although the courts of the country at first declared cooperatives as violators of the antitrust laws, later decisions definitely declared the opposite to be true. The early court decisions also declared state laws that exempted farmers' cooperatives from the state antitrust laws as vicious class legislation not amenable to the provisions of the Fourteenth Amendment to the United States constitution. Later, however, the courts reversed this opinion and held that agricultural cooperative associations constituted a general classification exemptible from antitrust laws. Purchasing associations are also legalized in the majority of the states.*





## CHAPTER XI

### LEGAL BASIS OF AGRICULTURAL COOPERATIVE ASSOCIATIONS

Economic activity is influenced by statutory law, common law,<sup>1</sup> and the decisions of the courts. One eminent economist contends that the Supreme Court of the United States "occupies the unique position of the first authoritative faculty of political economy in the world's history,"<sup>2</sup> and that all values and prices in their final analysis are determined by the opinions of those that sit on the bench. Hence, the status of cooperatives is just as contingent upon the welter of judicial and legislative opinion as upon membership relations and other conditioning factors.<sup>3</sup>

#### COOPERATIVES AND THE COMMON LAW

In order to understand more clearly the early attitude of the courts toward cooperative associations, it is necessary to review briefly the legal background respecting combinations, restraint of trade, and monopolies. The common law of England for centuries did not tolerate combinations or approve of many contracts which restrained trade. This was particularly true with respect to activities that hampered the trade in food prod-

<sup>1</sup> The common law, it will be recalled, is that rule of action which has grown up from old and popular usage, from the decisions of the courts, and from the opinions of text writers and commentators in contradistinction to the written statutory law, civil or Roman law, or the ecclesiastical law.

<sup>2</sup> COMMONS, JOHN R., "Legal Foundations of Capitalism," p. 7, The Macmillan Company, New York, 1924.

<sup>3</sup> The reader is advised to consult the following three excellent books on the subject of cooperative law for detailed historical and analytical material. EVANS, FRANK, and E. A. STOKDYK, "The Law of Agricultural Cooperative Marketing," The Lawyers Cooperative Publishing Company, Rochester, N. Y., 1937; NOURSE, EDWIN G., "The Legal Status of Agricultural Cooperation," The Macmillan Company, 1928; HANNA, JOHN, "The Law of Cooperative Marketing Associations" Ronald Press Company, New York, 1931. The bulletin *Legal Phases of Cooperative Associations* by L. S. Hulbert, *U. S. Dept. Agr. Bul.* 1106, 1929, is also excellent.

ucts or necessities of life. Consequently, rigid laws regarding forestalling, engrossing, and regrating were passed by Parliament.<sup>4</sup>

The Ecclesiastical Courts and the teachings of Christianity disapproved of interest (usury) and profits and of the activity of merchants in general. Commerce which had been in general disrepute during the feudal ages grew in importance in England, and the law merchant then defined the rights and duties of those engaged in it. Quite naturally the common law looked unfavorably upon any contract which lessened competition. Gradually, however, the common law relaxed and interpreted restrictions of competition on the basis of their *reasonableness*, leaving it entirely up to the courts, however, to determine what was reasonable or unreasonable. In 1844 Parliament completely repealed its laws against forestalling, regrating, and engrossing on the theory that such acts promote rather than restrain trade.

Under the common law, individual property rights were recognized. Included in these rights was the right of farmers to sell farm products and to buy farm supplies collectively.

Other groups of citizens could also lawfully associate themselves together for the purpose of collectively buying, processing, and selling farm products as well as to engage in industry. All groups were then on an equal plane under the law, all being permitted to handle, buy, process and sell commodities collectively and all subject to the common law prohibition of contracts or combinations that unduly, or unreasonably, restrained commerce.<sup>5</sup>

Later corporation laws were passed by the states that gave a more secure status to commercial concerns incorporated under them. When farmers' organizations were established to market farm products and to buy supplies, thus making necessary laws legalizing their collective activities, a storm of protest was at once raised on the grounds that the liberty or property of persons

<sup>4</sup> Forestalling consisted of buying articles before they reached the market place with the intent of selling them at a higher price. Engrossing consisted of buying up large quantities of commodities any place with the aim of later resale at an enhanced price. Regrating consisted of buying provisions in a market with the intent of reselling in the same market or fair or one within five miles at a higher price.

<sup>5</sup> MILLER, J. D., *The Philosophical and Legal Background of the Cooperative Movement in the United States*, p. 12, "American Cooperation, 1935," *The American Institute of Cooperation*, Washington, D. C.

would be deprived without due process of law and that the associations were in restraint of trade in violation of the common law. "While there were a few judicial decisions otherwise, the weight of judicial opinion is that under the common law farmers had the clear right to associate themselves together in any number, however large, for the purpose of making collective sales of their products or collective purchases of their supplies."<sup>6</sup> There were relatively few associations in this country before federal and state enabling legislation was passed.<sup>7</sup>

#### ENABLING LEGISLATION—STATE LAWS

Before specific statutes were passed in the several states legalizing cooperative marketing associations per se, associations had either to operate as unincorporated groups or to incorporate under the general incorporation laws. Some were granted special charters by state legislatures before the general incorporation laws were enacted. This was not entirely satisfactory, in view of the fundamental difference in the objective, as well as the mode of operation of the cooperative from the general corporation. The sheer difficulty of organizing under existing laws necessitated the enactment of enabling legislation which would legalize the type of company, such as the cooperative. Some associations, therefore, sought refuge by incorporating under the laws legalizing such nonprofit groups as religious, fraternal and literary clubs, libraries, cemetery associations, educational, scientific and benevolent institutions.<sup>8</sup> The veil of uncertainty still hung over cooperatives, however, even though no particular laws were enacted preventing their formation and operation. Amendments to the general corporation laws permitting cooperative associations were not deemed satisfactory as the number of associations multiplied and as the cooperatives became recognized as distinctive types of business concerns. Approval through negative

<sup>6</sup> *Ibid.*, p. 15.

<sup>7</sup> Of 18,923 associations for which the dates of organization are recorded, only 194 were organized prior to 1890. From 1890-1900, 756 other associations were started. This indicates how small a number of cooperatives existed in the United States before enabling legislation was passed. For more data see Statistics of Farmers Selling and Buying Associations—United States 1863-1931, *Federal Farm Board Bul.* 9, Table 2, 1932.

<sup>8</sup> The Pachappa Orange Growers' Association of California incorporated under the Benevolent Corporation Act of California in 1892.

means, or by inference, was not nearly so desirable as a positive statement of law granting assent.

Perhaps the first statute authorizing incorporation of cooperative associations was passed in New York in 1857 when a mutual town cooperative fire insurance law was passed. Certainly it was a forerunner of cooperative laws legalizing other types of cooperative business. This New York law was amended in 1879 to permit cooperative fire insurance companies to transact business in more than one town. In 1865 Michigan passed a law authorizing "the formation of mechanics' and laboring men's cooperative associations." This law is often reported as being the first cooperative marketing law. It was amended in 1875 to include agricultural and horticultural associations. Some of the other early cooperative laws were passed in the following states: Massachusetts, 1866; New York, 1867; Pennsylvania, 1868; Connecticut, 1870; Minnesota, 1870; New Jersey, 1875; California, 1878; Tennessee, 1882; Ohio, 1884; Kansas, 1887; Wisconsin, 1887; Nebraska, 1911. Since these early dates all of the states of the union, except one, have passed cooperative laws. Many states amended their early laws or completely revised their statutes and adopted new ones. Such process of amending is still going on; for example, the Wisconsin legislature has amended the cooperative law at every session of the legislature since 1919, except during the 1925 session. In 1921 it was not merely amended but completely revised. The 1935 Iowa legislature revamped the cooperative law of that state so as to confine its application more directly to agricultural producers' associations.<sup>9</sup> The Wisconsin law of 1911 (which was copied by sixteen states), the Nebraska law of 1911, and the Bingham law of Kentucky of 1922 became models after which other states patterned their laws. The Kentucky law, in particular, became the so-called Standard Cooperative Marketing Act and, according to Hanna, was copied in toto or with slight modifications by thirty-nine states and Puerto Rico.

<sup>9</sup> Some state laws do not restrict the cooperative to agricultural producers nor do they insure that the organizations incorporated under them are cooperative in spirit as this term is understood. Thus, it is found that some private individuals have organized cooperative oil companies, use the word cooperative in their title, but run the association for the profit of the private organizers rather than the patrons—an illustration of meeting all the conditions set up in the law, but still being a subterfuge.

The development of the Standard Cooperative Marketing Act includes a bit of interesting cooperative history. During the period from 1915 to 1920, the cooperatives in California made considerable headway under the energetic leadership of Col. Harris Weinstock,<sup>10</sup> state market director.

A San Francisco lawyer who had obtained considerable experience in drawing up the articles of incorporation, constitutions and bylaws, and marketing agreements for some of the larger California cooperatives was in Col. Weinstock's office. An ardent exponent of cooperative marketing associations, he soon realized that the development of cooperative marketing in this country was held back by the lack of enabling legislation in most of the states, and by the incompleteness of the legislation which some states had passed as their cooperative laws. He, therefore, drew up a cooperative marketing bill in 1919 which was far more specific and detailed than most of the laws already enacted by other states. The first state to adopt this bill practically in its entirety was Arkansas in February, 1921. Thereafter other states became so much interested in the provisions of the act that in the three years, 1921-1923, inclusive, twenty-six states adopted a standard cooperative marketing law. The laws of other states, as that of Wisconsin, were not publicized so much as this so-called model law, although the Wisconsin law was considered by many to be equally as good as that drawn up by Mr. Aaron Sapiro. Judge Bingham in Kentucky adopted the provisions of this bill and was instrumental in having the Kentucky legislature of 1922 pass this oft copied bill with its revisions. This Kentucky law, also called the Bingham Act, was typical of the standard cooperative act. Most states passed their enabling acts during the quinquennium, 1921-1925.

With so many states copying this law, and the others copying the laws of Nebraska and Wisconsin of 1911, which were not fundamentally different in principle from the standard act, considerable uniformity in state legislation concerning cooperative marketing was obtained. As a matter of fact, very few laws have such uniformity between states as do the laws legalizing cooperative marketing.

<sup>10</sup> Cooperative Marketing, Letter of Chairman of Federal Trade Commission, *Senate Document 95*, p. 326. 70th Congress, 1st Session.

Whether the cooperative law should be (1) a broad, general, and liberal enabling act, or (2) a specific, closely defined act was a subject of controversy at the time these state statutes were enacted. The advocates of general laws pointed out the advantages of latitude and of local expression in the organization of associations; those that favored the specific laws held that it was necessary to definitely define cooperation, incorporate its objectives and powers, strive for uniformity, and leave little self-expression to the local associations. The latter wisely contended that too few people were sufficiently informed to rely upon local talent to incorporate the truly cooperative features in their organizations. Therefore, a specific law was considered an important educational force as well as an enabling act. Had detailed laws been in existence from the very beginning, a still greater uniformity in the organization and operation of associations would have resulted and a larger number of the associations would be truly cooperative.

An account of the evolution of these laws will not be given here. A cursory review of the Standard Act will show the inclusion of the following provisions:

1. The declaration of policy is as follows:

In order to promote, foster, and encourage the intelligent and orderly marketing of agricultural products through cooperation, and to eliminate speculation and waste, and to make the distribution of agricultural products between producer and consumer as direct as can be efficiently done; and to stabilize the marketing of agricultural products, this act is passed.

2. Membership—restricted to agricultural, horticultural, and livestock producers, but one association may become a member of another. Twenty or more producers are necessary to form an association.

3. Incorporation—may incorporate as a nonprofit, cooperative association with or without capital stock.

4. Powers—permitted to engage in buying, selling, storing, manufacturing or any other utilization of products delivered by the members; to buy personal and real property; to finance all operations; to borrow money, set up reserves, draw up contracts, and exercise and possess all powers, rights, and privileges necessary or incidental to the purpose for which the association is organized.

5. Articles of incorporation and bylaws—state the name, purpose, and place of business of the association; the amount of capital stock and shares or, if nonstock, the property rights of its members; the time and place of meetings, quorums, etc.; number of directors; election of officers.

6. Stock ownership—limits the number of shares of stock which any member may own, and prescribes the conditions under which stock will be issued; for a nonstock association it states the manner in which membership certificates are granted.

7. Marketing contracts—permits associations to make contracts with its members for the delivery of their products; limits the length of such contracts to 10 years; provides for remedies in the event of breach of contract; considers it a misdemeanor for anyone to induce a member to violate the contract.

8. Annual reports—all associations are required to prepare annual reports.

9. Use of term "cooperative"—only associations incorporated under the act are permitted to use the word in their corporate title.

#### LAWS LEGALIZING CAPITAL STOCK ASSOCIATIONS

The first laws enabling farmers to organize on a cooperative basis were simply revisions of the general corporation laws all of which considered capital stock as an integral part of corporate organization. As a matter of fact the concept of making capital stock an essential part of cooperative companies conformed to the types of associations which were most common during the last decades of the past century and the first decades of the present, namely, cooperative creameries, cheese factories, and grain elevators. The dairy and grain cooperatives required capital for their land, buildings, and machinery as well as for current operations. Therefore, as long as the legislatures passed cooperative laws that permitted voting on a one-man, one-vote basis, permitted paying only a nominal interest rate on capital stock and allowed the distribution of net earnings on a patronage basis rather than on a stock-ownership basis, the chief interest of the organized dairymen and grain producers was met. The idea of associating profits and capital stock ownership was still prevalent, however, even after the cooperative statutes provided for the distribution of earnings on a patronage basis. The

concept of a nonstock nonprofit type of organization which renders superior marketing services for producers at cost was practically unheard of before 1900, and received only slight attention by state legislatures prior to 1915.

#### NONSTOCK LAWS

Many organizers of cooperative marketing associations, however, looked unfavorably upon the capital stock type of association. They felt that such a cooperative was simply a modified type of profit-sharing corporation. It was difficult for many to see how such a company was really cooperative, inasmuch as services were not restricted to members, since shares of stock could be sold to others than actual producers, and profits (or losses) on nonmember business accrued to the benefit (or detriment) of the bona fide members. Therefore, a plan of restricting the services to members only, of retaining the membership in the bona fide producers, of eliminating the capital stock type of financial structure, and of conducting marketing services at cost for members, was considered far more desirable and in conformity with the basic philosophy of cooperation. State laws legalizing a company of this kind were needed. As in so many cases, necessity became the mother of invention, and the laws enabling nonstock nonprofit types of companies were drawn up and enacted.<sup>11</sup>

As early as 1895 California enacted the first law providing for nonstock cooperative associations. It was not until 1914 that Congress passed the Clayton Act which exempted nonstock farmer companies from the Sherman Antitrust Act. The early California law was not specific with respect to the exact manner in which nonstock organizations had to be organized; nevertheless, it became the pattern or framework upon which other laws embodying the same principles were enacted. Only 8 states are reported to have passed legislation legalizing nonstock cooperatives prior to 1918. The reasons for desiring a nonstock law rested primarily on the viewpoint that the capital stock cooperatives still retained the capitalistic idea of organization. Capital, it was felt, should be loaned to the company rather than invested in it. It should not be the basis of membership.

<sup>11</sup> See Chap. III, *The Emergence of the Non-stock Association*, in Nourse, *op. cit.*, for a good discussion of this subject.



Membership is a *personal* matter divorced from ownership of capital. It was felt that the nonstock type of organization was the proper cooperative method of organizing inasmuch as it eliminated the base upon which dividends were declared and upon which voting rights were based. In spite of these beliefs held by the advocates of nonstock cooperative associations, the authors believe that a cooperative organization may be just as truly cooperative when incorporated under the capital stock laws as under the nonstock laws.

Since there is this important difference in organization, a number of states have passed two laws legalizing cooperative associations, one law permitting organization with capital stock, and the other without capital stock. Other states, however, incorporate in the same statute the permission to organize on either basis. As late as 1929 a decision of an Oklahoma case<sup>13</sup> indicated that the United States Supreme Court felt that the associations incorporated under the nonstock law of that state were truly cooperative, whereas those incorporated under the capital stock law were but little different from the usual corporation. This decision indicates that some courts retain the view that the nonstock corporation typifies more nearly the cooperative association in fact.

#### UNIFORM AGRICULTURAL COOPERATIVE ASSOCIATION ACT

At the instigation of one of the large general farm organizations in 1925, the National Conference of Commissioners on Uniform State Laws was requested to prepare a uniform cooperative marketing act. After 11 years, the fifth revised draft of the act was finally approved by the National Conference of Commissioners on Uniform State Laws and by the American Bar Association meeting at Boston, Mass. in August, 1936. In a prefatory note to the act the following statements are made:

The act is especially designed for producers of agricultural products, and membership in the associations is limited to such producers. It provides safeguards that it is thought will avoid abuses detrimental to the cooperative movement. It should meet the requirements of the Cooperative Banks, Rural Electrification and other Federal agencies doing business with cooperative associations of farmers.

<sup>13</sup> *Frost v. Corporation Commission of Oklahoma*, 278 U. S. 515.

The restrictions on dividends and doing business with nonmembers conform to the provisions of the federal statutes, exempting such cooperatives from income tax and antitrust laws, and to what may be considered sound practices for nonprofit corporations.

The procedure for organizing a cooperative association is in harmony with the provisions for the organization of business corporations under the Uniform Business Corporation Act. Other provisions [Sec. 6 (*d*), Sec. 9, (*I*)] follow modern corporation statutes, in an attempt to eliminate many troublesome questions that may arise under the *ultra vires* doctrine.

It is thought that the act will place cooperative associations on a higher business plane, approaching that of business corporations, so as to reduce the wide chasm that both laymen and lawyers have been prone to consider as separating cooperative associations from business corporations, without depriving such associations of any of the rights, privileges or exemptions which they have heretofore enjoyed.

The members and directors are given much latitude in providing suitable limitations and restrictions on the business and management of the association. They may insert such safeguards and restrictions in the Articles of Incorporation and in the Bylaws as may be deemed necessary in view of the particular type of association or the kind of business in which it is engaged.

The act avoids the expense of recording a large number of uniform membership contracts, by providing for the recording of only one of such contracts, and showing by affidavit the list of members who have signed similar contracts. It is thought that the act will give the desired flexibility in the management of cooperative associations, and at the same time provide safeguards and apply to their operations principles deemed vital to their success.<sup>13</sup>

#### FEDERAL LAWS

Federal laws legalizing cooperative marketing and purchasing associations were not enacted so early as state laws, even though many cooperative associations engaged in interstate and foreign commerce were in need of federal enabling legislation. Although associations do not incorporate under existing federal laws, the status of those engaged in interstate and foreign commerce is defined. A brief statement of federal acts bearing upon cooperative associations follows:

<sup>13</sup> Copies of the uniform act may be obtained from the Secretary of the Committee of the National Conference of Commissioners on Uniform State Laws, 1140 North Dearborn St., Chicago.

**Sherman Antitrust Act.** The Sherman Antitrust Act was passed by Congress at a time (1890) when cooperative associations in this country were in their infancy. Considering the generally prevalent disdain for trusts and combinations, it was natural that the courts of the country should interpret cooperative associations in the spirit of the antitrust law. The first Section of this act reads as follows:

Every contract, combination in the form of trust or otherwise, or conspiracy in restraint of trade or commerce in any Territory of the United States or of the District of Columbia, or in restraint of trade between any such Territory and another, or between any such Territory or Territories and any State or States or the District of Columbia, or with foreign nations, or between the district of Columbia and any State or States or foreign nations, is hereby declared to be illegal. Every person who shall make any such contract or engage in any such combination or conspiracy shall be deemed guilty of a misdemeanor, and, on conviction thereof, shall be punished by fine not exceeding \$5,000, or by imprisonment not exceeding one year, or by both said punishments, in the discretion of the court.

Until 1910 the United States Supreme Court consistently ruled that restraints of trade, whether reasonable or unreasonable, were prohibited by this act. But after 1910 the so-called "rule of reason" became the criterion of infractions. Mere size and method of organization were not indications in themselves that trade was being restrained. Action, rather than size, was questioned. As the large-scale cooperative associations grew to an extent that they sold products from all parts of a state they were vitally interested in knowing their status under the Sherman act. Decisions of the courts soon showed that the cooperatives had a precarious standing under this law and were easily adjudged as combinations in restraint of trade. Judge Miller points out in the article quoted on page 270 that during the period 1890-1910 "directors and officers of selling cooperatives were indicted in five states under state antitrust laws, and in Louisiana under the Sherman act."

The growth of large-scale cooperatives might easily have been retarded by the Sherman Antitrust Act in two ways: (1) in a direct way by the adverse decisions of the courts which adjudged cooperatives to be combinations in restraint of trade; (2) in an indirect way by creating the belief that this law was an effective

means of curbing monopolies and, therefore, that there was no particular need for cooperatives to combat the trust. In Sweden where no legislation has been enacted to curb the cartels, consumers and producers resorted to cooperation to fight monopolism. The Swedes did not rely on political measures to win the battle against the trusts as the Americans generally have. They took economic measures. As a direct consequence, numerous consumers' cooperative producing and distributing companies have emerged in Sweden. These might not have arisen if competition had been operating freely. During the postwar period, however, the more liberal attitude toward large-scale enterprises and their methods of conducting business,<sup>14</sup> exemplified in many instances by powerful holding companies, may have been a factor in causing people to consider cooperation as the only effective means of meeting these giants in business and industry. Does not the "cooperative" boom of the thirties reflect in part this public sentiment?

**The Clayton Act of 1914.** Leaders of the cooperatives desired a definite statement in the laws which would exempt them from the provisions of the Sherman act. In 1914 the Clayton amendment was passed and exempted agricultural and horticultural organizations instituted for the purpose of mutual help. Section 6 of this act included the following provisions:

That the labor of a human being is not a commodity or article of commerce. Nothing contained in the antitrust laws shall be construed to forbid the existence and operation of labor, *agricultural, or horticultural* organizations, instituted for the purposes of mutual help, *and not having capital stock or conducted for profit*, or to forbid or restrain individual members of such organizations from lawfully carrying out the legitimate objects thereof; nor shall such organizations, or the members thereof, be held or construed to be illegal combinations or conspiracies in restraint of trade, under the antitrust laws. [Italics by authors.]

It will be noted that this provision simply exempted the nonstock, nonprofit cooperative association but did not clarify

<sup>14</sup>The reader is advised to read the case *Appalachian Coals, Inc. v. United States*, 288 U. S. Reports 344 (1932) for the U. S. Supreme Court's approval of the organization of an agency to market and fix the price of coal for 137 independent coal mining companies without being considered in violation of the Sherman Antitrust Act. It approves the extension of cooperative principles to private companies.

the status of the capital stock associations. Since a large number of farmers' organizations had capital stock, and others were interested in organizing with capital stock, there arose a persistent demand that a definite federal law be enacted which would legalize both types of associations. Precedence had already been set by the passage of many state cooperative laws. It should not be inferred from the wording of this act that farmers' nonstock associations were permitted to engage in illegal business operations; it simply expressed the opinion of Congress that the organizations per se were not illegal and were not to be dissolved if they met the conditions specified in Section 6.

**The United States Department of Agriculture Model Bill.** Following the passage of the Clayton Act it soon became evident that associations which were to benefit from its enactment would have to be incorporated as nonstock associations. In order to bring about a uniformity of state and federal laws the Department of Agriculture at Washington prepared and published in 1917 a department bill which was suggested as a model to the several states. In drafting this bill the experiences of states that had already incorporated certain specific features in their cooperative laws were considered.

The bill, which was to serve as a model, included provisions for the incorporation of either capital stock or nonstock associations, provided for marketing agreements, and for penalties in the event of breach of contract. Other provisions relating to voting, ownership of stock, and distribution of patronage dividends were included. The department's bill found ready acceptance by numerous states during the years 1917-1921 after which the Sapiro model bill became better known. It also had its effect upon the wording of the Capper-Volstead Act of 1922.

**Capper-Volstead Act of 1922.** With the passage of the Capper-Volstead Act in 1922<sup>15</sup> the uncertainty of the capital stock associations was removed. This law was quite different from the Clayton Act in that it definitely authorized the association of agricultural producers. The Clayton Act was primarily designed to permit the organization of laborers for their mutual

<sup>15</sup> See *Nourse, op. cit.*, pp. 252-261 for an account of the passage of this act.

benefit, and merely included, as an afterthought, the nonstock, nonprofit associations of agricultural producers. The Clayton Act, however, is not repealed by the passage of the Capper-Volstead Act. The Capper-Volstead Act does not permit cooperative marketing associations to conduct their businesses as monopolies in restraint of trade which the Sherman act prohibits. The act permits the organization of producers of agricultural products to engage in interstate commerce and defines the method of organization of such association. Inasmuch as this act is exceedingly important its text is given in Appendix A.

Outstanding features of this act are: Each member is allowed one vote *or*, if voting is on a stock basis, dividends on stock can not exceed 8 per cent; nonmember business may not exceed in value that of members; the secretary of agriculture may determine whether the associations have unduly enhanced prices as a result of monopoly or restraint of trade; organizations with and without capital stock are permitted; marketing agreements are sanctioned; associations are restricted to agricultural producers; the associations are to operate for the benefit of their members; several associations may have marketing agencies in common; associations may or may not be incorporated. The act does not apply to purely cooperative purchasing associations or to consumers' cooperatives, nor does it provide for incorporation. Associations should incorporate under their state laws.

Certain clauses of this act define cooperative marketing more liberally than do many state laws. The nonprofit feature stressed by cooperative leaders as the chief identification of a cooperative is considerably weakened by permitting associations to pay as large a dividend on stock as they desire as long as the voting is on a one-man, one-vote basis. The fact that the business is not restricted to the member-producers but may come from nonmembers to the extent of being 50 per cent of the total value of all business further liberalizes the view of what really constitutes cooperation. The possibility of making net profits upon this nonmember business and of having such profits inure to the benefit of the members alone places the cooperative in somewhat the same category as that of commercial businesses.

The fact that associations, organized under the Capper-Volstead Act, are confined to "persons engaged in the production of

agricultural products, as farmers, planters, ranchmen, dairymen, nut or fruit growers" indicates that this restriction and classification was considered reasonable by Congress. The context of the act also intimates that cooperatives might become monopolies and unduly enhance prices to consumers. The belief evidently was held that prices would be enhanced somewhat, but if they became *unduly* enhanced then the Secretary of Agriculture and not the Federal Trade Commission or the Department of Justice is to step in to protect consumers. Although undefined in the act no doubt the term "unduly" will be interpreted largely on the basis of the disposition of the Secretary toward cooperative marketing in general and any association in particular. The fact that the Secretary of Agriculture rather than the Federal Trade Commission or the Department of Justice is charged with investigating any undue enhancement of prices indicates the sympathetic attitude of Congress towards the cooperative movement. There is, however, no clause in the act preventing the Federal Trade Commission from taking action against a cooperative in the regular course of its duties. Nor does the act permit the cooperatives to adopt methods of conducting business which are not permitted to other lawful associations.

#### SUPPLEMENTARY LAWS

In addition to the enabling legislation discussed above several other laws were passed by Congress which definitely influenced the development of cooperative marketing associations. These acts are considered as supplementing the enabling acts and likewise indicate a favorable public policy relating to the development of cooperative marketing agencies. In 1926 an act to create a Division of Cooperative Marketing in the Bureau of Agricultural Economics was passed. This division became one of the most constructive governmental bodies assisting cooperative marketing associations in the United States from 1926 to 1929. The division was authorized:

To acquire, analyze, and disseminate economic, statistical, and historical information about cooperative associations in the United States and foreign countries;

To study all phases of cooperation and publish results thereof;

To make surveys of accounts and other phases of cooperative practice for cooperative associations at their request;

To advise with committees of producers desirous of forming associations;

To acquire information of crop prospects, prices, market movements, and receipts and through marketing specialists to disseminate such information to cooperatives and others;

To promote the knowledge of cooperative principles and practices for the development of cooperation in this country. In short, the division became a national research and extension agency in cooperative marketing.

One other provision of this law, namely, Sec. 5, is significant. This section specifically permits associations of agricultural producers to exchange past, present, and prospective crop, market, statistical, economic, and other similar information. Such exchange may be directly between associations or through a common agent created for such purpose by them. Some critics contend that this provision grants cooperatives privileges which the Sherman act forbids private institutions, while others claim in defense that this proviso is no more liberal than rights conceded to trade associations and is in fact designed to make cooperatives more efficient marketing units with more intelligent bases for pricing farm products, all of which inures to the benefit of the producers directly and to society in general.<sup>16</sup> In a very practical manner this provision in 1926 permitted cooperatives to do what the NIRA of 1933 in its code agreements wanted all American industry to do. In 1929 the division was taken over by the Federal Farm Board, and since 1933, it has been a research and service division of the Farm Credit Administration.

On Feb. 24, 1925, the President approved the so-called Purnell Bill which appropriated \$20,000 for the fiscal year ending June 30, 1926 (increased by \$10,000 each year until the sum of \$60,000 was reached), to each agricultural experiment station for the

<sup>16</sup> In the cases *Maple Flooring Manufacturers' Association v. United States*, 268 U. S. 563 and in *Cement Manufacturers' Protective Association v. United States*, 268 U. S. 588, the Supreme Court held that those industries engaged in the same line of business may, through their trade associations, exchange information regarding stocks on hand, prices being charged, and orders remaining unfilled. No authority was given, however, for agreement on price schedules. Cases of this kind fall in the twilight zone of permitted joint action which has been allowed under certain conditions to trade associations. See also *Sugar Institute v. United States* 297 U. S. 553 (1936), for the most recent decision relating to this subject.



purpose of "making experiments bearing directly on the production, manufacture, preparation, use, distribution, and *marketing* of agricultural products . . . and such economic and sociological investigations as have for their purpose the development and improvement of the rural home and rural life . . ." Many experiment stations began research studies in the field of cooperative marketing and purchasing and on the basis of such research took a more active part in extension activities on behalf of cooperation.

Another act which was passed in 1927 prevented the discrimination against farm cooperative associations by boards of trade. The grain cooperatives, which became rather large, desired membership in some of the grain exchanges, but were denied on the grounds that they paid a patronage refund ("rebate" as the boards of trade call it) to their members, a practice which regular members did not follow. In essence, however, this was merely a discrimination against the associations. The act which prevents such discrimination includes the following important section.

Section 2. No board of trade whose members are engaged in the business of buying or selling agricultural products or receiving the same for sale on consignment in interstate commerce shall exclude from membership in, and all privileges on, such board of trade, any duly authorized representative of any lawfully formed and conducted cooperative association, corporate or otherwise, composed substantially of producers of agricultural products, or any such representative of any organization acting for a group of such associations, if such association or organization has adequate financial responsibility and complies or agrees to comply with such terms and conditions as are or may be imposed lawfully on other members of such board: Provided, That no rule of a board of trade shall forbid or be construed to forbid the return on a patronage basis by such cooperative association or organization to its bona fide members of moneys collected in excess of the expense of conducting the business of such association.

In the Grain Futures Act, 1922, Congress included in Sec. 5 the following antidiscrimination clause.

The Secretary of Agriculture is hereby authorized and directed to designate any board of trade as a "contract market" when, and only when, such board of trade complies with and carries out the following conditions and requirements. [Provisions *a*, *b*, *c*, and *d* are omitted here.]

e. When the governing board thereof does not exclude from membership in, and all privileges on, such board of trade, any duly authorized representative of any lawfully formed and conducted cooperative association of producers having adequate financial responsibility which is engaged in cash grain business, if such association has complied, and agrees to comply, with such terms and conditions as are or may be imposed lawfully on other members of such board: Provided, That no rule of a contract market shall forbid or be construed to forbid the return on a patronage basis by such cooperative association to its bona fide members of moneys collected in excess of the expense of conducting the business of such association.<sup>17</sup>

In 1932 the Secretary of Agriculture was called upon to invoke this provision of the act as the following case shows.

On Apr. 12, 1932, the Farmers' National Grain Corporation asked the Secretary of Agriculture to take action against the Chicago Board of Trade for denying full trading privileges to the corporation and its subsidiary, the Updike Grain Company. Some months later the federal grain futures commission issued a suspension order, to which the Board of Trade filed an appeal. The appeal was based on the contention that the Farmers' National Grain Corporation was not a lawfully organized and conducted cooperative, that it did not have adequate financial responsibility, and did not comply with terms and conditions imposed upon other members. On Oct. 31, 1933, the Circuit Court of Appeals of the Seventh District set aside the suspension order.

Measures to prevent the discrimination of any corporation against the cooperatives have also been enacted in some of the state cooperative laws. In the Wisconsin law this antidiscrimination clause reads, "Whenever any corporation shall have discriminated against any cooperative association transacting business in this state, its charter may be vacated or its existence annulled, if it is a domestic corporation; or, if it is a foreign corporation, its license to transact business in Wisconsin may be revoked. . . ." Soon after the passage of this clause suit was

<sup>17</sup> This section in the 1936 Commodity Exchange Act is changed only to the extent of substituting the word "commodity" for "grain." Section 6a (1) and (2), a new section in the Commodity Exchange Act not found in the Grain Futures Act, further elaborates upon the rights of cooperative associations that have membership in commodity exchanges.

brought against a Milwaukee dairy that discriminated in price against a producers' bargaining association. In the Wisconsin criminal law there is also an anti-slander provision which makes it unlawful for any person to "wilfully and maliciously make, circulate, or transmit to another or others, any false statement, rumor or suggestion, written, printed, or by word of mouth, which is directly, or by inference, derogatory to the financial condition or affects the solvency of . . . cooperative associations." In this respect cooperatives are placed in the same category as banks, building and loan companies, and investment companies.

Important in the history of cooperative marketing was the Agricultural Marketing Act of 1929. This act was primarily an agricultural relief measure adopted by a Republican administration during the spring of 1929. It propagandized the cooperative movement in this country as perhaps no other federal law has ever done. The first paragraph stated the declaration of policy of Congress in the following terms:

Section 1. (a) That it is hereby declared to be the policy of Congress to promote the effective merchandising of agricultural commodities in interstate and foreign commerce, so that the industry of agriculture will be placed on a basis of economic equality with other industries, and to that end to protect, control, and stabilize the currents of interstate and foreign commerce in the marketing of agricultural commodities and their food products—

(1) by minimizing speculation.

(2) by preventing inefficient and wasteful methods of distribution.

(3) by encouraging the organization of producers into effective associations or corporations under their own control for greater unity of effort in marketing and by promoting the establishment and financing of a farm marketing system of producer-owned and producer-controlled cooperative associations and other agencies.

(4) by aiding in preventing and controlling surpluses in any agricultural commodity, through orderly production and distribution, so as to maintain advantageous domestic markets and prevent such surpluses from causing undue and excessive fluctuations or depressions in prices for the commodity.

The principal features of this act were the following: It provided for the creation of a Federal Farm Board of eight members, of which the Secretary of Agriculture was ex-officio member. It

called for the appointment of advisory commodity committees which were to advise with the board members concerning the marketing of their respective commodities; it provided a revolving fund of 500 million dollars from which loans were to be made to cooperative associations (1) for merchandising purposes, (2) for the construction of facilities, (3) for the formation of clearing-houses, (4) for increasing the amount of cash advances to producers—so-called “commodity loans,” (5) for extending the membership of the cooperative associations; it provided for the establishment of stabilization corporations to handle whatever surpluses of agricultural commodities may exist; it also provided for price insurance to cooperatives and it established producer controlled clearinghouses.

The commission was primarily a planning commission and not a regulatory, fact-finding, or an investigatory one. With a very active personnel on the Federal Farm Board during its early years, it did a great deal to promote the development of cooperative marketing in the United States. Never before had this movement received such direct governmental sanction.

In other pages of this text, mention was made of the board's activity in the establishment of national cooperative marketing associations, of the coordination of marketing activities of competitive cooperative associations, of the great extent of cooperative financing which the board undertook, and of the crucial problems which were met in the operation of stabilization corporations for wheat and cotton. There is no doubt about the fact that the Federal Farm Board left its mark upon the progress of cooperative marketing in the United States.

With the incoming Democratic administration in 1933 and following the passage of the Agricultural Adjustment Act, most of the important functions of the Federal Farm Board were taken over by the Farm Credit Administration. Much of the direct, concerted assistance to cooperative marketing associations by federal authorities was discontinued. In its place the Cooperative Division of the Farm Credit Administration is functioning as a research and service agency.

#### COMPLEMENTARY LAWS

In addition to these supplementary acts, a number of laws have been passed by Congress which assist cooperative marketing

associations in their operations. These may be termed "complementary laws." In 1916 the United States Warehouse Act was passed which became instrumental in assisting cooperative associations with their financing activities. Cooperatives were now in a position to store agricultural commodities in federally licensed warehouses, obtain warehouse receipts for them, and use these receipts as collateral with financial institutions. This made it possible to advance a substantial amount upon the products delivered by the producers months before they were sold.

The negotiability of the warehouse receipts and their general acceptance by the leading bankers of this country made it possible for the large-scale associations to tap the large banks in the key cities for the huge funds which were needed to make the advance payments.

During the depression of 1921, the act creating the War Finance Corporation proved to be of inestimable value to cooperative associations. Its huge revolving fund was particularly instrumental in financing large-scale cooperative cotton and tobacco marketing associations. The importance of the War Finance Corporation is discussed in the chapter on Financing.

Likewise the Intermediate Credit Act of 1923, which provided for the establishment of 12 intermediate credit banks, proved to be of great value to the large-scale cooperative associations of this country in their financing activities. For the first time, credit of a longer duration than the usual short-time commercial credit was made available to farmer cooperative companies. The storing of farm products for several months and the desirability of making advance payments to producers, immediately upon delivery of their products, created a real need for the type of credit which the intermediate credit banks were in a position to extend.

The Revenue Act of 1926 contained a provision (Sec. 231) which was a boon to cooperative associations. This provision exempted cooperative associations from the taxation of their net incomes. While it was held in theory that cooperative associations were nonprofit, yet many tax collectors who examined their financial statements, and who were not particularly versed in the objectives and modes of operation of cooperatives, construed these associations as actually earning net incomes which were taxable. Consequently, a specific ruling by Congress which

would exempt cooperative organizations was necessary. Under the Internal Revenue Act of 1934, cooperative associations exempted from paying federal income taxes are also eligible for exemption from paying capital stock and excess profit taxes. Associations must communicate with the collector of internal revenue for the district in which the cooperative is located if exemption from the payment of capital stock, excess profits, and income taxes is desired. Briefly, the 1934 act required the following conditions before exemption would be granted:

1. Practically all of the voting stock or voting memberships must be held by farmers and by those producers who patronize the association.

2. The association must be organized and operated on a cooperative basis for the purpose of marketing farm products or purchasing farm supplies. The total sales value less the necessary marketing expenses must be returned to producers. In purchasing associations supplies are to be sold at cost plus necessary expenses.

3. Both members and nonmembers of marketing and purchasing associations must receive equal treatment with respect to patronage dividends. The patronage dividend for a non-member may be held by the association to apply on the purchase of a share of stock or membership.

4. Reserves or surpluses that are retained must be in conformity with the law of the state in which the association is incorporated, or such reserves must be reasonable and for necessary purposes.

5. Dividends on capital stock must not exceed 8 per cent or the legal interest rate of the state of incorporation, whichever is greater.

6. At least 50 per cent in value of the marketing and supply business must be transacted with members. Not over 15 per cent of the purchasing business may be with persons who are neither producers nor members.

In any event an association should communicate annually with the collector of internal revenue of the district in which the association is located and secure the necessary forms for exemption. Exemption is not automatic even if it was once granted. Proper claim and application must be made for it,

## PUBLIC AUDITS

A feature commonly found in enabling legislation in foreign countries is a provision requiring the cooperatives to have their accounts regularly audited by some public auditor. This provision is singularly absent from federal and state legislation (except in Minnesota) in the United States. The requirement that an annual report be prepared and submitted to some administrative officer of the state is not nearly so rigid a requirement as the necessity of submission to an annual audit by an appointed officer of the state. Most cooperatives, particularly the larger ones, have their accounts audited either by state accountants, private auditing firms, or by auditors provided by cooperative associations. Thus, the state Farm Bureau Federations, the Farmers Union, and the Central Cooperative Wholesale of Superior, Wisconsin, provide an auditing service for their affiliates. This voluntary audit serves the same purpose as does a compulsory audit. However, in associations in which no audit is made, much may be gained, no doubt, if an annual critical review of the business would be made by a sympathetic and constructive auditor.

## EARLY ATTITUDE OF THE COURTS—VIOLATION OF ANTITRUST LAWS

It has already been stated in the earlier part of this chapter that the common law considered all combinations as restraining trade and competition and that some courts considered the early cooperative associations as falling under the dictum of the common law. The passage of the state cooperative marketing laws indicated, however, a change of public policy toward cooperative marketing associations. But these laws were not passed by most of the states until after the passage of the Sherman Antitrust Act of 1890. Numerous states also adopted provisions in their state antitrust laws which exempted farmer cooperative marketing associations from the same. Courts, therefore, were obliged to pass upon the constitutionality of the state cooperative marketing acts, as well as upon the provisions exempting the associations from the antitrust laws. In other words, courts were called upon to decide two important questions: (1) are cooperatives organizations in restraint of trade violating the

common law rules regarding monopoly or the Sherman Antitrust Act; and (2) if they are, have the state legislatures the power to exempt them from these laws in view of the principles enunciated in the 14th Amendment?

Early decisions of the courts held that cooperative associations were in violation of the antitrust laws and that their exemption constituted a type of class legislation not amenable to the 14th Amendment to the Federal Constitution.

In 1895 the Illinois Supreme Court held that the Chicago Milk Shippers Association was an illegal corporation because it fixed the price of milk and controlled the production of the same, and in a Texas case in 1897, the court held that the anti-trust law of the state of Texas was unconstitutional for its exemption of cooperative corporations. In another case in 1902 the Supreme Court of the United States ruled that the Illinois law was unconstitutional because it included a clause which exempted farmers and truckmen from its provisions. But perhaps the most outstanding illustration of the court's interpretations of undue restraint of competition was the Iowa case of *Reeves v. Decorah Farmers' Cooperative Society*.<sup>18</sup>

Three hundred and fifty hog producers at Decorah, Iowa, organized a cooperative association for the marketing of their hogs in 1911 under the general corporation laws of Iowa (no cooperative law had been enacted.) For two years the cooperative was fairly successful. The purpose of the association was not to accumulate a large surplus and pay dividends, but simply to establish a market at Decorah where the farmers would receive all that their hogs were worth at the local loading point.

In this community there was also a local hog buyer named Reeves, who bought hogs to be consigned to the Chicago market. He brought suit against the association, charging that the group of farmers through their association made it necessary for him to pay more than the market price for hogs in that locality. A provision of the bylaws of the association stated that in the event any member sold hogs to anyone outside of the association, a "maintenance fee" of 5 cents per hundredweight should be paid to the association as liquidated damages. Reeves held that the

<sup>18</sup> The reader is advised to peruse the case in 160 Iowa 194, or 140 N.W. 844 (1913). A good analysis of the facts, rulings, and interpretations of this case is made by Nourse, *op. cit.*, pp. 337-343.



association was in restraint of trade, was a monopoly, and suppressed competition.

The Supreme Court of Iowa upheld a permanent injunction against this little group of producers on the ground that Reeves was placed at a disadvantage and could not compete with the society in purchasing hogs from its members and that the members were not free to deal with the plaintiff or anyone else. The court continued by saying that if the members dealt with Reeves, he either forfeited his profits by reason of having to pay too much for his hogs, or they forfeited a part of their purchase price as a penalty for selling outside of the association.

Since the time of the Reeves case (1913), the Iowa Supreme Court has decided similar cases with antithetical verdict and opinion.<sup>19</sup> Considered in the light of present public policy a decision such as was handed down in the Reeves case would be improbable. In Colorado, however, as late as 1925 the court held that marketing contracts entered into prior to 1923, when the state cooperative law was passed, were in restraint of trade.

#### LATER ATTITUDE OF THE COURTS—COOPERATIVES NOT MONOPOLIES

The attitude of the courts toward the cooperatives soon became changed when the public policy toward these institutions was expressed in the enabling acts passed by many state legislatures. The state cooperative laws, Sec. 6 of the Clayton Act, and the Capper-Volstead Act which exempted producers' associations from the provisions of the antitrust laws were no doubt powerful influences in bringing about general approval of cooperative associations by the courts. The legislatures expressed their policies in no uncertain terms as the following quotation from the Bingham Cooperative Marketing Act, Acts of Kentucky 1922, indicates.

Any association organized hereunder shall be deemed not to be a conspiracy nor a combination in restraint of trade nor an illegal monopoly; nor an attempt to lessen competition or to fix prices arbitrarily or to create a combination or pool in violation of any law of this State; and the marketing contracts and agreements between the association and

<sup>19</sup> *Clear Lake Cooperative Livestock Shippers' Association v. Weir* (Iowa, 1925) 200 Iowa 1293; 206 N.W. 297.

its members and any agreements authorized in this act shall be considered not to be illegal nor in restraint of trade nor contrary to the provisions of any statute enacted against pooling or combinations.

The fact that the cooperative laws were passed at a later date than the antitrust laws indicated that it was the intention of the legislatures that the antitrust laws were not to apply to farmers' cooperative associations. No longer was the common-law dictum applied indiscriminately to the associations, nor was the operation of the cooperatives considered as in restraint of trade and competition. The courts assumed an entirely different attitude and took judicial notice of the economic considerations of agriculture.

Among the economic bases for decisions that were made by the courts the following appeared to be uppermost:

1. Cooperatives do not control agricultural production and hence do not have a strict monopoly of the product which they market.

2. Cooperatives do not fix prices according to the usual interpretation of that concept, nor do they control the market, but simply sell the products for the best price obtainable in markets that are open to other businesses, as well as to the cooperative.

3. The agricultural depression of 1921 brought to the attention of the courts the plight in which American farmers found themselves and brought to the fore the wide margins between prices received by farmers and those paid by consumers. Improved marketing, which was the aim of the cooperative associations, was not only laudable but distinctly advisable, not only from the standpoint of the farmer's direct benefit, but from that of social welfare.

4. The operation of cooperatives did not result in increasing the cost of farm commodities to consumers. On the contrary careful grading and standardizing of products, the general improvement in the quality and the pack of farm goods, and the regularity with which they were sent to the markets of the country were distinctly advantageous to consumers.

5. Knowledge of the conditions against which farmers had to struggle in the market place where the financially weak, small-scale producer was pitted against the much better informed and financially more powerful middleman. Cooperation was simply a means of organizing the small-scale sellers on one side against

the established organized buyers on the other—a fair objective under any circumstances.

6. The importance of agricultural prosperity in a nation of interrelated industrial and agricultural activities was considered essential to public welfare; therefore, the cooperative association which aimed to improve the lot of farmers was not only approved but encouraged by statesmen, businessmen, bankers, and the public in general.

In addition to the economic basis for the change in the decision of the courts, there were certain ethical considerations involved. In some of the court decisions there is the suggestion that the court realized the injustice which farmers had to bear as a result of the craftiness and greater expertness of private tradesmen. Consequently, some courts looked upon the development of cooperatives as a means of obtaining justice for the producers and as an important step in the direction of obtaining just returns for farmers. The courts also recognized that membership was a voluntary undertaking of producers, and, contrary to earlier court decisions, cooperatives were not considered monopolistic in character.

An association, of course, cannot engage in acts illegal and forbidden to private businesses. The law simply declares that an association of producers organized for marketing purposes is not a monopoly; but that does not mean that associations may not be guilty of monopolistic action. Nor does it absolve cooperatives from illegal acts which they may commit. Section 2 of the Capper-Volstead Act definitely prescribes what action the Secretary of Agriculture should take if he has reason to believe that any association monopolizes or restrains trade in interstate and foreign commerce. In fact in several cases, notably in the California Associated Raisin case (1920), courts held certain practices as illegal and monopolistic in character.

#### THE CHARGE OF CLASS LEGISLATION

In the decision of the courts it was apparent that judges in earlier years held that the laws exempting farmers' cooperative associations from the antitrust acts of the states were a type of "vicious" class legislation not amenable to the Fourteenth Amendment to the constitution. In some of the first cases, such as *Connolly v. Union Sewer Pipe Company* (1902) and in the

Grice case in Texas (1897), the courts held such laws to be unconstitutional on the grounds of class legislation.

Later, however, the courts recognized a real distinction, namely, that production in agriculture was not so controllable as production in industry and that there are inherent difficulties involved in the production of farm products with which industry did not have to contend. It was correctly held that there was sufficient difference in the problems facing agricultural producers from those confronting the producers of industrial products to warrant the classification which would exempt the former class from the antitrust laws of the state and not the latter. Inasmuch as the classification of agricultural producers in cooperative marketing associations was considered a *general* classification and not a special one pertaining to a relatively small class in society, the exemption was considered not in violation of the Fourteenth Amendment. It was felt that the organization of agricultural producers did not constitute an act prejudicial to the interests of society in general, because of the distinctive characteristics of agriculture per se and because of the laudable purposes for which the associations were organized.

In various states of the Union classifications of one kind or another have been made which have exempted one group in society from certain laws, but not other groups. For example, in Pennsylvania it was considered proper to tax anthracite coal operators, but not the bituminous ones; in Louisiana it was considered legal to tax the refiners of sugar, but not the planters and farmers who ground their own. The Capper-Volstead Act exempts the cooperative associations engaged in interstate commerce from the federal antitrust law for the same reasons that the state laws exempt the associations involved in intrastate commerce from the respective state antitrust laws.

#### THE SEMIPUBLIC ASPECT OF AGRICULTURAL COOPERATION

From the beginnings of cooperative marketing in this country, there has developed a general feeling that the public has a direct interest in the organizations even though it does not contribute products to the cooperative for sale and seldom invests in the capital used by the cooperatives. In the Standard Cooperative Marketing Act, one of the provisions required that the Dean of the College of Agriculture of the state of Kentucky was to make

a preliminary survey and advise with the leaders of prospective cooperative marketing associations before any companies could be set up. It also provided in another section that the cooperative was to prepare an annual report and file the same with the Dean of the College of Agriculture. In 14 states the cooperatives must file annual reports with some department of government. In a number of states the cooperative law permits one director of the corporation to represent the state at large. Thus, in Arkansas the Director of Extension is the director at large, representing the public on the board of the Mid-South Cotton Growers Association.

In three countries, namely, Russia, Italy, and Germany, the cooperative movement has lost its independent voluntary character and has been brought under the surveillance of the state. In October, 1917, with the advent of the Bolshevik party "The cooperative movement was brought into subjection as an instrument of the Dictatorship of the Proletariat," from which it has not become entirely free and autonomous in the Soviet State. In Germany the cooperative movement has suffered a severe setback since May, 1933, when

. . . the National Socialist authorities, on the pretext that the societies were mixed up with political activities, but more particularly in the interests of private trading enterprise and in pursuance of the antidemocratic policy of the new regime, entered forcibly into control of the cooperative movement as they had already done in the case of the provincial and municipal government. The results to the movement in Germany have been, perhaps, more disastrous than in any other land where the dictatorship has entered control. . . . Unless wiser counsels prevail, as they well may, the German Cooperative Movement seems doomed to extinction, or at least to absorption into the general capitalist economy.<sup>30</sup>

In Italy, the two principles governing cooperation as decreed by Premier Mussolini in 1925 are:

1. The unity of the Movement in the sense that Fascist Cooperation, naturally unitary, aims at creating an organization, the voluntary character of which does not exclude efficient coordination.

<sup>30</sup> MAY, HENRY J., *The Orientation of the International Cooperative Movement*, in the *Review of International Cooperation* (London) 28th year, no. 7, p. 245, July, 1935.

2. The supremacy of the State [is to be recognized] in the sense that the State must intervene to regulate and to supervise the development of Cooperation.<sup>21</sup>

Cotta ascribes this need for state regulation to the frightful position to which the cooperative movement had fallen.

Incompetence, speculation and parasitism, then, vitiated and corrupted Italian cooperation.<sup>22</sup> . . . In Italy, before the advent of Fascism, in a small village of 5,000 inhabitants there were to be found three or four societies all competing with one another. Instead of one, there were three distinct federations with warring party allegiances, distinct policies, and clashing objectives.<sup>23</sup>

Cooperatives were aligned with three different political parties before Mussolini decreed that all cooperatives were to come under the Fascist regime.

The control of the state is apparent as Hobson states when associations are placed "under the minister of national economy who has the power, not only to inspect, but to dissolve their managing boards and to appoint representatives of his own to run the organizations." This in its final analysis means, of course, complete control and the abolition of volition. Politics and cooperation do not harmonize well. Hence, one principle of the consumer cooperators, namely, that of "Political and Religious Neutrality," is receiving a severe test in Italy. This relationship of the state to cooperatives in general has been ably put in the following terms.

The cooperative system is one which is generally deemed to require and deserve special consideration from the State. It is a method of increasing prosperity which is open to those with little capital, and therefore tends to a rapid increase of social wealth; it is of mutual advantage to all those engaged in it; it provides greater security than the individual enterprise; it can reach a socially more beneficial standard in the conduct of its business, owing to the fact that it is not immediately bound to the realization of profits as distinct from the creation of

<sup>21</sup> COTTA, FREPPEL, "Agricultural Cooperation in Fascist Italy," p. 7, P. S. King & Son, Ltd., London, 1935. See also WALTER, KARL, "Cooperation in Changing Italy," P. S. King & Son, Ltd., London, 1934, for a description of cooperation in Italy.

<sup>22</sup> COTTA, *op. cit.*, p. 2.

<sup>23</sup> COTTA, *op. cit.*, p. 1.

wealth; finally, particularly as concerns agriculture, it is a useful channel for the educational influence of the government on the agriculturist.<sup>24</sup>

All of this does not imply that the state through its administrative officers should run the cooperatives, appoint managers and directors, assume financial risks, and remove the necessity of efficiency for survival. Such paternalism would have a deadening influence on the association—it would be no stronger than the intelligence of the officers of the state who may have little experience in marketing. The relationship of the state which is sought is a sympathetic, affirmative approval of the self-governing cooperative type of business—not a paternalistic, “wet-nurse” relationship.

#### VALUE OF INCORPORATION

It is not necessary for cooperative associations to be incorporated, although it is generally advisable that they be so. An unincorporated association, in the eyes of the law, is comparable to a partnership arrangement in which each member is fully liable for the approved acts of the partnership. Incorporated organizations have a distinct legal status. The liability of individual members is usually limited to the amount invested in the organization if it is incorporated. Officers and directors, however, are liable to the corporation for all damages suffered by it as a result of exceeding the limit of indebtedness fixed by the statute, charter, or bylaws. The general rule is that each member of an unincorporated association is liable for the debts and obligations thereof incurred during his period of membership and which were contracted for the purpose of carrying out the approved acts of the association. The incorporated association may sue and be sued in its corporate name, whereas a noncorporate association would have to sue or be sued in the names of its individual members. Without exception all large-scale associations and those that operate in the central market places are incorporated. Most of the local associations having sizable capital investments are incorporated, but those without such are not incorporated. Hence, the majority of farmers' elevators, creameries, and local supply companies are incorporated, but

<sup>24</sup> DIGBY, MARGARET, “Yearbook of Agricultural Cooperation,” p. XIX, The Horace Plunkett Foundation, P. S. King & Son, Ltd., London, 1933.

the bulk of the cooperative cheese factories and livestock shipping associations are not.

Before incorporating an association, the laws of the state, in which it is planned to incorporate, should be carefully examined so that the steps taken may be in accordance with the state law. Usually it is advisable to confer with the Secretary of State and obtain from him the necessary papers. If an association is to operate on a national basis, then it is advisable to incorporate in a state that permits meetings of directors and of members to be held in other states and that grants associations the right to sell stock to associations incorporated in other states. For this reason many national associations are incorporated under the laws of the state of Delaware.

#### LIABILITY OF MEMBERS

The financial liability of members in incorporated associations is limited to the amount of capital stock held by the individual members. In unincorporated associations, the liability is shared jointly and severally and is unlimited. Danish cooperatives are not incorporated, but such a condition is wholly unsuited to America. In nonstock cooperatives, the liability of members is determined by the terms of the membership contract, the bylaws of the organization, and the statutes of the state in which the association is incorporated. Members in nonstock cooperatives cannot be assessed to pay expenses which were not incurred in accordance with the powers granted the association by the membership contract.

Members are liable, however, for any overpayments made to them in their advance payments. It is the custom of cooperatives to make advances to producers at the time of delivery of the product to a pool, such advances being based on the assumption that the sale of the products will cover all expenses of marketing and the amount of the advance. In the event of a decline in prices or a miscalculation of costs or prices, if the advance exceeds the net amount realized on the sale, then the association may recover the difference. If, however, after a final settlement has been made with the producer, it is discovered that an error was made in such settlement so that the producer received more than the net returns from the sale, the producer cannot be held for



such excess final payment. The reason the courts have granted the association remedy against the producer receiving excess advance payments rests on the grounds that a cooperative is a nonprofit, mutually helpful association in which one group of members should not profit at the expense of others. An excessive advance, if not recovered, becomes an extra cost to the association and a financial burden to the members who did not receive the excess. In the event products are bought at a cash price from the producer below the resale price, then the association has no recourse against the producer.

In capital stock associations the property rights of members are based upon the number of shares of stock owned. If associations are organized without capital stock, the articles of incorporation usually state whether the property rights of members shall be equal or unequal and, if unequal, the rule by which their rights shall be determined. Many unincorporated associations without capital stock have failed to indicate the manner in which the property rights are to be determined; as a result, many banks throughout the United States are depositories of funds belonging to associations that have ceased operating and whose officers do not know either legal or equitable ways of distributing the remaining assets. Provision shall also be made in the articles of incorporation for the admission of new members and the basis upon which they shall be entitled to share in the property of the association with the old members.

In nonstock organizations, membership is not transferable or assignable. In capital stock organizations members may sell their stock to anyone if no provisions are stated to the contrary in the bylaws of the association or on the face of the stock certificates. However, if the association wishes to prevent the stock from falling into hands of persons who are not producers it is necessary to define in the organization papers who may hold stock and how it may be transferred. Preferably its transfer should be permitted only with the consent of the board of directors. The association should have the first right of purchase of any stock offered for sale. Likewise, it is well to include in the bylaws a clause to the effect that any stockholder who ceases to be a producer also forfeits his voting rights in the association. These restrictions should be printed on the face of the stock certificate, or on a separate memorandum signed by the

producer, and incorporated in the articles of incorporation and bylaws.

#### THE LAW FOR CONSUMER COOPERATIVES

The Capper-Volstead Act relates entirely to farmers' cooperative marketing and distributing associations and does not apply to strictly purchasing associations or to cooperative stores. In order that consumers' cooperatives may obtain the same legal status under federal laws as sales associations have received, it will be necessary for Congress to enact permissive legislation to that effect. Many of the state cooperative laws, however, in their declaration of policy, include farmers' purchasing associations with the selling organizations. Both federal and state courts have upheld the right of individuals to purchase collectively commodities which they require in their separate undertakings. Such collective buying is carried on to effect economies for the purchasers rather than to restrain competition. In a Department of Labor publication,<sup>25</sup> it was stated that in 1930 there were consumers' cooperative laws of varying degrees of completeness on the statute books of thirty-four states and Alaska, some of which were very brief and others specific as to the operation of associations incorporated under them. These laws, however, are the same cooperative laws which were enacted to legalize the distributing associations and no state has passed an enabling act relating only to the cooperative purchasing associations.<sup>26</sup>

Farmers' cooperative purchasing associations are also exempted from the payment of federal income taxes if they meet the specifications set by the law for such exemption. Likewise the Cooperative Marketing Act of 1926, which created the division of Cooperative Marketing, authorized that research cover farmers'

<sup>25</sup> PARKER, FLORENCE E., Consumers', Credit, and Productive Cooperative Societies 1929, U. S. Dept. Labor, Bureau of Labor Statistics, *Bul.* 531, p. 83, 1931.

<sup>26</sup> All of the cooperative statutes of the individual states and Alaska are given in a recent publication, "Consumers' Cooperative Statutes and Decisions," The Consumers' Project, U. S. Department of Labor, Washington, D. C., 1937. "In this volume will be found the acts of the various legislatures of continental United States which are intended to facilitate the organization of consumers' cooperatives. In addition to the statutes this volume includes summaries of cases, both Federal and State, in which the consumers' cooperative statutes have come before the courts for application and interpretation."

purchasing associations and that assistance be given these companies. The Farm Credit Act of 1933 and of 1935 included features that make it possible for farmers' purchasing associations to obtain loans from the Federal Intermediate Credit Banks and from the Banks for Cooperatives. The acts preventing boards of trade from discriminating against cooperative associations relate only to producers' associations and not to consumers' companies.

#### Questions

1. What was the status of cooperative associations under the common law?
2. Why were cooperative leaders anxious to have the states pass enabling legislation for cooperative associations? Why did not the general corporation laws suffice?
3. What were some of the principal provisions of the Standard Cooperative Marketing Act?
4. Why was there such an urgent demand for laws legalizing nonstock associations?
5. Cite the principal provisions of the Capper-Volstead Act.
6. What supplementary legislation has been enacted for the benefit of cooperative marketing associations in the United States?
7. What conditions must be met before a cooperative becomes exempt from the payment of federal income taxes?
8. What was the early attitude of the courts toward cooperative associations and the reasons for this attitude? What caused the courts to change from this early opinion?
9. Do you think that state laws should require a public director with full voting power on the board of directors of all large-scale cooperative associations? Give the pro and con arguments.
10. Should all associations, local and regional, be incorporated? Why?

## XII

### *Membership Contracts*

*A large percentage of America's large-scale sales associations have written contracts with their members by which the members agree to market their farm products through the cooperative association during a specified period of time stated in the contract. A contract, in brief, is simply a statement in writing of the rights and duties of the members and the association relating to the products produced and marketed by the member. Many local marketing associations do not use contracts; neither do cooperative purchasing companies.*

*Contracts vary in length of time from a 3-month period to a 20-year period. Most contracts today are of the self-renewing kind with annual withdrawal privileges. Ordinarily, signing a contract is one condition of membership in many associations. Generally, contracts do not become effective until a certain volume of the crop or a certain number of producers have signed the contracts.*

*A contract has both an economic and a legal value. The greatest value from the use of a contract is obtained in the first few years of an association's operations. A contract is no stronger than the will of the majority of the membership—it is a valuable tool but not an indispensable one. The agency and the purchase and sale types of contract have been tested before the courts of the country and have received general approval.*

*In the event that the member violates his contract, the association may obtain redress by obtaining liquidated damages, an injunction, and a decree of specific performance.*



## CHAPTER XII

### MEMBERSHIP CONTRACTS

A large percentage of cooperative marketing associations use membership contracts as an integral part of their system of organization. Of 120 federated, centralized, and local associations operating throughout the United States, the authors found that 72 per cent used contracts in 1934-1935. Very few, if any, of the centralized types of associations and of the federated sales associations do without contracts. It is chiefly among the local cooperatives such as creameries, cheese factories, elevators, and livestock shipping associations where their use is not common.

A contract may be defined in legalistic terms but for general purposes it may be described for a cooperative association as a written statement of the rights and duties of the members and of the association relating to the marketing of the products of the producer through the association. The producer agrees to deliver all of his products to the association for a given period of time, permits the association to pool the products with those of other members, agrees to the deduction of marketing costs, and assents to certain methods of enforcement of the contract, or payment of damages in the event of breach. The association in turn agrees to market the products to the best advantage and pay for the same on the basis of the prices received for the goods. If the contract will be considered as a voluntary agreement between the producer and his association in which the rights and duties of each are explicitly listed, much of the value of using a contract becomes apparent.

The terms of a contract should be specific and clearly stated. It is not well to take things for granted. The contract that is carefully drawn will state whether the association shall have the right to pool products, whether it has the right to pledge the members' products as collateral for loans, how much will be deducted from the sale price of the commodities to cover costs

of operation (only specifically authorized deductions can be legally made), and such other conditions as will definitely inform the members and the association of their exact rights and duties.

The terms "marketing agreement" and "marketing contract" or "membership contract" are synonymous. The term "membership agreement" is sometimes used interchangeably with the term "membership contract." There is, however, a distinction between the two. The former term may specify the conditions of membership without stipulating the manner in which a member's products are to be handled. A membership agreement is oftentimes signed by farmers whereby they agree to become members of an association, sign the necessary marketing contracts, and comply with all other terms of membership provided a sufficient number of other farmers agree to do likewise. For example, one of the conditions of membership which became a basis of the validity of the membership contract in the Northern Wisconsin Cooperative Tobacco Pool in 1922 was the requirement that "growers of 75 per cent of the tobacco produced in Wisconsin in 1920 sign similar contracts."

Although this chapter will deal with the contract between producers and their marketing associations, it should be pointed out, moreover, that contracts are also drawn up between local associations and central sales organizations. Another contract is drawn between the central sales association and a national marketing association if the central is a member of the latter. These contracts differ in their wording from the producer contracts and are specially drawn up for the purposes they serve. Cooperative purchasing associations seldom use membership contracts requiring their members to buy exclusively through their associations. Certainly, detection of violation would be more difficult than in marketing associations, but there may also be a feeling that the advantages of a well-managed association will assure the continued support of the membership without need of a contract.

In the eyes of the law, producers' marketing contracts are considered on the same basis as any other contract recognized by law. There are no special considerations, rights and duties, powers and exposures which clothe these contracts that do not surround ordinary commercial contracts.

**PURPOSE OF CONTRACT**

Marketing contracts have (1) an economic and (2) a legal significance. Under the economic value of the contract we note the following important considerations.

1. A contract is used to assure the association the continuous support of its members. In the ordinary private business corporation the stockholders expect to profit from efficient and skillful management of the business. Reserves are laid aside to meet particular emergencies and to offset losses sustained during unprofitable years. Profits can therefore be paid out of reserves in certain years. Such is not a common practice in cooperatives. Each year's business is considered separately—earnings of one year are not prorated on subsequent years' business. Hence, each member's regular support is as vital to the success of the cooperative as the sale of the products by the management. Each member must do his particular part to assure the success for all. The cooperative, therefore, is entirely dependent upon deliveries by its members for its continuance. Any business done outside the cooperative is inevitably in competition with it. It becomes apparent that in order to assure the continuous support of each member, a contract is essential. A contract eliminates the opportunists who merely use the cooperative as a means of inveigling higher prices from private buyers but who care little for really improving the marketing system. In the large centralized associations where members are not so personally acquainted with one another as in the compact locals, a contract is especially valuable. A continuous delivery of commodities to the cooperative by its members establishes a permanency and stability in the organization which indiscriminate delivery would not accomplish. However, the mere formality of signing contracts does not assure delivery; there is no certainty that the association will receive all products which such contracts call for.

Some of the cooperative cotton and tobacco marketing associations in this country have experienced many cases of violation of marketing agreements. For example, in the Tobacco Growers Cooperative Association of Virginia, North Carolina, and South Carolina, it was found that in the years 1922-1925 the following percentages of contract signers actually delivered crops in the

various years: 1922, 87 per cent; 1923, 75 per cent; 1924, 59 per cent; 1925, 45 per cent. When the members of this organization were asked, "When did you first sell outside?" 13.6 per cent of those who sold outside admitted first doing so in 1922; 22.1 per cent in 1923; 28.2 per cent in 1924; 32.4 per cent in 1925; and the remainder stated that they did not know when they first broke their contracts. Of all the members visited 44 per cent admitted having sold outside of the association."<sup>1</sup> Reasons most frequently given by members were: "forced to sell outside," "payments were too low," "association had failed," "everybody else was selling outside."<sup>2</sup>

In a study of the Staple Cotton Cooperative Association made by the United States Department of Agriculture the following information in the table below was obtained with respect to the deliveries upon marketing contracts.

TABLE VI.—DELIVERIES ON CONTRACTS IN THE STAPLE COTTON COOPERATIVE ASSOCIATION 1921-1925\*

Season	Contracts signed	Delivering on contract	
		Members	Percentage of contracts signed
1921-1922	1,832	1,508	82.3
1922-1923	2,445	1,770	72.4
1923-1924	2,497	1,384	55.4
1924-1925	2,518	1,165	46.3

\* SWARTHOUT, A. V., *Farmers' Cooperative Business Study, U. S. Dept. Agr., Circ. 397, p. 18, 1926.*

According to this table, less than half of the contract signers delivered cotton in 1924-1925. There were theoretically 2,518 contracts in force at the end of 1924-1925, but on only 2,249 had deliveries been made at any time. This left 269 contracts, or 10.7 per cent on which no deliveries had been made and for which the reasons for nondelivery were not a matter of record. The records of this association showed that of the members who signed the contract prior to the end of the first year 1921-1922,

<sup>1</sup> SCANLAN, JOHN J., and J. M. TINLEY, *Business Analysis of the Tobacco Growers' Cooperative Association, U. S. Dept. Agr., Circ. 100, p. 41, 1929.*

<sup>2</sup> *Ibid.*, p. 41.



14 per cent never delivered cotton to the association; 19 per cent delivered in 1921 only; 37 per cent in all of the four years; 11 per cent for three years; 17 per cent for two years and 2 per cent for one year, except 1921. These illustrations are to point out that 100 per cent deliveries, even with the use of a contract, are by no means definitely assured to the association.

The experience of the South Carolina Cotton Growers Cooperative Association with respect to its marketing agreement showed very clearly that (a) a whirlwind sign-up does not result in a loyal membership, (b) many irresponsible small producers are easily obtained but not retained, and (c) dependable larger producers can be secured when the terms, conditions, and advantages of the marketing agreement are fully explained. When the organization was started in the typical fashion of the large centralized tobacco and cotton associations, county organizers, who received a commission for each contract secured, literally herded hundreds into the association regardless of the production or the credit standing of the producers signing the contract. Numbers and nothing else seemed to count. Naturally, much difficulty would be encountered with this type of membership. Practically all of those who flocked to the association on the slightest impulse also forsook it about as rapidly. When the contract expired in 1927, only 8 per cent of the original signers signed the new contract. This is shown in Table VII.

TABLE VII.—MEMBERSHIP PERFORMANCE OF THOSE WHO SIGNED THE SOUTH CAROLINA COTTON GROWERS MARKETING AGREEMENT IN 1922  
TOTAL SIGNERS 11,434\*

Year	Members delivering		Year	Members delivering	
	Number	Per cent		Number	Per cent
1922-1923 1st year	7444	65	1927-1928 6th year	900	8
1923-1924 2d year	6489	57	1928-1929 7th year	652	6
1924-1925 3d year	5452	48	1929-1930 8th year	536	5
1925-1926 4th year	4771	42	1930-1931 9th year	403	3
1926-1927 5th year	3284	29	1931-1932 10th year	202	2

\* From GEN. WILSON, and EDWARD ALLISON TERRY, "The Cotton Cooperatives in the South-east," p. 160. D. Appleton-Century Company, Inc., New York, 1933.

According to this table, only 65 per cent of the contract signers delivered during the first year, and during the fifth and last year of the contract only 29 per cent of the original signers delivered their cotton. Only 8 per cent of the 11,434 signers in 1922 signed the second contract in 1927, and by the tenth year only 2 per cent still delivered cotton to the cooperative. Other producers swelled the ranks in the meantime. Some growers quit raising cotton, some died, and no doubt, some moved away, but the vast majority, 95 per cent or more in the first few years, simply did not deliver the cotton they produced. What an appalling example of disloyalty and what a reflection upon the manner of organizing an association! What an argument for a selective membership policy!

In the next table the interesting fact is presented that in several southern states the larger—and very likely more debt-free producers—signed the second contract as against the small, credit-restricted producers who signed the first. The large average baleage for the South Carolina association during 1922–1923 and 1923–1924 was due to the inclusion of large eastern producers of long staple cotton. The average baleage of 23 and 26 in the last two years when compared with the 11 and 12 bales per delivering member in 1925 and 1926 shows the contrast.

TABLE VIII.—AVERAGE NUMBER OF BALES OF COTTON PER DELIVERING MEMBER BY ASSOCIATIONS AND YEARS\*

Year	Alabama	Georgia	North Carolina	South Carolina	Average
1922–1923	7	7	9	16	8
1923–1924	5	5	8	13	7
1924–1925	7	7	7	11	8
1925–1926	14	8	10	12	10
1926–1927	16	10	10	12	11
1927–1928	12	9	13	14	12
1928–1929	15	18	17	17	16
1929–1930	16	20	18	23	19
1930–1931	10	23	17	26	17

\* From GEE, WILSON, and EDWARD ALLISON TERRY, "The Cotton Cooperatives in the South-east," p. 168, D. Appleton-Century Company, Inc., New York, 1933.

In another association, the Northern Wisconsin Cooperative Tobacco Pool, the annual number of contract breakers varied

from 0.14 to 8.00 per cent of the membership over an 8-year period.

2. A contract is also used to cut down the cost of assembling members' products by insuring their delivery. Private businesses solicit farmers' business at considerable expense to themselves. Such expense is obviated in associations by membership contracts. Therefore, aside from the economies of large-scale operations, the contract can become an instrument to definitely lower the costs of marketing farm products. To the extent that the contracts are broken and extra costs due to litigation are placed upon the association, the economies in obtaining member patronage may be completely lost.

3. The contract also assures the association a certain volume of business upon which to plan future operations, sales, commitments, and merchandising programs. This is particularly important for the large-scale sales associations that make contracts months in advance, with business firms for the delivery of their members' products. Such commitments would be impossible if there were not some assurance of the delivery of a certain volume of products from the association's membership.

4. To the extent that a contract assures and increases the volume of business of a cooperative, the association is in a position to adjust its costs to a minimum. A large number of deliveries one year may necessitate extra investments in plant and equipment which are only partially used if a small number deliver the next year. Plant managers are in a much better position to handle deliveries of their members' products if some knowledge is had ahead of time as to the probable receipts. Costs in such cases can be kept down. Marketing companies in general are businesses subject to decreasing cost; the increased volume which contracts may secure is an important factor in reducing the costs of operation.

5. The contract is also valuable in materially assisting the association in its financing operations. Practically all bankers require that the sales associations have valid contracts with their members which specifically state the rights and powers of the association with respect to the farmers' products. Many well-drawn contracts include a clause permitting the association to pledge the producers' crops as collateral for a loan. A more substantial basis for credit is thus established.

6. The prestige of the association is enhanced by the use of a contract. The stability and permanency do much to elevate the standing of the association in the eyes of both the public and business interests. A strong appeal to competent managers can be made.

The economic value of the contract is particularly important during the early years of the association. During this crucial period the members, who have subscribed to the program of the association, are most likely to default in their responsibilities to it. Also it is during the early years of the association that the competition from established agencies is keenest and sometimes vicious. During these trying years, the contract becomes an important instrument in helping the association "to get on its feet."

After the association, however, has demonstrated its ability as an efficient distributor of the farmer's products, the contract becomes less important from the economic standpoint. It is for this reason also that we note in many associations that the first contracts call for longer duration periods than the contracts in subsequent years after the business has been firmly established. If the association cannot demonstrate efficient operations superior to that of independent marketing companies it is unlikely that the contract alone will hold the membership.

#### LEGAL IMPORTANCE OF CONTRACTS

A contract also has its legal value. As a matter of fact when contracts were coming into general use, the legal value of the contract was emphasized as being more important than the economic value, and, therefore, the legal implications of a contract, the ironclad features of the same, and the coercive powers of the contract over disloyal members were pointed out in glowing terms. Oftentimes the legal value was emphasized out of all proportion to its real merits. Four important considerations under the legal value of the contract are:

1. It prevents minority groups from deserting an association and violating an agreement with impunity which they originally made in good faith.

2. It has proved invaluable in numerous instances to restrain outside interference with the delivery of the members' products to the association. Private businessmen who are interested in

obtaining the products of the members of the cooperative are restrained by the contract from obtaining the same. Numerous cooperative associations have to invoke the rights under the contractual relations with their members in order to obtain their just rights against third party interference. In June, 1935, for example, the Supreme Court of Rhode Island upheld the contention of the Local Dairymen's Association of Providence that third parties would be enjoined from delivering milk produced by members of the association to dealers or places not expressly designated by the association.

3. The contract is almost indispensable if the association is to obtain damages from the noncooperating member. Damages caused to the association through the nondelivery of commodities are collectable if the contract is used, but without it no redress is legally obtainable.

4. Another minor legal value of the contract rests in the fact that the rights and duties and obligations of both parties are in writing and, therefore, are a matter of record.<sup>3</sup>

The late G. Harold Powell, long time general manager of the California Fruit Growers' Exchange, made this important comment about the usefulness of a marketing contract:<sup>4</sup>

No form of contract will hold the membership together indefinitely unless the benefits of the organization justify its continuance but the human side of some men has not yet evolved to that ideal state in which a temporary advantage offered them may not blind them to the permanent values of their own association. Therefore, voluntary membership is not practicable. Always, too, there are opportunists who take no

<sup>3</sup> BLACK, JOHN D., and H. BRUCE PRICE in *Cooperative Central Marketing Organization, Minn. Agr. Exp. Sta. Bul.* 211, p. 84, 1924, have pointed out the purposes of the membership contract as follows:

"1. To assure in advance a sufficient volume of business.

"2. To let the association know in advance how much business it will have, so that it can make adequate plans for it.

"3. To furnish a basis for credit to the association and to the growers.

"4. To furnish a basis for control over distribution of the product.

"5. In some cases, to furnish a basis for more control of quality.

"6. In some cases to furnish a basis for collective bargaining and control over time of movement to market.

"7. To prevent competitors from disrupting the organization."

<sup>4</sup> POWELL, G. HAROLD, *Fundamental Principles of Cooperation in Agriculture, Calif. Agr. Exp. Sta. Circ.* 222, pp. 11-12, 1920.

interest in the real problems of agriculture and do not see their position as part of a great working whole, *i.e.*, they have little consciousness of the larger factors influencing the disposition of crops, and, in their disposal, are rampant speculators buying and selling to individual merchants and speculators. The opponents of the cooperative system, understanding this psychology, tempt the speculative farmer with offers of high prices as a means of strengthening themselves in the community and, unless this type of producer has formally bound himself to his association by a contract to handle all of his produce through it for a given time, the buyers may draw heavily from the membership and thereby weaken its financial and business stability. A large proportion of the failures in cooperative marketing have been due to the irresponsibility of the membership when an association has been subjected to competitive fire. Then if the association has incurred liabilities, based on the expected loyalty of its members, it finds itself not only with a reduced membership but also with a correspondingly reduced income with which to meet its liabilities. Though the contract is essential to stabilize an association, it is clearly apparent that the best success will only follow when a majority of its members are convinced that the cooperative principle is most beneficial, ultimately. This conviction will be strong enough to hold them together when their opponents attack them—providing it is reinforced by the successful returns of the association itself in the management of its business.

#### THE EVOLUTION OF MARKETING AGREEMENTS

In the very earliest cooperative associations, disloyalty of membership was experienced. With the least provocation, some members forsake their organization to obtain the "high nickel" from the association's competitors. Immediate higher returns appear to be more important to a large number of producers than the greater returns which come from a long-time policy of cooperation. Consequently, the first associations included in their bylaws statements to the effect that the members were to deliver all of their products to the cooperative associations. For failure to do so, a certain charge would be imposed upon the defaulting member in accordance with the damage which such defection caused.

These early clauses in the bylaws were called "maintenance clauses," because they were designed to maintain the association, even though a member may default in delivery of products to it. Critics of the cooperative called such clauses "penalty

clauses" for they considered them as penalties upon the producer members. These clauses were, of course, defensive moves. Most of their merit depended upon the moral effect which such clauses had on the members who signed the bylaws.

Some of the first cooperative associations to use the maintenance clause in their bylaws were the cooperative grain elevators that had to meet the competition of the more firmly established private line elevators. It was possible for the line elevators in a community where the cooperative was located actually to pay more for grain than was customary, or even possible, in order that the association may be defeated in its early years of operation. Losses sustained at such points could be recouped by wider margins at other points where the line elevator did not have to meet competition from the cooperative. The cooperatives permitted the producers to take advantage of the higher prices on the condition that a payment be made to the association for such default and for the extra expense which the smaller volume of business would impose upon the remaining producers. This was simply a recognition of the fact that the member who sold to the private dealers may actually receive more money for grain than the association could obtain for it and also that the failure of a member to support his own association would be its undoing.

Of course, the defaulting member might realize enough from the deal in violation of his contract to pay damages and still have net proceeds to equal or exceed what he would have obtained from his cooperative. Under the circumstances, even though it did not have to handle the producers' grain, the association did derive an income which facilitated keeping the operating margin at a figure no greater than if all members had delivered their grain. It is, therefore, important to note that the member was permitted to sell to outsiders as long as the damage payment was made to the association.

In livestock shipping associations, it was commonly found that members who sold their livestock outside of the association were also assessed a payment for such act. Experience, however, proved in very many associations that it was nigh impossible to collect such payments from the defaulting member. In Missouri, for instance, only three out of fourteen livestock shipping associations, which reported violations of the damage clauses,

attempted to enforce this provision.<sup>5</sup> Very few local associations in other states could report a better record of enforcement.

Perhaps the first association to use a membership contract which was distinct and separate from the bylaws of the association was the Pachappa Orange Growers Association of Riverside, Calif.<sup>6</sup> This membership contract was drawn up in 1893 and followed the form which fruit growers were accustomed to sign with the private buyers of fruit. It, however, contained no enforcement clause.

During the years 1920-1925, the membership contract received special emphasis. It was considered an integral part of the organization of the centralized cooperative marketing associations and was adopted by marketing associations of practically every type of commodity. During this period, the contracts became quite detailed with respect to the numerous rights, duties, powers, and obligations of the parties to the same.

Most contracts first used were of an agency type, but in the period of 1920-1925, the purchase and sale type became particularly prominent among the fruit and vegetable marketing associations and among the centralized types of organizations in general.

In Denmark contracts have been used for many years in each of the various commodity organizations. Christensen reports that these contracts ranged in length from 1 to 20 years, and have been used to bind the members to deliver all of their marketable products to their marketing associations.<sup>7</sup> The unlimited liability of members in their associations made it particularly important for all members to deliver their products. Likewise, the fact that the fixed and circulating capital was obtained through bank loans rather than from investments by members made it essential that long and continuous operation of the associations be assured in order that the loans could be obtained and repaid.<sup>8</sup>

<sup>5</sup> THOMSEN, F. L., and G. B. THORNE, *Cooperative Marketing for Missouri, Mo. Agr. Exp. Station Bul.* 253, p. 83, 1927.

<sup>6</sup> NOURSE, EDWIN G., "The Legal Status of Agricultural Cooperation," p. 183, The Macmillan Company, New York, 1928.

<sup>7</sup> CHRISTENSEN, CHRIS L., *Agricultural Cooperation in Denmark, U. S. Dept. Agr. Bul.* 1266, p. 13, 1924.

<sup>8</sup> In a letter to Black and Price, *op. cit.*, p. 37, Mr. Christensen stated, "My experience and studies in Denmark induce me to say that the Danish membership contract is a very vital part of Danish cooperation. . . . The



## TYPES OF CONTRACTS

From the standpoint of the legal relationship of the cooperative association to the producer and the product which is handled, there are two principal types of producers' contracts which are used: (1) agency; and (2) purchase and sale. These types relate primarily to the difference in the legal position of the association with respect to the commodity handled rather than to the enforcement or attitude of the court toward the membership contract in general. As the name suggests, the agency contract is designed to establish an agency relationship between the association and the producer. For all intent and purposes, the association becomes the agent of the grower in the sale of his product. As such, the laws relating to agency relationships determine the rights and duties of each party.

Under the purchase and sale type of contract, the association actually takes title to the commodity purchased from the producer and agrees to pay for the commodity on the basis of the sale price obtained by the association.

A third type, combining certain features of both the agency and the purchase and sale types, is being considered by some associations. As proposed for a potato marketing organization this contract permits the association to buy the growers' potatoes under certain conditions and at other times to handle the potatoes for the grower on an agency basis. (See Appendix B.)

Contracts may be classified, however, on another basis, namely, on the basis of the method in which the growers' products are to be handled. In this respect, there are again two main types of contracts, (1) pooling, and (2) nonpooling contracts. A pooling contract, as the name suggests, is an agreement in which the grower allows the association to pool his products with the products of other producers, usually according to definite grades. In the nonpool contract each grower's products are handled as separate units. Some associations have found it advisable to change their form of contract from a nonpooling to a pooling

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success achieved by the Danish cooperatives is, in a measure, due to the strong financial position which their membership contract makes possible, together with an assured volume of business. The most active leaders in Danish cooperation today consider their membership contract an important feature in their cooperative organization."

contract, or vice versa. For example, the former contract of the Rice Growers Association of California which provided for the sale of each member's crop to commercial millers at a minimum price fixed by the growers was discarded for a new pooling form of contract which would serve its changing needs.

Pooling contracts usually called for the pooling of seasonally produced products on a seasonal basis, but in more recent years, particularly among the cotton cooperatives, growers were granted the choice of optional pools.

In the agency contract the following type of clause establishes the agency's relationship:

The member hereby appoints the association his sole and exclusive agent and also his attorney in fact — with full power and authority in its own name, and in the name of the said member or otherwise to transact such business — including the power to pool —.

The association on its part agrees to prepare for market, market and sell — and rateably to divide the proceeds of the sale of the — of like variety and grade pooled —.

In the purchase and sale type of contract the relationship is usually established in the following terms:

The grower agrees that he will sell to the pool all the — either planted or harvested, either by or for the grower, during the term of his contract. The pool agrees that it will buy all the — so planted or harvested by or for grower. The parties agree that the purchase price which shall be paid for the — shall be the average price which the pool receives upon resale minus a uniform charge on all — of the same grade or of the same classification to substantially cover the expense of operating the pool; average price to be based upon the pool's total receipts from the sale of — of the year's crop which is of the same grade.

Or it may read as follows:

The association agrees to buy and the grower agrees to sell all the — produced or acquired by or for him in — during the years —.

The use of the different types of contracts has been the subject of various studies. Johnson<sup>9</sup> in his thesis on "The Coopera-

<sup>9</sup> JOHNSON, GEORGE F., *The Cooperative Marketing Contract*, mimeographed publication of the Wisconsin Experiment Station, Madison, Wis.

tive Membership Contract" states that the agency contract was used by thirty-six out of ninety-four associations reported in his study.

The purchase and sale contract was used by fifty-eight associations as is indicated in the following table:

TABLE IX.—SALES AND AGENCY CONTRACTS CLASSIFIED ACCORDING TO PERISHABILITY OF PRODUCTS MARKETED\*

Kind of contracts	Total	Perishable	Non-perishable	General
Agency.....	36	22	12	2
Purchase and sale.....	58	15	43	
Total.....	94	37	55	2

\* JOHNSON, GEORGE F., *The Cooperative Membership Contract*, p. 3, mimeograph Publication of Wisconsin Experiment Station, Madison, Wis.

It is apparent from this study that in associations handling perishable commodities the agency type of contract predominated, while the purchase and sale contracts were used to a larger extent by associations handling staple commodities. In another study made of the use of contracts it was found that of

54 contracts analyzed . . . 41 specifically transfer title to the product to the association and the other 13 are agency contracts. Of the 41 contracts specifically transferring title, 39 are centralized organizations and 2 are federations. Of the 13 agency contracts, 8 are for federations and 5 for centralized organizations. Of the 41 which transfer title, 25 are called "purchase and sales agreements" in the contract, 14 simply specify transfer of title, and 2 are called agency contracts in spite of the fact that they specifically transfer title.<sup>10</sup>

Of 68 capital stock associations reporting to the authors in 1934, 45 or two-thirds used contracts, and of 52 nonstock associations reporting, 41 or four-fifths used contracts. On the basis of this small sample it appears that the nonstock associations use the contracts more generally than the capital stock companies.

The purchase and sale type of contract was used chiefly by organizations selling nonperishables. It was used rather universally by the centralized type of organizations which handled cotton, tobacco, wheat, and fruit. The association buys the products from the members and takes title to the same, and

<sup>10</sup> BLACK and PRICE, *op. cit.*, p. 84.

such purchase may be either by cash or one in which the price depends upon the resale value of the commodity.

The remedies for breach of contract are the same under both types, and in the decisions of the courts, there appears to be no marked difference in the attitude toward one or the other. The bankers of our country, however, appear to be more favorably disposed toward the purchase and sale contract in which the association has a clear cut right with respect to the storing of commodities and the use of the same as collateral for loans.

#### DURATION OF CONTRACTS

The length of time in which a contract is in force is an important consideration, for both the producer and the association. Most people are not disposed to obligate themselves to market for many years through a company newly organized, inexperienced, and different in operation from the usual type of concern. Consequently, contracts of varying lengths have been used by associations throughout the United States.<sup>11</sup>

Of eighty-three contracts in force in 1934-1935 and analyzed by the authors, the shortest ran for 3 months and the longest for "life." The 1-year, 3-year, 5-year, 10-year and "continuous" contracts were used most frequently as the following listing shows.

TABLE X.—DURATION OF CONTRACTS IN LARGE-SCALE AMERICAN COOPERATIVE SALES ASSOCIATIONS, 1934-1935

Length of contract	Number of associations reporting	Length of contract	Number of associations reporting
3 months.....	1	17 years.....	1
1 year.....	18	20 years.....	2
2 years.....	4	As long as stock is held..	2
3 years.....	9	"Life".....	4
5 years.....	9	"Continuous".....	18
10 years.....	13		
15 years.....	2	Total reporting.....	83

<sup>11</sup> In Danish cooperative creameries contracts are from 5 to 20 years in length; in cooperative packing factories 5, 7, or 10 years; in cattle export associations 3 years; and in cooperative butter export associations 1 year. Some of these contracts also include provisions for automatic renewal, unless notice is given to the effect that the member does not wish to renew his contract. CHRISTENSEN, *op. cit.*, p. 13.

Of the 94 contracts analyzed by Johnson, the duration period varied from 1 to 15 years with the 5-year and 1-year terms in greatest use. This is shown in Table IX. The Poultry Producers of Central California uses a 15-year contract. It includes, however, definite cancellation periods provided proper notice is given.

Contracts may be divided into (1) terminating contracts, and (2) the self-renewing contracts. The terminating contracts contain a clause specifically stating the expiration date. The self-renewing contract runs for a definite time period mentioned in the agreement, but in addition, as the name suggests, includes a renewing clause. According to Johnson's study few of the terminating contracts granted a withdrawal privilege to the producer, while most of the self-renewing contracts did.

Ordinarily a contract runs for a period of 1, 3, or 5 years, but at the expiration of this period, during some specified month, the producer and the association have the right to terminate the contract. If such termination is not made, the contract automatically renews itself usually for a period of 1 year. The inclusion of such a provision gives a flexibility to the contract which more nearly meets the approval of a large number of producers than the long-term contract without the period of withdrawal and without the self-renewing feature. If the contract is not self-renewing, it is necessary for the association to go through a difficult and oftentimes critical period of re-sign-up. The expense of such a sign-up campaign and the opportunity which it affords to the antagonists of cooperative associations are important reasons for using the annual self-renewing contracts.

Fifty-five of the ninety-four contracts analyzed by Johnson had no withdrawal privilege during the contract period, whereas thirty-nine gave this privilege to the producer. In all likelihood the ratio of those having the withdrawal privilege to those that do not would be greater today than during 1924.

The clause including this withdrawal and self-renewing feature is worded similar to the following:

After the association has been in operation for the receiving of (tobacco) of one crop year, either party hereto may cancel the contract on May 1 of any year thereafter by notifying the other party in writing of this intention; such notice to be given during the month of April, immediately prior to the effective date of cancellation. If neither of

TABLE XI.—CONTRACTS CLASSIFIED ACCORDING TO DURATION, WITHDRAWAL PRIVILEGE, AND POSSIBILITIES OF RENEWAL AT END OF CONTRACT PERIOD 1924\*

American organization	Duration of contract	Number of organizations	Self-renewing† contracts	Terminating contracts‡	Time of exercising withdrawal privilege	
No withdrawal privilege during contract period	7 years	2		2		
	6 years	5	1	4		
	5 years	40	3	37		
	4 years	4		4		
	3 years	4	2	2		
Total		55	6	49		
Withdrawal privilege during contract period	15 years	1		1		Every 2 years Each year Every year
	5 years	5		5		
	4 years	1		1		
	1 year	26	25	1		
	No time stated	6	6			
Total		39	31	8		
Danish organization§	1 year	8	8		End of fiscal year on 2-6 months notice	

\* JOHNSON, GEORGE F., "The Cooperative Marketing Contract," p. 2, mimeographed publication of the Wisconsin Experiment Station, Madison, Wis.

† These contracts continue indefinitely unless member gives notice of withdrawal at end of stated contract period.

‡ Contracts which terminate at end of contract period. New contracts must be signed. Old contracts not renewable.

§ Eight of the eleven largest Danish Cooperative Associations.

the parties hereto cancels this agreement on May 1 of any year as aforesaid, it is hereby mutually agreed that that fact shall constitute conclusive evidence that the parties hereto have renewed this contract for another year.

Some of the state laws today definitely limit the length of time for marketing contracts. The Wisconsin and Minnesota laws, for example, do not permit contracts to run longer than 5 years, the North Carolina and Washington laws for 10 years, and the Standard Cooperative Marketing Act for a period not exceeding

10 years. The general tendency is to shorten, rather than to lengthen, the period of time for the contracts.

What should determine the length of a marketing contract? It has already been stated that the contracts introduced in 1920-1925 were of long duration and inflexible.<sup>12</sup>

The Associated Raisin Growers used a contract 15 years in length and many of the associations in the South had 10-year contracts. The question naturally arises as to the need of such long contracts. The length of a contract should be based upon the time required for an association to demonstrate its efficiency as a marketing agency. There appear to be, therefore, two important factors which influence the length of a marketing contract, (1) the market characteristics of the commodity, and (2) the amount and the nature of the capital investment.

Commodities which require storage, curing, or preserving and those which are produced seasonally, but marketed over a period of 1, 2, or more years naturally affect the business of associations in an entirely different manner from those commodities which are sold in a relatively short period of time. It is not uncommon to find cooperative tobacco marketing associations holding tobacco for 1 to 3 years for the purpose either of selling the tobacco to better advantage or of holding a normal amount in storage. Large-scale sales associations which are engaged in long-term sales arrangements find it to their advantage to have contracts of a greater length than 1 or 2 years. For some a 3- to 5-year contract appears desirable and amply suitable. There is some question, therefore, whether a contract longer than 5 years is essential to such associations.

The size of the investment in physical facilities, such as warehouses, drying plants, and packing establishments, requires the

<sup>12</sup> Aaron Sapiro, an advocate of long-term contracts, expressed himself as follows in 1923: "The contract should always be a long-term agreement. It is impossible for farmers in a period of less than three years to develop a trained personnel, to perfect the process of receiving the commodity, to make good and wise commercial connections and to effect satisfactory banking arrangements. The rule is rather sound—a short-term contract is hardly worth the paper it is written on. A long-term contract gives the farmer a chance. There should be no right of withdrawal whatsoever, except at the end of a specified long term. If the farmers intend to try the cooperative marketing system, they should go into that work seriously, earnestly, and on a permanent basis."

assurance of a certain volume of business for a sufficient number of years in which these capital investments may be paid off. It is apparent at once that few investors would care to place their investments in companies erecting such plants if there were not some assurance of a fairly long life of the association, which a contract for a relatively long period could give. In livestock shipping associations, which complete all transactions with respect to particular shipments within a few days after the shipment is made, there would be little reason for having contracts for periods longer than one year. From the standpoint of the management, it is, of course, quite desirable that the contract call for a period longer than one year in order to obviate the necessity of having a re-sign-up campaign, or of meeting the period of withdrawal at an early date. The merits of the livestock shipping association are often revealed to the producers before the entire year is passed, and it should be primarily on the strength of the efficiency of the operation, rather than on the coercive nature of a contract, that the members are held to the organization.

Black and Price in writing about the length of the membership contract state.

A membership contract ought to run long enough to give an association an opportunity to demonstrate its possibilities. With some commodities two years, or even less, may be enough; with others five years may be needed. It is difficult to see why more than five years will ever be needed. The factors determining the time required to demonstrate success are as follows: (1) With some commodities the price is not sufficiently predictable that an association may not go wrong several years in succession, . . . (2) With some commodities, a large nationwide selling organization may need to be set up which will take several years to develop properly. . . (3) If all the financing that is needed is a crop at a time, a one-year contract will be adequate for any sound plan of financing. If, however, warehouses need to be built and paid for, and the like, it may not be possible to borrow the money unless the contract ties up the members long enough to insure the payment of the loan.<sup>13</sup>

The unhappy experience which many cooperative associations, particularly cotton and tobacco, have had with the enforcement of long-term contracts, together with the lessons learned from having too inflexible pooling privileges, has caused two important

<sup>13</sup> BLACK and PRICE, *op. cit.*, pp. 86, 87.



changes in modern contracts, (1) a shortening of contract periods, and (2) optional pooling or sales methods. Instead of the usual seasonal pool which has not always proved practicable in potato and cotton marketing associations for all producers, optional pools and shorter pool periods are now included in the contracts. Not all contracts are shorter now than they were a decade ago. For example, the cotton contracts in Alabama, Georgia, and South Carolina were changed in 1926-1927 from a 5-year terminating contract to a 7-year contract with annual withdrawal periods. These are, however, exceptions to the rule, but even these contracts can be canceled at yearly intervals. The so-called "perpetual" or "life" contracts are, in fact, 1-year contracts, but since they do not have to be renewed each year (if no notice of cancellation is given during a specified period, the agreement is automatically renewed for another year—comparable to leases on homes), they have been given the more descriptive term. The Connecticut Milk Producers Association of Hartford, Connecticut and other large bargaining associations of the country use such "perpetual" contracts.

#### FILING OF CONTRACTS

The fact that the cooperative association has a legal interest in the crops to be marketed is particularly important to third parties, who also may desire to obtain the products of the cooperative's membership. In order that third parties may be properly notified of the legal interest which cooperatives have in the members' products, it is well for the association to file its contracts with the Register of Deeds in the counties where the cooperative is located. Relating to the filing of contracts the state law of Wisconsin includes a provision in the following terms:

The association may cause to be filed in the office of the Register of Deeds of the county in which the member maker of such contract resides, a copy of any such contract to sell to or through the association. In case it has more than one contract in any one county, it may cause a copy of any uniform contract, together with a sworn list of the names of all makers of such contracts residing in any such county to be so filed. . . . From and after the date of such filing the same shall constitute notice to any and all persons that an interest in the title to all property so agreed to be sold by the maker of such contract during the term of such contract is vested in the said association. In case of a purchase

thereafter of any such property by any party, other than the association, no title of any kind or nature shall pass to such other purchaser, and the said association may recover the possession of such property from any and all such other parties, or from any party in whose possession the same may be found, by replevin action, or may sue for injunction.

A few years ago a tobacco cooperative association in Wisconsin recovered several thousand pounds of tobacco by replevin action in accordance with the terms of this section of the law. In other states where the filing of contracts is not definitely included in the cooperative marketing act of the state, recovery was nevertheless obtained according to the laws which appertain to contracts in general.

#### REMEDIES FOR BREACH OF CONTRACT

The enforcement of contracts is no easy matter, particularly for the management of local associations. Large-scale associations which have a legal department find it less embarrassing. Before legal action is taken against the defaulting member, the matter of breach should be discussed with the member and if possible settled out of court.<sup>14</sup> For those, however, who surreptitiously sell outside the association or break their contract with impunity, it becomes necessary for the association to invoke the remedies at law if the morale of the loyal producers is to be maintained. The breach of contract results in two types of damages; (1) the economic damages, and (2) the adverse psychological effect which the defection has on other producers. In many instances the effect of both types of damages is immeasurable, although the economic damages can be approximated after a fashion. The remedies which are ordinarily open to the association are of three kinds (1) liquidated damages; (2) injunction; and (3) specific performance. All of these remedies have been approved in practically all courts of the land in numerous cases that have come before the courts during the last 20 years.

<sup>14</sup> The Georgia Cotton Growers' Cooperative Association instituted well over 200 suits against contract violators. The expense of such suits, the fact that dissatisfied members are retained in the association even if the association wins the decision, and the adverse effect which the recalcitrant members have on good members make doubtful the advisability of such wholesale litigation.

**1. Liquidated Damage.** The early maintenance clauses which were included in the bylaws of associations were an attempt to reimburse the association for damages which defection caused. Such damage is not always definitely measurable, although it can be approximated. Liquidated damage is a payment for the estimate of the harm done following defection of a contract and is agreed upon by both parties in advance. Sometimes it is confused with a penalty, but the essential difference is this: A liquidated damage is a suitable, reasonable compensation for economic loss, while a penalty is considered to be unjust, oppressive, and more than sufficient to pay for the loss which was sustained. A penalty is considered a punishment, but a liquidated damage is not punitive in character. Courts have almost regularly upheld the payment of reasonable liquidated damages, but not payments which in effect constituted penalties. The character or type of contract does not effect the enforcement of the payment, and liquidated damages, injunction, and specific performance are remedies granted under the types of contracts previously discussed.

Liquidated damages may be (a) on a percentage of sale value basis; or (b) on a flat sum per unit of product basis. Thirty per cent of the value of the products is a common damage assessment. Such flat sums as 4 cents per gallon of milk, 25 cents per bushel of wheat, 7 cents per dozen of eggs, \$5 per cow (for members of fluid milk associations), 2 cents per pound of peanuts, \$2 per ton of hay, 3 cents per pound of cotton, and 25 cents per box of fruit are damages included in various contracts. These amounts vary by organizations and with changes in the level of prices.

In lieu of a specific sum the state cooperative marketing law in Wisconsin permits a liquidated damage to be as high as 30 per cent of the value of the products which are the subject of the breach. Black and Price report that

. . . of 67 contracts of central marketing organizations examined, 61 specify amounts to be paid by the member in case of failure to deliver his product to the organization. . . . Thirty-nine of the 61 associations, whose contracts provide for liquidated damages, also include a clause giving the association the right to secure an injunction to prevent breach or to secure a decree for specific performance. The contract of one association entitles it to an injunction without liquidated damages

or penalty. Of the 40 associations which are entitled to an injunction by the terms of their contracts, 39 are of the centralized type. This indicates clearly the origin of the provision.<sup>15</sup>

**2. Injunction.** Ordinarily where liquidated damages suffice in reimbursing the association, a court will not issue a decree of injunction. Usually a decree of injunction and one of specific performance are considered together. The injunction is a negative method of enforcement by restraining the producer from marketing his crops through anyone other than the association. The injunction does not enforce the producer to market his crops; he may keep his products, use them entirely on his farm, give them away, or destroy them, but if marketed they must be sold through the association.

A court injunction may be of two kinds: (a) It may enjoin the members from selling outside the association; (b) it may enjoin outsiders or third parties from inducing members to violate their contracts. In numerous cases which have come before the courts in which third parties were involved it was shown that some had gone so far as to offer to pay liquidated damages to the association if such were invoked. It is apparent at once that the use of the injunction is especially significant for those associations that have made commitments to deliver the products anticipated from their members. If a tobacco cooperative, for example, has agreed to sell millions of pounds of tobacco, it must have the tobacco in order to make delivery or be able to enter the market and buy the kind of tobacco which the commitment calls for. Since the latter is oftentimes impossible, it is perfectly apparent that the paying of liquidated damages would not help the association in meeting its delivery commitments. Enjoining outsiders is important for another reason, namely, it has a psychic effect upon the association membership. An action of specific performance is not applicable to third parties. Through replevin action the identical commodities sold by producer members to outside parties can be recovered by the association. The first injunctive relief was sought by the Riverside Fruit Growers Association in 1894 and, according to a report, the first Supreme Court decision which granted an order of injunction was in Kentucky in 1908.

<sup>15</sup> BLACK and PRICE, *op. cit.*, p. 90.

**3. Specific Performance.** If the remedy at law, that is the payment of liquidated damages, is adequate and complete, no decree for specific performance will ordinarily be granted by the court. This remedy is sought in a court of equity because adequate relief cannot be obtained by the payment of liquidated damages or perhaps because products are not purchasable in the market. A decree of specific performance is a definite statement of the court, directing the producer to deliver his crop to the association as he has contracted. At once the question of involuntary servitude arises which is not permitted under the Thirteenth Amendment to the Constitution. However, a decree of specific performance does not force a producer to grow a crop under his contract, not even to harvest a crop which has been planted, but it does force him to sell the crop to the association if it is sold. It is the positive method of enforcement and one which the courts will order if the remedy at law is inadequate.

#### CONCLUSIVE PRESUMPTION

The cooperative marketing statutes in some states provide that "it shall be conclusively presumed that a landowner or landlord or lessor is able to control the delivery of products produced on his land by tenants and others," if such tenancy is established after the contract is signed. This provision is embodied in the Standard Marketing Act. The execution of a marketing contract, preceding that of a tenancy contract, requires delivery of products to the association. No question arose under a crop-share lease as to the duty of the landlord to deliver his share of the crop to the association with which he held a contract, but an entirely different situation arose under cash leases. The courts of some states have questioned this conclusive presumption. Louisiana and Mississippi have held it unconstitutional, whereas others, such as Kentucky and Colorado, have upheld the provision. Examination of the law and court decisions of the respective states is necessary to discover the status of such contracts.

Certain complex problems of law have also arisen with respect to the rights of parties holding liens against crops that are under contract to the association. Who has prior right to the crop, the lien holder or the association? In such cases the question of notice of the existence of a marketing contract between the pro-

ducer and the association is important. If a lien is placed on the crop with full knowledge of the producers' contract, then the association has the right to receive the crop. The lien holder receives payment from the association if a claim is made to the association. Usually this payment is made within a year after the crop is delivered. If the lien holder has no notice of the existence of a contract between the producer and association, then the lien holder has the first right to control the marketing of the crop. If the crop is not marketed through the association, the association may collect its damages from the producer for nondelivery. State laws and court decisions of the states should be investigated for local interpretations of this problem.

#### METHODS USED IN VOIDING CONTRACTS

Numerous methods have been used by members who desire to void their contracts. Some placed liens on the crop, some sold crops in the names of their wives, others rented their farms, while still others formed corporations to take title to the land upon which a crop under contract to the association was grown. The member's defense, in such cases, is that he has lost control of the crop and, therefore, can not deliver. In these instances, however, as was stated above, it is well to look into the nature of the contract and the state law to determine definitely whether the contracts run with the land so that although there is a transfer of land, in good or bad faith, the member may still be responsible for the delivery of the crops to the association.

#### ARGUMENTS OF MEMBER DEFENDANTS

A number of common defenses have been presented in the courts when members have defaulted in their contracts. Oftentimes these defenses have been rejected by the courts. The usual arguments are that the contract lacks in consideration, mutuality of obligation, and mutuality of remedy. In other cases it has been held that misrepresentation, fraud, and duress were used in getting members to sign. In case the existence of fraud or duress is proved to have existed the argument is a valid defense. However, promises and exaggerations of what the association will be able to accomplish have not been considered as grounds for breaking the contract. The impression that a larger payment could be received from outside parties or that the association is

mismanaged are likewise generally unjustifiable causes for breaching the contract.

If the association, however, fails to receive a necessary sign-up of the contract which becomes the basis of the establishment of an association then the defense is a good one.<sup>16</sup> However, if the producer knows that a sufficient sign-up was not obtained, but later delivers his crop according to the contract without reference to this conditioning factor, he is estopped from using this defense for a later violation.

Failure of an association to perform marketing services called for in the contract are valid arguments. Where it is demonstrated that the association has not fulfilled its obligation to the member according to the terms of the contract, courts have permitted the grower to be absolved from the contract thereafter. Two cases in recent years bear upon this point. In Washington<sup>17</sup> a cooperative refused to accept a grower's 1926-1927 crop and refused further to grant the producer the right to sell outside of the association. The grower sold his crop to an outside buyer and thereafter failed to perform the terms of his marketing agreement. The court held that the association's refusal constituted a breach of the agreement and thus permitted the member to ignore his contract thereafter. The court also held that the association was unjustified in attempting to restrain the member from selling to outsiders after the crop was refused. In a Wisconsin case,<sup>18</sup> the court held that the association, refusing to regrade and reclassify a grower's tobacco crop, has not acted in good faith, and that such refusal, together with the fact that the association had no right to require the grower to execute a supplemental contract, relieved the grower from the terms of the agreement thereafter.

Two other arguments, namely, that contracts are in restraint of trade and that the laws granting the use of contracts are unconstitutional have been presented numerous times. These

<sup>16</sup> The contract of the poultry producers' association in central California became effective after the owners of a million hens had signed; of the prune growers after 75 per cent of the prune acreage was contracted, and of the Northern Wisconsin Cooperative Tobacco Pool after 20,000,000 pounds of tobacco had been signed up.

<sup>17</sup> *Guglielmelli v. Walla Walla Gardeners Association*, 288 Pac. 251 (1930).

<sup>18</sup> *Myrold v. Northern Wisconsin Cooperative Tobacco Pool*, 239 N.W. 422 (1931).

two defenses, however, have not been considered as valid by the courts in recent years.

#### PRODUCER CONTRACTS AND EFFICIENT MARKETING

It should be emphasized that the producer contract is by no means a substitute for efficient marketing by the associations. It would be incorrect for any manager or producer to consider the marketing contract as the *sine qua non* of cooperative marketing. A contract is no stronger than the will of the majority of producers that have signed the same. It is a helpful tool in the organization and simply a means to an end, rather than the end in itself. To mistake these two may lead to disastrous results in the cooperative. To consider the contract as an ironclad tie to compel membership loyalty in the face of unfavorable comparisons with private companies is placing a wholly incorrect construction upon its merits.

Thomsen and Thorne have quoted several writers in the Cooperative Marketing Journal on this subject in the following terms:<sup>19</sup>

It is a matter of common experience that a contract becomes practically unworkable as soon as a large percentage of the membership are, for any reason, inclined to disregard its conditions. . . . In a strictly cooperative association the significance of a contract depends upon the grower's attitude toward it. . . . A contract as an instrument of force is inconsistent with the idea of cooperation which is inherently a mutual and free relationship. Cooperation ceases to be cooperation as soon as it savors of coercion and force. . . . Involuntary cooperation is a contradiction of terms. . . . There is, however, no objection to mutual agreements among members in the form of . . . contracts, provided their true significance is understood. . . .

A contract is worth no more than conscience and conviction of the members behind it. . . .

Success depends upon the spirit of the growers, not on the signing of a contract.

In one of the largest cooperative marketing associations of the United States, namely, the Dark Tobacco Growers Cooperative Association of Kentucky in the year 1925, there was such a wholesale violation of the marketing contract that the management knew it inadvisable to even attempt to force delivery of the commodities. The directors on Oct. 13, 1925, passed a

<sup>19</sup> THOMSEN and THORNE, *op. cit.*, pp. 82-83.



resolution stating that no legal action would be taken against any contract signers selling outside of the association. The will of the majority was such that the contract should not be enforced, and even though the contract called for deliveries for several more years the association failed dismally, because the majority no longer desired to belong to it. As a result of the catastrophic decline in grain prices in 1929 and 1930, and the financial difficulties of the Canadian Wheat Pool, the three provincial pools in June, 1931, released their members from their contracts knowing that most contracts would be unenforceable.

From this discussion of the marketing contract, it should not be deduced that only the successful associations in this country use contracts and that those which do not use the same become unsuccessful. It is true that most large-scale marketing associations of the federated and centralized types and large bargaining associations use producer contracts; experience has proved their value. But there are thousands of local associations that operate with varying degrees of success without employing membership contracts. Very few creameries, cheese factories, and livestock shipping associations have contracts with their members and yet they seem to run successfully from year to year.

In this connection it is rather interesting to note the conclusions which Black and Price arrived at concerning the contract.<sup>20</sup>

The efficacy of membership contracts is usually greatly exaggerated. Their most important reason for being is that they furnish the basis for a membership drive and reduce the matter of membership to very definite terms. Their second most important reason for being is that financial agencies granting loans like to have the basis for their credit made as definite as possible. For most marketing organizations, especially overhead or central marketing organizations, contracts will make success somewhat more probable; in some cases a great deal more probable; in more cases, only a little more probable. In few cases are they absolutely essential to success. At present the membership contract is something of a fetish; we shall need a good bit more experience with it before we understand its true usefulness.

The authors, however, feel that experience is replete with illustrations of the successful use of contracts and that they are no longer "something of a fetish."

<sup>20</sup> BLACK and PRICE, *op. cit.*, p. 91.

**Questions**

1. Do you think farmers should be asked to sign marketing contracts with their associations? Why?
2. Should the organization of a local cooperative association be stopped if farmers in the community do not wish to sign a contract?
3. Examine a marketing contract and report what provisions are included in it.
4. In what stage of an association's existence is the contract most useful? Why?
5. On what grounds did G. Harold Powell justify the use of contracts?
6. What were the weaknesses of using maintenance clauses in place of membership contracts?
7. If a contract is violated, what remedies for breach are open to the association? What is the difference between a penalty and liquidated damage?
8. What factors determine the duration of contracts? Do you agree with the statement that "the contract should always be a long-term agreement"?
9. Does the annual withdrawal privilege weaken or strengthen a contract?
10. Why should contracts be filed with the Register of Deeds?

**PART IV**  
**FUNCTIONAL RELATIONSHIPS OF COOPERATIVE**  
**ORGANIZATIONS**

## XIII

### *Management of Cooperatives*

*Perhaps the greatest single force for the success or failure of a business venture is its management. In a cooperative where each member is given a vote and in which the members supply the products to be sold, or give the orders in the case of a purchasing association, the members are more directly concerned about the management, and have a greater influence than the usual stockholder in a private corporation.*

*Management in a cooperative rests with the membership. The directors, who are elected by the members, formulate the broad policies underlying the operations. The manager who is placed in active charge of operations is the hireling of the board. These three—members, directors, and the manager—constitute the management.*

*The rights of members respecting the organization and operations are varied. They include the adoption of the constitution and bylaws and permission to appropriate money as well as to require the directors, officers, and manager to operate within the law. The election of directors is one of the principal obligations of the membership.*

*Directors act as the governing board which directs and governs the course of action which the association should take. Besides formulating policies, enforcing their execution, and appraising the results, they must select a manager. A director cannot act as an individual; his rights and powers are limited to the authority of the entire board. Directorship is a position of trust that only men of business ability, sound judgment, and unquestioned integrity should hold.*

*The manager is the servant of the board but, as the one in charge of active operations, should not be interfered with by either members or individual directors. His task is twofold—solving the technical business problems as well as keeping the membership fully informed. Employees are urged to have their own association or union rather than become members of an association in which their interests are incompatible with those of the membership at large.*



## CHAPTER XIII

### MANAGEMENT OF COOPERATIVES

Economists have pointed out for more than a century that the factors of production consist of land, labor, capital, and entrepreneurship. The one who undertakes the management of a business organizes and directs the other three factors of production, and he becomes a claimant to a share of the total social income for the risks which he bears and the special abilities required of him. This share is called profits in contrast to rent for land, wages of labor, and interest on capital which the other factors command. In the maelstrom of production, management is the vortex. It is the hub that links the other three factors together and makes a working unit of all four. There is no phase of business organization that is more directly related to the success of an enterprise than that of management. From a practical standpoint, management consists of the control and direction over the activities of an organization.

#### IMPORTANCE OF GOOD MANAGEMENT

A number of studies of the reasons for failures or suspensions of cooperative associations indicate that lack of efficient management is responsible about as often as any other single reason. Other causes for failure such as financial difficulty, insufficient volume of business, inability to meet competition, lack of membership interest, and an inadequate accounting system are quite generally directly traceable to inefficient management though they may appear as the immediate causes for the cessation of cooperatives. Of 1,000 associations that failed during the years 1913-1923, 558 reported that inefficient management was the principal reason for the failure, according to the United States Department of Agriculture. The thousands of cooperative associations which are operating successfully in the United States and abroad today are proof that high-calibered management has been recognized as essential and capable men have been enrolled in the service of the movement.

## MEMBERS' PART IN MANAGEMENT

Without reference to the plan of organization, the successful cooperative is built from the ground up. It is a democratic institution in which the membership constitutes the legislative body which takes a vital interest in the major organization and operating policies of the association. That this function should be preserved and remain inviolate is one of the underlying reasons for the adoption of a democratic form of representation in most cooperative organizations. All who are members should have the right to express their opinions in governing the affairs of their enterprise. The members are the association; they own it and have the right to control it. Hence they should exercise their right lest control might be usurped by others. Being member owned does not necessarily imply member managed unless the members actively participate in the affairs of their organization. Voting by proxy is forbidden in cooperative associations but all are assured free expression of opinion regarding the management. Those not present at a meeting may vote by mail on specific questions and through power of attorney by individual representation.

Since an association is operated *for* the benefit of the membership and is composed *of* the members, it is logical that it should also be run *by* the membership. In a democratic institution, such as a cooperative, management cannot fall upon a few men. If that were so, then the association would soon be an oligarchy and not a democracy. It devolves upon the board of directors in particular and upon the membership in general to formulate the broad policies according to which the business should be conducted. The directors and the manager must obtain from the membership an expression of the membership's wishes, be they in the form of resolutions, bylaws, or mere pronouncements, if the organization is to serve the patrons with greatest satisfaction. It follows, therefore, that members should attend meetings regularly to discuss the business affairs of their company, to vote upon the proposals before them, and to cooperate with the manager and employees in carrying out the wishes of the association. Membership carries with it this obligation; if it is not faithfully performed, then the limitations of management become apparent.

The rights of members in the management of cooperatives are varied. A listing of these discretionary rights will suggest the range of important matters which they cover.

1. To adopt the constitution, bylaws, and amendments, as well as to change the bylaws.

2. To elect and recall directors.

3. To vote upon the appropriations of money for various purposes, to approve or disapprove loans, to increase or decrease the capitalization, to authorize deductions for operating costs, and to decide upon pooling practices and contractual arrangements between members and the cooperative.

4. To require both directors and officers, as well as agents, to run the business legally and according to the constitution, bylaws, and marketing contract.

5. To hold directors and officers liable for any damage inuring to the members for failing to discharge their responsibilities or violating the statutes, bylaws, or constitution of the association.

6. To elect a competent committee to periodically examine the records and audit the books.

7. To examine the annual reports and books of the company (for just and proper reasons).

The members, however, serve no purpose in interfering with employees and the manager in the details of the administration of a cooperative business. A manager and assistants are hired to attend to such details and should be held responsible only by the proper officers.

One of the principal duties of the members respecting the management of an association is the selection of a board of directors. Just who is qualified to be a good director is not often known until a trial-and-error process proves the merits or shortcomings of an individual. According to the bylaws of most associations, "any bona fide producer who is a member of the association" is eligible for this position of trust. Although any member in good standing is eligible, still it is apparent that not all members have the necessary qualifications.

It is assumed that honest members will be selected, that they will possess leadership, ability, good business judgment, and above all, a sound conviction that cooperative organization is good economic procedure in production and distribution. It is claimed by some that too often these desirable qualifications are overlooked and that the responsi-

bility is given to the "loudest orator," to the member who is not "so busy," to the one who deserves an honor, or perhaps it becomes a custom to "pass the office around."<sup>1</sup>

It cannot be emphasized too strongly that men with the greatest business acumen are needed on the board of directors. Soundness of judgment in business matters, an ability to grasp management problems, and an understanding of executive duties and responsibilities are essential; suavity, affability, and amicability—commendable traits as they may be—are not the most desirable ones in a good director. The selection of the directors who can act as trustees of the association is, therefore, one of the membership's principal functions in management.

#### DIRECTORS ARE THE GOVERNING BOARD

The duties of directors in local associations are usually less important than those of directors in large-scale associations. The problems of local associations are generally simple in character compared with those of large-scale organizations. In either case, however, the board, not the individual director is the governing agency, and as such constitutes with the manager the active management of an association. As the agency in command of an association, certain obligations rest upon it; to wit:

To formulate operating policies

To retain competent managerial officers who are to execute the board's policies

To enforce the policies adopted

To appraise the results of its policies

To attend all board meetings and keep accurate records of the same

To keep in touch with the membership as a liaison officer between the association and the membership

To create confidence in the organization

A board of directors determines the broad policies which serve as a guide to the manager and employees in the conduct of the business. The manager advises and confers with the directors upon the formulation of policies but, as a chosen agent, he is guided by the policies declared by the board. The minute

<sup>1</sup> BAKKEN, HENRY H., *Directors of Farm Cooperatives—Their Duties and Responsibilities*, *Wis. Agr. Exp. Sta., Circ. 245*, p. 6, 1931.



details of the business are left to the manager's discretion, but basic operating procedure is determined by the board itself. It is apparent at once that a good director must acquaint himself with marketing functions, competitors' practices, and business procedure if he is to formulate operating policies wisely.

In actual practice, however, it is found that the boards of directors do not always formulate the policies, but rather that they become in many instances the rubber stamp of approval for policies laid down by the manager. A manager of dominant personality may usurp the powers of the board or assume such powers with the board's approval. The answers of 120 associations to the question Who formulates the policies of your association? in a study made by one of the authors indicated the following:

In 49 associations it was reported that the directors assumed this responsibility

In 41 associations the managers assumed this responsibility very largely

In 10 associations the manager and the board formulated the policies with the initiative coming from the manager; in 10 others, policies were formulated in the same manner, except that the initiative came from the board; in 7 associations the initiative for policies was equally divided, and in 3 associations the executive committee (including the manager) made the policies. That the suggestion or initiative for certain policies should emanate from the manager is in keeping with good business practice, but the adoption or refusal of a suggested policy should remain with the board of directors.

Besides laying down the policies of operation, one of the duties of the board is to select a competent manager. The significance of considered judgment in this matter cannot be overstressed. Other functions which a board cannot treat lightly are observing whether the board's policies are executed by the manager as well as appraising the policies in the light of practical operations. Some of the obligations which each director assumes upon election are to keep actively in touch with members, to ascertain their wishes, grievances, and suggestions, as well as to instill confidence in the board, the manager, and the cooperative itself. A director cannot instill confidence in an association by exhorting members to patronize their cooperative unless he himself does so.

**Directors Have Certain Powers.** The duties of directors listed above are not legally enforceable but are discretionary only. If a director is negligent in these duties the membership can recall him or fail to re-elect him when his term expires, but recourse through the courts is not possible. A legal duty implies a right which the director may or may not choose to exercise. There are, however, certain powers that the law grants a director, and if these powers are exceeded or if any damage or injury accrues to the association because of his negligence or failure to fulfill his office, then legal action can be taken against a director individually. A power implies a liability. Liability for illegal acts cannot be passed to the association but remains with the directors. Powers granted by law or by the association's bylaws to directors of corporations in most states are:

1. To call regular and special meetings at will or on command
2. To elect the officers of the directorate
3. To employ a manager for the association
4. To remove officers for cause, or act to have them removed, and to fill vacancies
5. To receive, deposit, and disburse the funds of the organization
6. To make contracts
7. To issue stocks and other instruments of credit or obligations
8. To establish minimum prices on products
9. To revise and amend grades and standards within statute limitations
10. To borrow money for the association in its name<sup>2</sup>

In a local association each director has one vote, but in a large-scale central association a director may have greater voting power. The contract between a local association and the central association in a federation may provide that directors in the central association shall have votes according to the amount of stock held by the local in the central, according to the volume of business, or according to the number of members represented. Likewise in a large-scale association, the directors may elect an executive committee to which are delegated certain responsibilities in order to lessen the number of meetings of the entire board as well as to effect efficiencies in management.

The study of 120 local and large-scale sales associations named above revealed that 70 per cent of the associations have their

<sup>2</sup> BARKEN, *op. cit.*, pp. 13-14.

directors meet once a month or oftener. This high percentage of frequent meetings of boards may suggest that directors of cooperatives are attending to the affairs of management, *i.e.*, if the time of such meetings is not frittered away with the discussion of petty, nonsignificant events wholly unrelated or trivial to the business affairs of the company.

#### THE MANAGER—THE SPEARHEAD OF MANAGEMENT

In many businesses the manager is the deciding factor for success or failure. He is the technical expert, the "brains" of the going concern, the dynamo and driving force of the business. Together with his executive staff he is responsible for carrying out the policies formulated by the board of directors as well as the hundred-fold details of the business with which the board does not concern itself. Alertness and business sagacity, ability to deal with people, a reputation for business integrity—these are a manager's forte.

In a cooperative association a manager has to cope with a dual problem, (1) the technical business problems, and (2) the membership morale. In a local association a manager with a few employees usually has charge of all operations; but in a large-scale association that markets products valued at millions of dollars, the manager is assisted by executive officers, department heads, foremen, and employees. The organization of the business staff as well as the system of distributing the products of the cooperative devolves upon the manager. Keeping bankers informed of the true facts of operation at all times and establishing a high credit rating of the company are duties a manager performs. The technical business problems resolve themselves into (1) external operating policies such as sales promotion, car routing, preparation of products for market, claims, advertising, and all problems that relate to the physical distribution and pricing of the commodities; and (2) internal management problems consisting of accounting, financing, labor problems, insurance, and personnel. Interdepartmental meetings, attendance at trade association meetings and conferences with employees and directors are some of the manager's duties in keeping the association forging ahead on all fronts.

Keeping abreast of business developments or being in the vanguard in the competitive race is for many managers a simpler

task than solving the difficult problems of membership relations. A cooperative sales association must have the products of members delivered to the association if there are to be any products for sale. To keep this stream of goods flowing to the association year after year requires that the membership be informed of the sales policies, operations, and successes of management. Such information is the vitalizing element in an association. A membership relations department in charge of an "educational director" serves an admirable purpose, but in addition, the personal appearance of a manager at meetings of the membership is essential in many instances. Members want to know their manager personally, ask him questions, and receive "firsthand" information about prices, sales conditions, operating costs, and sundry other things. The manager who does not "sell" himself to the membership, be he ever so efficient in business matters, operates under a serious handicap. A sympathetic understanding of the producers' problems is no less important than ability to master the internal and external operating problems of the business itself. The difficulty in meeting this membership problem is augmented by the large number of members to be pleased.

**Frequent Mistakes by Cooperatives in Past Years.** Mistakes, errors in judgment, and lack of experience may handicap any type of business. An efficient management, however, profits by the errors of the past. Mistakes are costly. They undermine confidence, lose customers, and may cause failure of the business. The following mistakes as listed have occurred in cooperative associations. No doubt, a list equally as long could be presented for private enterprises.

1. Organizations were set up too hurriedly without a full knowledge of existing facts or a full appraisal of some of the factors necessary for success
2. Members were improperly advised as to what cooperatives could and could not do
3. Members expected the impossible
4. Organizers made extravagant promises
5. Associations attempted to operate too many delivery points
6. Associations bought too much property instead of leasing property until definite needs of the organization were more clearly established

7. Management antagonized existing trade interests by severe criticism of their past methods of handling farm products
8. Managers attempted to set arbitrary prices
9. Organizations developed into holding associations rather than organizations to merchandise their products
10. Directors were paid employees of the association
11. Secretive policy of officials resulted in distrust and rebellion on part of members
12. Contracts provided no withdrawal privilege
13. Members did not realize the importance of competent management
14. Directors did not realize that they must pay adequate salaries for competent management
15. Sufficient capital was lacking
16. Operation was attempted with insufficient volume
17. Operation was conducted with too much overhead
18. Operating costs were too high
19. Capital reserve was used to meet competition of private agencies
20. Sufficient reserves and surpluses were not built up<sup>3</sup>

Some of these mistakes are due to a lack of experience in cooperative organization but others are due to negligence, inefficiency, and indifference on the part of directors and manager. Jones in a recent bulletin propounded two lists of 30 questions for directors and manager, respectively, in order that a self-analysis may be made by each. If an analysis such as Jones suggests were seriously made by the management, there can be little doubt that some of the mistakes listed above could be avoided.<sup>4</sup>

**The Question of a Manager's Salary.** Wages of superintendence fall in a higher bracket than wages of skilled and unskilled labor. This phenomenon is not always fully appreciated by those farmers who compare their own incomes with those of managers and expect the latter to work at rates which the farmers receive. Not all members view the salary situation in this light but, rather, realize full well that expert managers

<sup>3</sup> Cooperative Marketing of Farm Products, Federal Farm Board *Bul.* 10, p. 13, 1932.

<sup>4</sup> See Jones, J. W., Membership Relations of Cooperative Associations, *Bul. No. 9*, pp. 12-17, Farm Credit Administration, Cooperative Division, sections headed The Manager's Self-analysis and Leading Questions for Directors.

of proven worth are both difficult to get and high priced. Likewise, many members also know that a well-paid manager may not be costly compared with a poorly paid manager who may be exceedingly so. A low salary does not assure economy, neither does a high salary indicate efficiency. Other things must be taken into consideration. Low cost operations, increased savings, and higher average prices received for commodities sold may go hand in hand with large salaries; whereas the reverse may be true with low salaries. Economy measures may be more profitably started in other places than in cutting salaries of management and of employees in many instances. Since the qualifications of management are not capable of standardization such as those of unskilled labor, it is obviously impossible to make an accurate comparison between salaries paid by private and cooperative associations. Some contend that salaries in cooperatives are lower because farmers are known to pay low wages, that tenure of office is more secure and hence offers an attraction to managers at lower rates, and that in harmony with the philosophy of some cooperative leaders large salaries are frowned upon. Others contend, however, that a cooperative must pay more for managerial ability because it is necessary to compete with private corporations in securing managers and that many qualified managers prefer employment in a private business in which they may hold common stock and in which advancement to the presidency or chairmanship of the board is possible (impossible in a cooperative). These are only opinions and are merely listed to give two points of view. As among private corporations, some cooperatives are known to pay low salaries to their managers and others high salaries. In fact a proposal was made by some Congressmen in the days of the Federal Farm Board to prevent the Farm Board from lending money to cooperatives who paid their managers high salaries.

#### EMPLOYEES AND MANAGEMENT

The policy of most corporations is to permit the manager to hire and discharge all employees in unimportant positions but to submit the names of department heads or other high salaried appointments to the board of directors for approval. Every manager attempts to create an *esprit de corps* among his employees through such means as high wages, sociability, bonuses, old-age

pensions, or promotions. Employees are not a part of the management but their cooperation with the manager can make the task of management an easier duty to perform.

In theory a cooperative should be in sympathy with organized labor but in practice many cooperatives disapprove of trade-unionism within their own plants. This antipathy is largely induced by a competitive situation and reflects the personal feelings of the manager or the individual members of the board rather than the basic philosophy of cooperativism. The fear is, of course, that organized labor may be successful in getting a larger share of the consumer's dollar as wages than the farmer gets as prices for his product. Even though the interests of the two groups clash, it is apparent that if cooperators are consistent in their viewpoints regarding organization they should welcome organized labor within their own plants.

This view, however, does not imply that laborers in a cooperative sales or purchasing association should be taken in as copartners in the business, that they be given common stock, voting rights, positions on the board of directors, and share with the members in the dividends of the cooperative. In a cooperative sales association farmers are members and their interest is not compatible with that of the employees of the company. The former want high prices and low costs of operation; the latter want high wages which increase the cost of operations at the expense of the farmers. It appears far more expedient to limit the membership of the association to the farmers and have the employees have their own organization which will strive to enhance their interests. In a consumers' cooperative the situation is somewhat different. Employees, as consumers, are also eligible for membership in the cooperative that hires them. But even here, when policies of the cooperative are discussed, the attitude of a consumer rather than that of a wage earner must predominate, otherwise a clash of interests is almost certain to arise. Many members of a consumer cooperative are not laborers but as consumers have certain interests in common with the laborers who are also members.

Employees in a cooperative sales association can have, and should be encouraged to have, a financial interest in the company they serve by buying preferred stock in the same. This procedure has much in its favor. Some cooperatives of the past

and even today divide the net savings between the employees and the members as dividends on wages and dividends on patronage. This is a dangerous practice and as experience has demonstrated should not be countenanced. In its final analysis any net savings are simply withholdings from the returns that members of a sales association have a right to expect. In a cooperative purchasing association, they can be likened to "overcharges" that have been made only to be returned to the members when costs of operation for a given period have been ascertained. The employees who have been hired at fixed wages have no legitimate claim to these savings. Dividends upon fair wages are an unjust diversion of funds rightfully belonging to the members of the association. If an association wishes to grant a bonus for exceptional service or as a reward for efficiency, extra labor, or special circumstances, such procedure can be condoned. The fact that some state cooperative laws permit such appropriation before the patronage dividends are declared indicates the fact that appropriation even for this purpose has been challenged and only made certain after the cooperative law was amended to include this right. The principle underlying such gratuity is quite different from that which considers laborers as legitimate claimants for dividends on wages.<sup>5</sup>

#### Questions

1. Who is an entrepreneur? Does the member of a cooperative classify as such?
2. List the rights of the membership and prepare a second list showing some actions not considered rights.
3. Does farmer owned imply farmer controlled? Explain.
4. What powers do directors have? What liabilities do they also assume?
5. Do you think it is wise to forbid a director to be a salaried employee of the cooperative?
6. What do you consider as "broad operating policies" of a cooperative? Illustrate. What operating practices, for example, are determined by a manager? Illustrate.
7. What qualifications would you like to see in a good director? in a capable manager?

<sup>5</sup> For a discussion of the relationship of employees to cooperatives in European countries see Chapter XII of the Report on the Inquiry of Cooperative Enterprise in Europe 1937, Washington, D.C.



8. Do you believe it good policy to sell common stock carrying voting rights to employees in a farmers' cooperative processing plant? Explain.
9. Should a cooperative purchasing association take the place of a labor union for its employees who are also members of the cooperative?
10. Show how it may be "penny-wise and pound-foolish" to hire a manager at a low salary in preference to a better manager at a much higher salary.

## XIV

### *Financing Cooperative Marketing Associations*

*Unsound and inadequate financing has caused the suspension of numerous sales and purchasing cooperatives. Hence, the problem of adequate financing is one of serious import to all associations. Unlike private corporations, cooperatives organize freely on a non-stock or membership basis as well as on a capital stock basis. A nonstock association requires capital for its physical investment as well as its operations. Capital is required for the (1) organization of the association; (2) physical facilities, land, and equipment; (3) operations; and sometimes (4) for financing production on farms.*

*The three usual methods of financing cooperatives are through the sale of common stock, collection of membership fees, and borrowing from local banks. Other methods, such as selling preferred stock and bonds, deferring payment, making deductions from sales returns and issuing certificates of interest, using sight drafts, and creating subsidiary corporations are also practiced.*

*Shares of common stock are ordinarily of low par value (\$5, \$10), so that all producers may obtain the same. Seldom can all producers pay for the full value of the shares at the time of purchase, and therefore several plans are used for paying for the shares. Some associations require producers to buy shares of stock in proportion to the use which is to be made of the organization. Other associations place a limit on the number of shares any individual may hold. A nominal interest rate, if available, is paid on stock before patronage dividends are declared.*

*Bonds are not used extensively in financing cooperatives. Associations organized as nonstock associations and having need for a small amount of capital depend upon membership fees as a source of part of the capital funds needed. Many local associations have been financed at their inception by loans from local banks secured by the directors' notes. Since 1933, the Banks for Cooperatives have been important sources of loans.*



## CHAPTER XIV

### FINANCING COOPERATIVE MARKETING ASSOCIATIONS

Agriculture is predominantly a small unit industry carried on by those who generally do not have large capital funds. By the time the crops are ready for harvest or livestock is ready for slaughter, most farmers have utilized all their ready cash or the full amount of loans they were able to obtain, so that immediate sale has become a necessity on many farms. Yet, the consumers' and the processors' needs are not concentrated into the short periods in which the heavy marketings take place. The marketing of a large share of the crops and livestock products, therefore, must be financed by middlemen over many months of the year. Previous to 1921 there was a lack of adequate credit facilities to meet agricultural financing problems. This made it necessary for many farmers to unload their products even though they were disposed to hold them longer. The cooperatives which undertake the marketing tasks that independent middlemen have been performing must, therefore, assume the duties of financing. To meet these obligations farmers who organize the cooperatives must: (1) provide their own funds to conduct the business, and/or (2) arrange for and secure necessary credit, and (3) administer the finances—three obligations which any marketing agency must assume.

#### FUNDAMENTAL BASIS OF FINANCING

It is universally recognized that adequate financing of cooperatives is essential. To many, the financial soundness of a cooperative is the sole criterion of its success. Associations deeply in debt, with no reserves set aside, and with so-called "shoestring" financing methods are in a precarious situation. Of 1,500 associations that suspended business operations prior to 1926 more than a fourth gave unsound or inadequate financing

as the main or contributing cause. A sound financial program and status invite the backing of bankers, credit institutions, public officials, the public at large, and otherwise skeptical producers. It behooves associations to do a great deal to solicit this confidence. A weak financial position may easily increase the operating expenses of an association, may place the association in an unfavorable competitive position, and more than likely discourages the progressive farmers from joining an association.

Stanley Reed, former counsel to the Federal Farm Board, properly considered that the chief basis of the financial structure of a cooperative is the commodity which the cooperative handles. To quote,

In industry and commerce we have come to regard the capital with which a business is conducted as the basis upon which the financial structure is built. The scattered and relatively weak individual producer cannot subscribe adequate funds for a proper capital structure. . . . It is natural when a cooperative presents itself to the public that those interested in its financial affairs should look to its capital. If such persons look for the capital of a cooperative, it will not be found in its stock or its membership liability, but in the commodity which is delivered to the cooperative. This commodity becomes the capital of the cooperative and is responsible for its debts and other liabilities. It is rather immaterial whether a cooperative is created upon the capital stock or membership theory because subscribed capital will never be adequate to its needs. The commodity, however, can provide adequate capital to meet all financial requirements of any cooperative. If that is treated as the basis of credit, it is the soundest of enterprises because it has acquired this capital without any obligation to make return to those who have furnished it except the net amount that may be received from its sale, after the deduction of operating costs, reserves for credit and emergencies, and retains for the acquirement of facilities where needed.<sup>1</sup>

Thus, it is apparent that the financial commitments of most cooperatives rest upon a very desirable basis, namely, com-

<sup>1</sup> REED, STANLEY, *Financial Structure of Cooperatives*, Federal Farm Board *Circ.* 4, pp. 4-5, 1931. The remark of J. E. Wells, Jr., of the Farm Credit Administration, that "the statement often made that the commodity itself is the capital of the cooperative is to a degree correct" indicates that one must look to other things besides the commodity to determine the capital of a cooperative.

modities that are primarily necessities of life and for which ready markets exist at all times.

**Capital Stock or Nonstock.** The capital needs of cooperatives vary a great deal, depending mainly upon the nature of the marketing tasks to be performed. These needs determine very often, but not necessarily, the type of corporation that is set up, *i.e.*, *capital stock* or *nonstock* or a membership association as it is also called.<sup>2</sup> The laws of practically all states provide that either capital stock or nonstock organizations may be formed. In a capital stock corporation certificates of stock are issued to the stockholders or shareholders upon payment of a certain sum of money or its equivalent, and such certificates provide evidence of ownership in the corporation. A nonstock corporation obtains some capital for carrying on the business of marketing by issuing certificates of membership to those who pay membership fees or meet other requirements of membership. These certificates give evidence of the rights of the members in the corporation. Nonstock does not mean noncapital as is sometimes erroneously assumed. Indeed, the price of capital stock shares may be no higher than that of certificates of membership in a nonstock association. As will be apparent from the discussion which follows, the concept of capital stock and nonstock fundamentally relates to the type of legal business corporation created, rather than to the financial or capital needs of the corporation. It is primarily a legalistic concept—not a functional one. As a matter of fact many nonstock cooperatives require more capital than capital stock associations. Either form of organization may have much need for capital. Which form of organization is to be used can be answered best from an analysis of the particular problems to be solved. It does appear, however, that stockholders in most capital stock organizations have a feeling of greater financial responsibility than members in most nonstock companies.

<sup>2</sup> Oftentimes the phrase "nonstock, nonprofit" is used to designate this type of cooperative. It might be concluded by some that all capital stock associations are organized for profit whereas the nonstock are not. This is erroneous. The form of organization is no indication as to the method of operation. A capital stock organization as well as a nonstock association may be conducted on a nonprofit basis; or both may be run for profit (net savings).

### I. NEED FOR CAPITAL

Cooperatives require capital for: (1) organization, (2) physical facilities, (3) operations, and in some cases for (4) financing production on farms. These needs vary greatly according to the commodities handled, the type of associations (local or large-scale regional associations, bargaining or marketing organizations), the management policies relating to pooling, pricing, and selling of commodities, and the general practices followed in financing production.

**Organization Expense.** Before most cooperatives obtain a corporate standing, some expenses are incurred for organization purposes—in some cases very high fees have been paid to professional organizers. In other instances programs for expansion of membership call for significant outlays. Pre-organization expenses include such items as traveling expenses, hotel expenses, printing charges, postage, telegrams, legal fees, rentals of halls, fees for filing incorporation papers, costs of securing contract signers, obtaining membership fees, selling of stock, and other costs incident to organizing activities. At first these costs are usually paid for by the promoter, but later he is reimbursed by the association. The association frequently pays these expenses out of its membership fees or stock sales, or by deductions from the members' returns during the first year.<sup>3</sup> An audit of the Arkansas Cotton Growers' Cooperative Association in 1923 showed that its organization expenses were \$38,988, and its membership campaign expenses \$11,448. Members of the board of directors personally guaranteed notes for \$50,000 during the organization and initial operating period. These expenses were later paid for by deductions of 1 per cent from the growers' returns.<sup>4</sup>

Costs of engaging representatives of governmental agencies, who may assist in the organization, are borne usually by the government instead of the cooperative. The Agricultural Mar-

<sup>3</sup> In states where the statutory limitation upon promotion expenses is rigid, prospective associations have found it advantageous to sell memberships in an association for the purpose of organizing a cooperative. In addition shares of stock in the operating cooperative are sold.

<sup>4</sup> GILE, B. M., *The Status of Cooperative Cotton Marketing in Arkansas*, *Ark. Agr. Exp. Sta. Bul.* 245, p. 25, 1929.

keting Act, 1929, authorized the Federal Farm Board to make loans from the revolving fund to assist in "extending membership of the cooperative association applying for the loan by educating the producers of the commodity handled by the association in the advantages of cooperative marketing of that commodity." Apparently loans were not authorized for pre-organization expenses, but simply for extension of the membership. It was not mandatory that loans be made for expansion, and the board was conservative in granting such loans. Practically every agricultural experiment station is prepared to assist farmers without cost in organizing cooperative associations.

Before incorporation, the expenses of organization are legally obligations of the incorporators which should be assumed later by the corporation. In many cases the pre-organization expenses have been borne by general farm organizations which were directly responsible for starting cooperatives. The Land O'Lakes Creameries, Inc., received the pledge of a loan of \$1,000 from the Farm Bureau. In the years 1920-1922 the American Farm Bureau Federation was particularly active in organizing large-scale cooperative associations, such as the cooperative livestock commission firms, a fruit and vegetable commission house, and a sales agency for grain. The pre-organization expense and initial capital were frequently supplied by the parent organization but, after some time, such expenses were usually repaid by the operating company.

Pre-organization expenses can be kept at a minimum if groups of farmers do the work. Some state laws which limit the amount that can be spent for organization are designed in part to discourage "professional" organizers. In Oregon, for example, incorporated associations cannot expend more than 10 per cent of their paid-up capital stock for such purposes, and must refund total organization expenses out of any net profits before patronage dividends can be declared. In Wisconsin not more than 5 per cent of the paid-up capital stock or membership fees may be used for promotion expenses.

**Capital for Facilities.** One of the chief purposes of capital is to provide the land, buildings, machinery, and equipment which the cooperative requires. Capital for such purposes is called fixed, permanent, or long-time capital. In a cooperative creamery the fixed capital is invested in the site, buildings, churns,

vats, separator, boiler, and other durable equipment. A cooperative livestock shipping association may have no capital invested in fixed assets. If possible, members of an association should provide all of the capital necessary to acquire the fixed assets, but if this is impossible, they should borrow only such an amount as will not jeopardize the operations of the cooperative. The Farm Credit Act of 1935 permits the Farm Credit Administration to make facility loans (loans secured by physical assets) not in excess of 60 per cent of the appraised value of the security offered, indicating that the cooperative may borrow the full cost of the facility to be constructed or acquired, if it can furnish sufficient collateral. For a new cooperative this means that at least 40 per cent of the fixed assets must be provided by the members or from other sources since additional collateral would be lacking.

**Capital for Operations.** In addition to using capital for the fixed assets, cooperatives use capital for current operations. Funds are needed to pay wages, salaries, interest, rent, advances to growers, raw materials, supplies, freight charges, fuel, service fees, and other current expenses. Capital for such purposes is called "working," "circulating," or "short-time" capital. Quite often it is found that members provide sufficient funds to acquire fixed assets but have little left to finance current operations. If the fixed assets are owned, they may ordinarily be used as security to obtain funds for initial operations. If, however, the fixed assets are not fully owned by the members, greater difficulty is experienced in obtaining the original working capital. If the cooperative takes title to the products delivered by its members, it will be able to use these as collateral to secure a loan since the sale of the products will enable the association to repay the loan.

As to what proportion of its operating capital a cooperative association might reasonably expect to borrow, will depend upon a number of factors such as the character of the products handled, the degree to which the volume handled fluctuates from season to season, the necessity for storing the products, the trade channels employed, and the experience of the management. It would appear reasonable, however, that a new cooperative with obligations on its fixed assets have at least \$1 of its own operating funds for every \$4 which it expects to borrow. Some organizations which expect to store commodities for a considerable



period would perhaps need a larger proportion of their own funds to finance such undertakings before they could obtain assistance from lending agencies.<sup>5</sup>

J. E. Wells, Deputy Cooperative Bank Commissioner, also suggests this ratio when he writes,

If an association has working capital of its own equal to one-fourth of its normal total current liabilities, and if it is properly and soundly managed, it should be a good credit risk. This does not mean that it would be wise to loan three-fourths of the total amount of dollar value of current operation assets on an entirely unsecured basis. It usually means, however, in actual operations that the amount loaned on an unsecured basis does not exceed the amount of working capital owned by the association.<sup>6</sup>

The value of having sufficient working capital is readily seen. Cash discounts, quantity discounts, savings of interest payments, ability to take advantage of opportune purchases and to make repairs and alterations of plant and equipment when needed are some of the benefits obtained. To advance payments to members before the crops are sold by the cooperative requires large amounts of working capital.

**Capital for Financing Farm Production.** On account of the systems of farming in some sections of the country,<sup>7</sup> cooperatives find it necessary to extend credit to their members for production purposes, or else they experience difficulty in securing members or the members' crops for marketing. This is particularly true in the South among the cotton farmers. Landowners and "croppers," as many of the tenants are called, find it necessary to borrow heavily from one harvesttime to another. Most of the croppers buy their family needs at a local store by means of credit granted by local banks and merchants. Merchants grant credit, commonly called "store credit," on the condition that they receive a lien on the growing crop or a mortgage on

<sup>5</sup> STOKDYK, E. A., *The Financial Structure of Cooperatives*, "American Cooperation, 1934," p. 171, American Institute of Cooperation, Washington, D. C.

<sup>6</sup> WELLS, J. E., *Financing Current Assets*, *News for Farmer Cooperatives*, vol. 2, no. 1, p. 6, April, 1935.

<sup>7</sup> For a detailed discussion of Agricultural Credit Corporations Affiliated with Cotton Cooperative Marketing Associations, by William H. Rowe, see *U. S. Dept. Agr. Tech. Bul.* 322, September, 1932.

the land itself if the customer is a landowner.<sup>8</sup> The grower obligates himself to sell to the merchant, or to a buyer named by the merchant, and may be restrained from delivering his cotton to his cooperative. Such restriction by the creditors is easily understood when it is realized that often the 60 to 65 per cent advance payment (in 1929 raised to 90 per cent by the Federal Farm Board) on cotton placed in seasonal pools was insufficient to pay the loans, that the possibilities of making a profit on marketing the cotton were considered in determining the interest rate on the loans, and that some creditors opposed the cooperative marketing movement.

Store credit is expensive—rates ranging from 12 to 40 per cent per annum are not uncommon. The high interest rates paid by southern farmers during the years 1927–1930 are recorded in Table XII prepared by Rowe.

These high rates, together with the sheer difficulties of obtaining loans from banks and merchants and the utter lack of latitude in market selection by the debtor-farmers, made it expedient for the cotton cooperatives to provide production credit or credit to finance the delivery of mortgaged cotton. From 1924 to 1931 seventeen subsidiary credit corporations were organized by cotton cooperatives. Only half of this number were operating in 1932, the others had either failed or ceased operations.<sup>9</sup>

Production credit for feeders of livestock is also provided by credit corporations organized by cooperative associations selling

<sup>8</sup> In one district in Arkansas in 1926, 83 per cent of the mercantile credit was secured by means of a chattel mortgage on all crops, livestock, and equipment, 9 per cent by a lien on the cotton crop, 2 per cent by a mortgage on real estate, 1 per cent by a chattel mortgage on work stock, 4 per cent on open account, and 1 per cent on unendorsed note. GILE, B. M., and A. N. MOORE, *Farm Credit in a Plantation and an Upland Cotton District in Arkansas*, *Ark. Agr. Exp. Sta. Bul.* 228, p. 39, 1928.

<sup>9</sup> There are several ways in which agricultural credit corporations can be set up: (1) as an affiliate of a local bank; (2) as an affiliate of a group of banks serving an agricultural area; (3) by a group of farmers within a given community; (4) as a subsidiary to a cooperative buying and marketing association.

REED, STANLEY, *op. cit.*, p. 15, has the following advice to give, “. . . it seems proper to say that credit corporations are an extremely hazardous angle of the financial structure. Stay away from them if you possibly can without losing your business.”

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livestock. Extending credit to livestock feeders by cattle loan companies is an old practice. It became necessary for cooperative sales associations to provide a service similar or at least equal to that of competitors if they wished to receive shipments of fattened cattle, sheep, and hogs. The National Livestock Marketing Association has a subsidiary financing company known as the National Feeder and Finance Organization, which

TABLE XII.—COST OF CREDIT ON A PER ANNUM BASIS IN SOUTHERN STATES,\* 1927-1930

State	Cash credit, per cent			Merchant credit, per cent		
	All	Owner	Tenant	All	Owner	Tenant
North Carolina †.....	7.7	7.7	7.9	25.5	27.7	20.9
South Carolina †.....	9.6	8.8	10.5	31.6	32.6	30.4
Georgia †.....	11.5	8.6	16.0	26.3	27.1	26.0
Arkansas						
Craighead County †.....	8.7	8.7	8.7	17.7	13.5	18.9
Alzheimer District.....	8.8	7.7	10.0	....	20.0	41.5
Rison District.....	10.0	10.0	....	....	18.0	20.0
Louisiana.....	8.1	....	....	16.6	....	....
Oklahoma †.....	11.4	11.0	11.6	34.8	18.4	38.5
Texas.....	9.4	....	....	27.0	....	....

NOTE: Data are averages obtained from eight separate studies made by the sampling method between 1927 and 1930. Reports of these studies were published by the agricultural experiment stations of the various states, the Bureau of Agricultural Economics cooperating in the preparation of all except those in Louisiana and Texas. *N. C. Bul.* 270; *S. C. Bul.* 282; *Ga. Bul.* 153; *Ark. Bul.* 233 and 228; *La. Bul.* 208; *Okla. Bul.* 198; and *Texas Bul.* 351.

\* From ROWE, WILLIAM H., Agricultural Credit Corporations Affiliated with Cotton Cooperative Marketing Associations, *U. S. Dept. Agr. Tech. Bul.* 322, Table 2, 1932.

† Averages weighted according to the size of the loans.

finances farmers' feeding and finishing operations. In Washington the Wenoka Agricultural Credit Corporation was established for the purpose of making production and marketing credit available to fruit growers who are members of the Wenatchee-Okanogan Cooperative Federation, or to members of its 13 affiliated local cooperatives. This indicates somewhat the diversity of needs of production credit.

**Amounts of Capital Needed by Local Associations.** *Fixed Capital.* The range in capital requirements of local associations is from none to thousands of dollars, depending upon (1) the kind of commodity which is marketed, (2) the character of services rendered, and (3) the willingness of patrons to wait for their payment. It also depends upon whether the association leases existing facilities or whether it is obligated to purchase or erect plants. A farmers' livestock shipping association ordinarily does not require any capital outlay. The local stockyards' facilities are most frequently furnished by the railroad company, and payment for the livestock, freight charges, manager's fees, and other charges is made after the stock is sold. With but few exceptions local collective bargaining associations require no capital investments. Their functions of bargaining for a price and of performing auxiliary operations such as checking accuracy of weights, grades, and tests do not require financial outlays. Many local associations, however, need capital equipment in order to perform marketing functions. Local grain elevators, packing houses, cheese factories, creameries, gins, canning plants, equipment, warehouses, poultry dressing plants, and processing plants represent significant outlays of permanent or fixed capital. Such plants vary in cost from several hundred to more than a hundred thousand dollars.

The investments of fixed capital by many local cooperative associations are shown in Table XIII.

These are relatively small amounts, but to many farmers with limited incomes and cash savings they represent substantial investments. Very often manufacturers install equipment upon receipt of a small down payment followed by partial payments after operations are under way.

*Working Capital.* Just as there are varying demands for permanent capital by local associations, there are also wide ranges in the demands for working capital. A livestock shipping association, a collective bargaining association selling fluid milk, fruit, or sugar beets, or a cooperative cotton ginning association needs very little ready cash or credit to carry on its operations. The major expenses are paid for *after* the commodity is sold and the deduction from sales is made. Few store products a long time. Thus, no large fund is needed to defray operating costs that arise prior to the sale of the product. On the other

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hand, a local grain elevator that purchases grain, or a potato warehouse that buys potatoes, or a creamery that pays cash for butterfat, or a packing house that buys fruit outright needs ready funds to defray purchases and expenses. If patrons are willing to wait for their payments until the products are sold by the cooperative, the amount of working capital needed at all times is reduced. It is evident that the length of the pooling period,

**TABLE XIII.—APPROXIMATE VALUE OF LOCAL PLANTS**

Cooperative creameries .....	\$25,000-\$50,000
Cooperative cheese factories.....	2,000- 8,000
Cooperative grain elevator.....	10,000- 20,000*
Cooperative potato warehouse.....	1,000- 5,000
Cooperative fruit packing house.....	3,000- 50,000
Cooperative cotton gin.....	3,000- 15,000
Cooperative tobacco warehouses.....	1,000- 3,000

\* KNOTHER, J. J., writes in "American Cooperation, 1929," p. 531, The American Institute of Cooperation, Washington, D. C., "The cost of construction of a country elevator varies according to type, arrangement, capacity and equipment. The common studded wood and metal-covered elevator and all concrete and steel elevator, with modern equipment consisting of truck scales, automatic weighing and loading-out scales, automatic truck dump, fast elevating belt, leg and boot, cleaner, electric power, office, etc., will cost per the following schedule:

Capacity, bushels	Wood and metal	Concrete
10,000	\$ 9,000	\$12,000
15,000	10,000	13,500
20,000	11,000	14,500
25,000	12,000	16,000
30,000	13,000	17,000
35,000	14,000	18,000
40,000	15,500	20,000
50,000	18,000	23,000

**AUTHORS' NOTE:** These were predepression cost figures and do not include costs of land for most generally elevators are built on the railroads' right of way.

which will determine whether advance payments are made, influences the amount of credit required. It is well that an association requiring varying amounts of working capital should have an amount sufficient to meet normal or average requirements, and be able to borrow funds to meet peak load needs. The lessons learned from experience together with the advice of reputable bankers are valuable in solving this problem.

No hard and fast rule can be laid down as to the amount of capital which a cooperative needs and as to its division into fixed and circulating capital. The present and future needs of the company must be considered as well as the principles of organization and operating policies. "The test of the amount of capital which an association requires is the amount of capital which it can use efficiently."<sup>10</sup> To have an amount so that operations are not cramped and yet not have idle funds or excessive investments which are a constant burdensome cost is the goal to be sought.

The varying needs of capital, fixed and circulating, as well as the ratio which the capital bears to the volume of business transacted by different commodity organizations, are indicated in the following table.

TABLE XIV.—CAPITAL INVESTMENTS IN DIFFERENT TYPES OF MICHIGAN LOCAL COOPERATIVE ASSOCIATIONS\* 1923-1924

Type of commodity handled	Total capital per association	Fixed capital per average association	Circulating capital per average association	Ratio of circulating to total capital, %	Average volume of business per association	Ratio of total capital to volume of business
Grain.....	\$35,400	\$18,400	\$17,000	48.0	\$155,500	1 to 4
Livestock.....	8,500	1,400	2,100	66.7	108,400	1 to 31
Dairy products...	21,800	12,200	9,600	44.0	149,700	1 to 7
Potato.....	12,200	7,100	5,100	41.8	71,000	1 to 6
Fruit.....	33,000	19,300	13,700	41.5	157,700	1 to 5
Store.....	39,300	13,100	26,200	66.7	111,100	1 to 3
Supply.....	11,500	4,500	7,000	60.8	45,700	1 to 4
Simple average.	\$22,400	\$10,857	\$11,543	51.5	\$114,157	1 to 5

\* Adapted from data in Tables XIX and XXII, CLAYTON, C. F., and J. T. HORNER, *Farmers' Cooperative Buying and Selling Organizations in Michigan*, *Mich. Agr. Exp. Sta. Special Bul.* 171, p. 60, 1928, with some changes made by the authors. The total capital per association is a summation of the average of the fixed and circulating capital in columns three and four and varies from that shown in the Michigan bulletin.

Associations marketing grain, fruit, and dairy products have several times as much capital as those handling livestock and potatoes. The associations listed as marketing livestock also

<sup>10</sup> So write C. F. Clayton and J. T. Horner in *Farmers' Cooperative Buying and Selling Organizations in Michigan*, *Mich. Agr. Exp. Sta. Special Bul.* 171, p. 60, 1928.

quite generally conduct a supply business for which the bulk of capital is used. Like the dairy cooperatives, the cooperative elevators have considerable fixed capital invested in buildings and equipment, but unlike the dairy cooperatives, which do not generally make cash purchases, they have fairly large amounts of working capital which is essential for purchasing grain. Fruit marketing associations also have large capital investments, due partly to the building facilities which are needed and partly to the supply business which is often conducted for the growers. Although potato marketing associations also need warehouse facilities which represent investments of fixed capital, still these facilities are not very costly. Nor is there a need for much circulating capital since some potatoes are pooled for a short time and require no advance payment, some are handled on a joint account basis with terminal commission firms, and some are bought for cash upon delivery.

The ratios of circulating capital to total capital indicate the division of these funds among typical local cooperative associations, and the ratio of total capital to volume of business transacted shows the utilization of capital in different types of organizations. These ratios do not indicate, however, the efficiency with which the capital is utilized, but merely point out differences between numerous organizations. Analyses of associations handling the same commodities under similar circumstances must be made to measure the comparative efficiency of use.

**Capital Needs of Large-scale Associations.** *Permanent Capital.* The capital requirements of a large-scale association selling in terminal markets, like those of a local association, also depend upon the characteristics of the commodity, the nature of marketing services which are performed, and the willingness of members to wait for their payments, or the pooling arrangements. Processing plants, warehousing facilities, machinery, and loading and unloading equipment may represent investments from a few thousand to millions of dollars. To mention merely a few fixed investments of some large-scale cooperatives:<sup>11</sup> the per-

<sup>11</sup> Terminal elevators, according to J. J. Knight, "American Cooperation, 1929," p. 530, The American Institute of Cooperation, Washington, D. C., vary in cost according to geographical location and handling equipment. Elevators of 100,000 bushel capacity cost approximately \$60,000, and those of 5,000,000 bushel capacity as much as \$1,200,000.

manent assets of Land O'Lakes Creameries, Incorporated, on Dec. 31, 1936, were \$1,688,602, and the Mid-South Cotton Growers' Association in 1937 had an investment of \$121,255 in a new office building and \$11,952 in furniture and fixtures.<sup>12</sup> The amount of the investment also hinges upon the character of services which the central organization performs. A cooperative commission firm that receives fruit and vegetables, poultry and eggs, butter, or livestock has a small amount invested in permanent assets. More often than not office space is all that is necessary to conduct the business of the company. The Pure Milk Products Cooperative, a large-scale cooperative bargaining association of condensery patrons, like many other collective bargaining associations, simply rents office quarters.

Whether the association is a centralized or a federated type of organization also bears upon its capital needs, for under the former type the central organization must provide the local warehousing, packing, or processing plants, whereas under the latter type it must furnish only the central office and terminal facilities. If facilities can be leased instead of purchased, the initial demands for capital can be greatly reduced.

*Working Capital.* Performing the functions ordinarily assumed by middlemen of the wholesale trade, the large-scale cooperative requires large amounts of working capital. Sales in carload lots, large appropriations for advertising, necessary storing of substantial portions of entire crops, granting of credit to jobbers and retailers for 15-day, 30-day, or 60-day periods, necessity of making fairly large advances to shippers long before the products are sold—all these demand that the large-scale cooperative ordinarily have a great deal of working capital. Other large-scale central organizations require little working capital inasmuch as sales are made soon after the product is received, and the cash is forwarded at once to the shipper. A cooperative commission firm receiving shipments on consignment sells the produce or livestock immediately, receives the cash from the buyer, and remits promptly to the shippers. That it requires a negligible amount of working capital for the total

<sup>12</sup> For the financial investments in a large number of large-scale cooperatives in the state of Washington, see E. F. Dummeier, Financing Cooperative Marketing of Farm Products in Washington, *Wash. Agr. Exp. Sta. Bul.* 322, October, 1935.



volume of business transacted is illustrated by the record of one firm which in 1927 sold livestock valued at \$29,566,355. Its current working capital was \$88,687, and other working capital such as deferred charges and investments amounted to \$33,543. The total net fixed capital as represented by automobiles, a horse, furniture, and fixtures was only \$12,824. On the other hand, a fruit marketing association that sold \$3,198,200 worth of fruit in one year reported at the close of the crop year working capital (current assets) of \$92,120 in cash and \$34,369 in accounts receivable. It had fixed assets of \$23,486. The large differences in these amounts are explained by the commodities handled, the sales policies used, and numerous other factors.<sup>13</sup>

## II. METHODS OF PROVIDING CAPITAL

Numerous methods are open to cooperative associations to secure capital. The three most commonly used are: (1) sale of common stock, (2) collection of membership fees, and (3) borrowing from local banks. But in addition to these a dozen other plans are followed with most associations using several methods at the same time.

In some respects cooperatives experience greater difficulties in obtaining capital than private organizations and in others greater ease. Some credit institutions are not sympathetic toward

<sup>13</sup> The manager of a large cotton cooperative which handled about one-third of the cotton produced in Oklahoma gives some idea of the financing problem for the 1928 crop in the following statement. "For weeks at a time, during the past season, the Oklahoma Cotton Growers' Association found it necessary to borrow from \$500,000 to \$800,000 per day to take care of the drafts issued to our members as an advance on their cotton. We found it almost necessary to arrange for half a million dollars every morning before breakfast in order to take care of the situation, and after our limit was reached with the Intermediate Credit Bank, I found it necessary, on many occasions, to get up earlier than usual in order to make arrangements for the necessary funds to pay these drafts before the hour of closing of our custodian bank." MORLEY, SAM L., *Commodity Credit Needs for Cotton*, "American Cooperation 1929," p. 572, American Institute of Cooperation, Washington, D. C.

For a good discussion of the financing needs for various commodities, see *Cooperative Marketing*, Senate Document 95, 70th Congress, 1st Session, a Letter from the Chairman of the Federal Trade Commission, Chap. 14. Some of the illustrations of particular financing methods cited in this and the following chapter are mentioned in this document.

farmers' cooperative marketing companies and hence will not lend to them except on a most conservative basis. In other instances cooperatives have not shown a long enough record of performance to invite approval and approbation of bankers. The cooperative with its inherent purpose to conduct marketing operations for the benefit of its patron-members, rather than for those who invest in it, has failed to arouse much interest on the part of the investing public. State and federal laws that limit the dividends upon stock strengthened this general lack of interest. The fact that cooperatives are organized by farmers and for farmers, who as a class are known to have limited means, creates further need for various methods of financing. A member, that is, a stockholder or a holder of a membership certificate, must not only have the amount of the fee, but in most instances must be a bona fide producer as well. This too limits the procurement of capital to a restricted class. Hence, numerous methods are employed to overcome the varied difficulties inherent in financing.

Cooperatives sometimes experience advantages over private companies in financing as during 1929-1932 when cooperatives only could borrow at unusually low rates of interest from the Federal Farm Board. Furthermore, only cooperative associations and not private companies can borrow from the Intermediate Credit Banks and Farm Credit Administration and become exempt from the payment of federal income taxes.

The capital needs of cooperatives are provided in the following ways:

**I. Direct methods**

1. Sale of shares of common stock
2. Collection of membership fees
3. Sale of preferred stock
4. Sale of bonds
5. Requiring members to execute promissory notes to the association
6. Borrowing
  - a. From members and nonmembers
  - b. From central cooperative organizations
  - c. From existing marketing agencies—such as factors, commission houses
  - d. From local banks; from large commercial banks
  - e. From government agencies

**II. Indirect methods**

7. Deferring payments to patrons

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8. Deduction of definite amounts from members' returns
  - a. Issuing certificates of interest—revolving fund plan
9. Accumulation of surpluses, reserves, sinking funds
10. System of assessments, so much per cow, or so much per acre
11. Use of sight drafts
12. Use of trade acceptances
13. Conducting joint-account dealings with central market operators
14. Creating subsidiary companies and selling stock in the same
15. Delaying payments of bills

Not all of these methods are open to all types of cooperatives, nor are they of equal importance or practicability. The use of particular methods listed above may be optional with an association in some cases, but mandatory in others.<sup>14</sup> Each of the methods will be discussed in the subsequent pages. It will be noted that the first six methods are classified as *direct methods* and the others as *indirect methods*. The distinction is an arbitrary one and signifies whether a direct payment or "line" of credit is made to the association, or whether the capital or credit needs are obtained through indirection, *i.e.*, without the actual direct outlay of any sums of money or credit.

<sup>14</sup> To illustrate the methods of obtaining capital, consider the cases of typical cooperatives in Virginia. The methods followed by 70 cooperatives in Virginia in obtaining *permanent* capital were:

Capital	Number of associations	Capital	Number of associations
Capital stock.....	25	Certificates of indebtedness	5
Preferred stock.....	5	Membership dues.....	4
Donated capital.....	1	No permanent capital....	34
Mortgage on real estate....	8	(Some used more than one method)	
Demand notes of directors..	2		

*Working* capital was secured in the following manner: By accounts payable—28 associations; notes other than to directors—15; demand notes of directors—9. TALBOT, RANSOM C., *An Economic Study of Cooperative Buying and Selling among Farmers in Virginia, Va. Agr. Exp. Sta. Bul.* 286, p. 20, 1932.

Forty-six per cent of the entire capital of cooperative grain elevators in Minnesota in 1922-1923 was provided by *other* sources than the sale of common stock, *Minn. Agr. Exp. Sta. Bul.* 224, p. 68, 1925.

Cooperative marketing associations obtain capital funds chiefly from four sources: (1) members, (2) nonmember investors, (3) credit agencies, and (4) business operations. Occasionally gifts and donations augment the capital derived from these primary sources. Local cooperatives also receive funds from the central organization of large-scale cooperatives with which they are affiliated. These are ordinarily obtained on a loan basis. The sources of finances for cooperatives will be discussed in the following chapter.

**1. Common Stock.** Organizing associations on a capital stock basis is one of the oldest methods and one very common for associations that market potatoes, cheese, butter, and other dairy products, as well as for those that warehouse and process dried fruits, store cotton, or ship grain. The sale of common stock to bona fide producers of the commodities handled is the method usually adopted in capital stock organizations, although other plans are also used. The capital stock of a corporation consists of common stock or of common and preferred stock.<sup>15</sup> Bonds are not a part of the capital stock of a company.

The capital stock of a cooperative, as of any incorporated private business concern, is an approximate measure of the funds invested in the fixed assets and circulating capital of the company. After the entire capital needs of the association are estimated in advance, it is determined how much of these needs can or should be provided by the sale of common stock, preferred stock, bonds, and by other methods. The amounts decided upon for each type of investment are then subdivided into numbers of shares of stated par values. Thus, a cooperative may desire to obtain \$10,000 through the sale of 1,000 shares of common stock at \$10 a share, possibly \$5,000 through the sale

<sup>15</sup> In Cook on "Corporations" it is stated: "By *common stock* is meant that stock which entitles the owners of it to an equal prorata division of profits, if any there be; one stockholder or class of stockholders having no advantage, priority, or preference over any other stockholder or class of stockholders in the division. By *preferred stock* is meant stock which entitles its owners to dividends out of the net profits before or in preference to the holders of the common stock. Common stock entitles the owner to prorata dividends equally with all other holders of the stock except preferred stockholders; while preferred stock entitles the owner to a priority in dividends." COOK, WILLIAM W., "A Treatise on the Law of Corporations," 8th ed., Vol. I, p. 76, Baker Voorhis and Company, New York, 1923.

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of 500 shares of preferred stock at \$10 a share, and another \$5,000 through loans. Or, it may decide to sell 2,000 shares of common stock at \$10 a share to obtain \$20,000 without resorting to any other methods. No-par stock, such as is issued by many large private corporations in America and sold upon the exchanges of the country, is not commonly issued by cooperative corporations.

*Extent of Use of Common Stock.* In order that the extent of capital stock organizations among cooperatives may be visualized, the following table, taken from the Federal Trade Commission's report on Cooperative Marketing 1928 is included.

TABLE XV.—NUMBER OF COOPERATIVE MARKETING ASSOCIATIONS ORGANIZED AS CAPITAL STOCK OR NONSTOCK\*

Commodity	Number associations reporting	Number of		Per cent of	
		Stock	Non-stock	Stock	Non-stock
Cotton.....	47	7	40	15.0	85.0
Dairy products:					
Creameries.....	742	682	60	92.0	8.0
Cheese factories.....	233	196	37	84.0	15.9
Whole-milk marketing.....	68	40	28	58.8	41.2
Fruits and vegetables.....	532	214	318	40.2	59.8
Grain.....	612	585	27	95.6	4.4
Livestock.....	716	100	616	14.0	86.0
Poultry and poultry products.....	59	23	36	39.0	61.0
Tobacco.....	12	....	12	....	100.0
Wool.....	76	8	68	19.5	89.5
Nuts.....	41	11	30	26.8	73.2
All other.....	34	9	25	26.5	73.5
<b>Total.....</b>	<b>3172</b>	<b>1875</b>	<b>1297</b>	<b>59.1</b>	<b>40.9</b>

\* Senate Document 95, 70th Congress, 1st Session, Cooperative Marketing, letter from the Chairman of the Federal Trade Commission, p. 248, 1928.

Of the 3,172 associations reporting, 3,015 were local associations. In the local associations organized on a capital stock basis, the sale of common stock is practically the only direct method used to obtain funds.<sup>18</sup>

<sup>18</sup> In Virginia there were in 1931, 25 capital stock and 45 nonstock associations, Talbot, *op. cit.*, pp. 19-20. In New York, of 166 incorporated selling

*Methods of Paying for Common Stock.* The capitalization of a capital stock company is stated in the incorporation papers. In very many instances this amount is not fully paid in nor fully subscribed. A subscriber is usually a person who has agreed to purchase stock from the corporation. After the subscription is made for the stock, it may be paid for in several ways: (1) outright payment for the full value, (2) partial payment basis, (3) deductions from returns, or (4) applying patronage refunds. In addition to the direct payment for stock with cash, it may be paid for with property or labor. Since there are statutory restrictions relative to paying for stock in other ways than cash, it is necessary to examine and follow the laws of the state in which the cooperative is incorporated. The corporation laws of states must also be looked into to ascertain the minimum amount of stock that must be subscribed and also the amount which must be paid in before operations can commence or dealings with other corporations are permitted. Corporation laws in most states provide that 50 per cent of the capital stock must be subscribed and 20 per cent must be paid in.

and purchasing associations active in 1930, 79 were incorporated as non-stock companies, and 87 as capital stock. F. A. Harper, *Cooperative Purchasing and Marketing Organizations in New York State, Cornell Univ. Bul.* 544, p. 10, 1932. In 1925 there were in Michigan 203 associations organized originally as capital stock cooperatives, and 283 as nonstock. The types used for associations handling different commodities are shown in the following table:

Type	Number of associations	
	Capital stock	Nonstock
Grain.....	69	59
Livestock.....	29	109
Dairy products.....	54	16
Potato.....	10	69
Fruit.....	9	13
Store.....	32	8
Supply.....	...	9
Total.....	203	283

CLAYTON and HORNER, *op. cit.*, p. 21.

*Value of Shares of Stock.* The value of shares of common stock is by no means uniform in different associations; variations from \$1 to \$100 a share are to be found.<sup>17</sup> A common denomination is \$10, but \$25 and \$50 shares are also commonly issued. Consideration must be given to the financial standing of the producers to whom the common stock is sold in determining its par value. In poor communities a real hardship would be imposed upon the farmers if the shares of stock in cooperatives were to have a high par value, whereas among well-established and wealthy farmers such would not be the case. If a cooperative requires but a small amount of capital stock and hundreds of farmers wish to buy shares to attain membership, it will be necessary to issue shares of small denominations and limit the number which any one person may own. Whether the stock of the cooperative is sold to farmers directly, as in local or centralized associations, or whether the stock is sold to other cooperative associations as in federations and national marketing associations<sup>18</sup> must also be considered. When stock is sold to other cooperatives, shares of high par value can be issued with little difficulty.

*Prorata Basis of Stock Sales.* In quite a number of cooperative associations, the distribution of shares of stock is upon a prorata basis according to the use that members will make of the cooperative. If a creamery is to be built, a fruit warehouse constructed, or a canning plant erected, the prospective patrons of the company are asked to take out stock in proportion to the use which they will make of the association. Possibly for every 10 cows, one \$25 share is to be bought in the creamery association, for every 5 acres of apple trees one \$10 share in the fruit association, and for every 100 cherry trees one share of stock in the cooperative canning company. These minimum amounts may be exceeded at the wish of the producer if the association's bylaws permit it. A few illustrations follow.

<sup>17</sup> By value here is meant the par value. The book value and sales value of stock of any corporation theoretically stay the same or differ from the par value as soon as operations commence. Inasmuch as cooperatives wish to confine the sale of their stock to their members, they do not list the stock for sale on the stock exchanges as do private corporations.

<sup>18</sup> In case the stock is sold to other cooperative associations, the association cannot be exempted from paying federal income tax.

In the organization of the locals in the California Fruit Growers Exchange,

As a rule, a certain number of shares is issued to each member for each acre of "bearing grove" that he owns. In some organizations the investment of the members in the stock of the association is as high as \$125 per acre; in others it is \$10 per acre or less. A representative figure is \$50 per acre. In practically all cases the investment of each member is in proportion to the acreage of citrus fruit which he cultivates, or the quantity of fruit which he produces. If the stock of the association is not distributed on an acreage basis, one share may be issued for each 10 or 20 trees. In a few instances, the members subscribe for a certain number of shares per 100 boxes of fruit shipped, and the investment of each grower is maintained in proportion to his shipments by means of a revolving fund.<sup>19</sup>

The National Livestock Marketing Association requires each stockholder to buy one share of common stock for each 10 single decks of livestock handled during the calendar year preceding stock purchase.

In the Twin City Milk Producers' Association, each producer selling through the association must subscribe for one share of stock for each four cows owned and payment is made through a 5 per cent deduction from each month's milk check. In the Washington Cooperative Egg and Poultry Association, Seattle, common stock is issued to members for the amount of deductions made from their sales returns. As the revolving fund so created is increased to the desired amount, common stock issued in previous years is called in and retired. In this manner members contribute capital in accordance with their patronage and only active members are retained in the association.

The above requirements comply with the democratic principles of cooperative marketing. It is logical to expect that the financial risks should bear some relation to the use that is to be made of the organization. To have only a few members supply the capital for an organization used by many for their personal gain is scarcely in accordance with the idea of collectivism. It was for this reason that some of the earliest cooperators conceived the idea of proportioning the sale of stock with reference to the

<sup>19</sup> MCKAY, A. W., and W. MACKENZIE STEVENS, Organization and Development of a Cooperative Citrus-fruit Marketing Agency, *U. S. Dept. Agr. Bul.* 1237, p. 17, 1924.



use to be made of the company. Although the majority of associations do not live up to this policy, it has distinct advantages.

*Limitation of Stock Ownership.* A cooperative may set the maximum, as well as the minimum, number of shares which any person may own.<sup>20</sup> The purpose of this is threefold: (1) to prevent the concentration of shares in the hands of any one individual, (2) to effect a wide distribution of the shares, (3) to forestall the possibility of using the cooperative simply as a place to invest funds, making the association an investment institution rather than a service agency for which it was designed. The early Rochdale pioneers set down as an important precept the limitation of shares to any one person. The fear of capitalistic control and the operation of the association for the financial interests of the investors, rather than for the best interests of the patron-members, underlaid this wise policy. Although the one-man, one-vote feature of cooperative organization may fully protect the mass of members from the selfish interests of a few large stockholders, yet there is the inherent fear that "he who holds the purse strings rules the organization." The Farmers Cooperative (Grain) Commission Company of Kansas permits each local elevator to hold not more than fifty shares in the over-head organization, and the California Fruit Exchange allows but two shares to a member, to cite two illustrations.

Limitation of shares has its handicaps as well as advantages. (1) It may result in sales of too few shares to meet the financial needs of the association. (2) Farmers with no ulterior motives may be prevented from giving full expression to their endorsement and financial backing of the cooperative. (3) It may destroy some of the enthusiastic support which accompanies large financial investment in a concern. There is certainly a correla-

<sup>20</sup> For example, in Minnesota "out of 50 elevators, two limit the ownership of individual stockholders to two shares; three, to 4 shares; one, to 5 shares; three, to 8 shares; eleven, to 10 shares; five, to 15 shares; one, to 16 shares; four, to 20 shares; two, to 40 shares; while three simply reported that the number of shares was "limited"; and fifteen have no limit." PRICE, H. BRUCE, and CHARLES M. ARTHUR, *Management Problems of Farmers' Elevators*, *Minn. Agr. Exp. Sta. Bul. 224*, p. 65, 1925.

The Bingham Cooperative Marketing Act includes a provision limiting the ownership of common stock to one-twentieth of the common stock of the association by any one stockholder.

tion between the amount of interest one has in the welfare of a company and the amount of money invested in it. Some of this extra interest, if it may be called such, is damped by restriction of the number of shares one person may own.

It is the authors' conviction that the policy of limiting the number of shares to any individual is a good one, even though the problem of selling stock is not one of oversubscription, but undersubscription. In many associations it is difficult to induce members to take out the minimum number of shares of stock without worrying about the maximum. The handicaps mentioned in the paragraph above can be met very largely by the issuance of preferred stock or by borrowing. A plan of stock limitation thwarts the designs of unscrupulous investors and gives double assurance that the cardinal principle of cooperation, control by the masses for their interests, will be upheld.

*Interest Paid to Stockholders Precedes Payment of Patronage Dividends.* The primary purpose of the sale of common stock is to provide all or part of the fixed and circulating capital. It is not for the purpose of creating a corporation as a good investment medium, although it often becomes such. In a private corporation the returns upon the common stock are called dividends, payable annually, semi-annually, or quarterly, in varying amounts depending upon the profits of the company and other prior claims and appropriations. The common stockholders are the residual claimants of all unappropriated net profits. In a cooperative corporation, the member-patrons, not the common stockholders, are the residual claimants, and they receive patronage dividends. The common stockholders of a cooperative are, in a sense, comparable to preferred stockholders in that they receive a nominal *interest* payment upon their stockholdings instead of dividends. (Members sometimes call these interest payments dividends, but since their amount is usually a fixed percentage comparable to current interest rates on notes, mortgages, and the like, and not a fluctuating amount in proportion to net profits, it is better to call these payments interest.) The amount of money needed to pay the interest on the common stock is set aside before the patronage dividend is determined.

In most states the cooperative laws fix the maximum interest which directors may vote to pay to common stockholders, and

under the Capper-Volstead Act the interest payment on common stock cannot exceed 8 per cent, if voting is not limited to one man, one vote. A nominal interest payment is essential to attract investments. If interest is not paid, rumors concerning the cooperative's solvency may be started. If none is ever declared, those who have invested may try to dispose of their stock while others will be reluctant to invest. Important exceptions are to be found, but such exceptions do not alter the general observation.

*Advantages of Paying Nominal Interest.* The advantages of paying a nominal, going rate of interest on common stock are: (1) It forestalls use of the cooperative as a lucrative investment medium; (2) it permits a greater amount to be paid as patronage dividends to the member patrons for whom the association is organized, or, if patronage dividends are not paid, it allows the association to operate on a narrower margin, or appropriate more to the reserve fund; (3) it dispels the idea that the cooperative is a profit-making institution for its investors, and in this manner may assuage the prejudices of the court or the threats of the income tax collector. It gives assurance to public officials and others that the association is organized and conducted strictly on a cooperative basis. At times, however, such nominal interest payments may act as a deterrent and lessen the value of the shares of stock of the association. Knowing that in "good times" only a nominal interest is paid and in "hard times" no interest whatsoever may be forthcoming, producers and others may refuse to purchase stock in a cooperative. It is recognized that the policy of restriction of interest payments to a nominal current rate will add to the solidarity and stability of the association and that it is a good policy to follow. When one considers that the average dividends on the stock of hundreds of leading American corporations in normal periods do not usually exceed 6 per cent per annum, a rate most often paid on stock in cooperatives, the investment in cooperatives from an income point of view is relatively attractive.

*Legal Relationships.* The relation of a common stockholder to the corporation is that of an owner with a proprietary interest. He is neither a lender nor a creditor as is a bondholder. His legal status is distinctly different from that of a bondholder or other lender. The cooperative may restrict the transfer of stock

so as to prevent nonproducers from holding it, provided statutory authority exists in the state. Even in the absence of specific statutory authorization courts have upheld restrictions on the transfer of stock.<sup>21</sup> The cooperative may declare in its bylaws or on the face of the stock certificate that it retains the priority right to purchase any shares of stock which any member wishes to sell. If, after due notice, the cooperative fails to take up the stock offered for sale, the owner has the constitutional right to sell to anyone. The amount of capital stock paid in determines the legal indebtedness which the directors may authorize. Some common stock which does not grant voting privileges may be issued. Ordinarily, however, common stockholders have rights (a) relating to management, the selection of directors, and voting privileges, and (b) relating to earnings of the cooperative and to assets of the company.

**2. Collection of Membership Fees.** It has already been pointed out that some associations are organized on a nonstock basis, and that the members are given certificates of membership upon payment of a membership fee. The sale of certificates of membership may either supply all the capital which is needed or it may fall far short. Indeed, the latter is usually the case, for in many associations the collection of membership fees is considered merely an incidental means of financing the company. It is part of one system of organizing cooperatives. Since no interest is paid on membership fees, this manner of financing is significant from the cost standpoint.

*Size of Membership Fees.* Membership fees vary considerably from less than \$1 per person to as high as \$100,<sup>22</sup> although \$1, \$5, and \$10 fees predominate. Some local associations collect annual membership fees or dues, but this practice is gradually disappearing. The receipts from the sale of memberships may

<sup>21</sup> See HULBERT, L. S., *Legal Phases of Cooperative Associations*, U. S. Dept. Agr. Bul. 1106, pp. 21-24, 1929, for a fuller discussion of this question.

<sup>22</sup> As an illustration of the variable membership fees note those charged by the cotton cooperatives. The Staple Cotton Cooperative Association had a membership fee of 25 cents per bale, with a \$10 minimum; the Farmers Union association and the North Carolina association adopted a membership fee of \$3; the South Carolina and Georgia associations, \$5; and the others \$10. In both North Carolina and Georgia the fee was later changed to \$10. GATLIN, GEORGE O., *Cooperative Marketing of Cotton*, U. S. Dept. Agr. Bul. 1392, p. 22, 1926.

be ample to provide all of the capital needs in an association requiring little or no permanent capital and only small amounts of working capital. But, in the event that large capital needs are present, other means of financing must be resorted to, such as sale of preferred stock, sale of common stock without voting privileges, sale of bonds, borrowing, and the establishment of subsidiary companies to conduct the marketing operations. In many local associations, such as livestock shipping associations, fruit and vegetable associations, and poultry marketing companies, the income from the sale of membership certificates is ample to supply the small capital needs of the organizations; but in the central marketing organizations for tobacco, wool, cotton, and nuts, in which the nonstock type of organization predominates, additional means of financing are necessary.

Membership fees are usually smaller than shares of stock, although exceptions are to be found. This is owing to the fact that the sale of memberships and the signing of membership contracts are frequently done at the same time, and, if the fee were considered high by the prospective member, the sign-up campaign would be slowed up considerably. Furthermore, since the amount of capital needed in nonstock organizations is often small, there would be no purpose served in having large fees. Frequently, the fee is merely sufficient to cover the expenses of organizing, incorporating, and setting up the association together with tiding it over until the first crop or first few shipments of produce are sold. If warehouses are needed at once, these can probably be rented by the association, or, if they are to be erected or purchased, a subsidiary corporation may be formed in which the sale of stock or other financing methods may be carried on more leisurely.

In some states, one of which is Minnesota, the cooperative laws provide for the issuance of variable membership fees according to the volume of business to be handled for the members. If the fees are considered an important means of financing and if the patronage of individual members varies considerably, there may be ample grounds for varying the fees. If a large amount of capital is borrowed as a result of a low income from membership fees, it is evident that the cost of financing may be an important item to the cooperative. Another of the legalistic characteristics of certificates of membership is their nontransferability and

nonassignability. It was for this reason that some associations preferred this form of organization. In membership associations, it is also essential that the articles of incorporation state whether the property rights of the members are equal or unequal and, if unequal, on what basis they are to be determined. Ordinarily property rights are considered unequal and in proportion to the volume of products each patron delivers to the cooperative owing to the wide variations in volume marketed by the members.

**3. Sale of Preferred Stock.** The sale of preferred stock is one means of acquiring capital in purchasing and sales organizations. Unlike common stock, preferred stock does not carry with it voting rights. Holders of this stock have preferred claims to dividends or interest after other prior claims such as those of creditors and bondholders are met. The owner of preferred stock has a proprietary and not a creditor relationship to the cooperative and, as such, bears the risks that accompany ownership. He has a prior equity in the assets of the company over the common stockholder in the event of dissolution of the association. Cooperative associations frequently sell preferred stock to both members and nonmembers and oftentimes resort to its sale as an auxiliary means of financing after the sale of common stock, credit loans, and other ordinary methods have been utilized. Subsidiary corporations, created by nonstock or capital stock organizations, often sell preferred stock.

One feature of preferred stock which makes it desirable for a cooperative is that the stock is ordinarily divested of voting rights, which enables the member-patrons to retain control of their organization even though the preferred stock is held by nonmembers. Furthermore, no interest need be paid on the stock unless it is earned, and unless otherwise stated, such non-payment does not become a cumulative obligation. To offset these advantages, however, the rate of interest which such stock carries must be high enough to attract the funds of both members and nonmembers. It is evident that the record of performance of the cooperative becomes a vital consideration in this matter. Consequently, it is clear that this means of financing is more costly for the cooperative than either the issuance of common stock or membership certificates.

Funds received from the sale of preferred stock are primarily used to finance purchases of land, buildings, or equipment (dur-

able capital), but they are frequently used to enlarge the working capital. In California some years ago, the Sun-Maid Raisin Growers' Association (of Delaware) sold \$2,500,000 of 7 per cent preferred stock largely to nonmembers for the purpose of financing the purchase and construction of warehouses and packing plants. In 1928 a large dairy cooperative sold \$265,000 worth of preferred stock bearing 6 per cent interest so as to increase its current capital account. Seldom is the purchase of preferred stock obligatory upon the membership, but in the Washington Cooperative Egg and Poultry Association, where the net earnings of the supply department are retained as operating capital, preferred stock bearing 8 per cent interest is issued to each patron in the amount of his share of the net earnings. At the discretion of the board of directors, early issues of preferred stock are redeemed from the revolving fund.

4. **Sale of Bonds.** The sale of bonds as a method of securing capital is confined chiefly to a few central marketing associations whose credit is well established and whose assets are sufficient to guarantee the safety of its bonds.<sup>23</sup> A bondholder is a creditor of the association. He is promised a fixed interest rate, repayment of the face value of the bond at maturity, and is assured a preferred claim to the assets of the company in the event of

<sup>23</sup> In a letter to the authors, the President of the St. Paul Bank for Cooperatives wrote: "We have refinanced a few creameries which had bonds outstanding. Generally, these bonds are sold to local people, the bank frequently holding the greater part. Back of such bonds is usually a first mortgage on the plant and equipment of the borrower. They are used merely as a means of dividing up the loan among a few local people. A series of notes could have been used, in most cases, just as well. The issues with which we have come in contact have been for \$20,000 or less." July, 1936.

The President of the New Orleans Bank for Cooperatives wrote: "At the present time we know of no cooperatives in our district financing their fixed investments through the sale of bonds." July, 1936.

The president of the Berkeley Bank for Cooperatives wrote: "Since this Bank started operating, I know of only one cooperative which has floated a bond issue, and it is a mutual water company. Several of the mutual water companies have bond issues outstanding. . . . Very few of the cooperative marketing agencies with which I have come into contact have financed through bond issues; yet, we did run across three or four in our survey of the financial structure of cooperatives in this district." July, 1936.

The President of the Spokane Bank for Cooperatives wrote: "In our dealings with large-scale cooperatives operating in this district, only two of them made use of bonds to finance their fixed investments." July, 1936.

liquidation. Members and nonmembers purchase bonds, and since such purchases are considered primarily investments, the buyers are guided by the same rules as would be followed in making investments in any company.

When large-scale cooperatives resort to selling bonds, they proceed the same as independent corporations do in this respect. Investment bankers "float" the bond issue for the cooperative after a careful analysis is made of financial and operating statements, of membership contracts, of sales policies, of the history of the company, and all other factors that have a direct or indirect bearing upon the financial status of the association. Such bonds are usually sold for the purpose of providing fixed investments. For example, the Burley Tobacco Growers Association financed the purchase of 123 warehouses valued at 6 million dollars through the sale of both capital stock and debenture bonds. The amount of capital which is occasionally obtained through the sale of bonds is further illustrated by the bond issue of 5½ million dollars in February, 1926, by the Sun-Maid Raisin Growers Association (of Delaware). Such bonds are retired by deductions from receipts. The Yakima County Horticultural Union and the Yakima Fruit Growers' Association of Washington issued bonds to finance the construction of cold-storage and packing plants.

Clayton and Horner call attention to two types of bonds used in financing local associations, namely, blanket bonds and limited liability bonds.<sup>24</sup> These instruments are used in negotiating loans from local banks. Both types of bonds are reported to be used a great deal by local cooperative grain associations. These bonds are in many respects similar to promissory notes.

**5. Members' Notes.** One of the earliest forms of financing which has been used by cooperatives is that of members' promissory notes. The plan is simply to have the member make out a promissory note, which the cooperative endorses and discounts at a local bank. Many local cheese factories and other local produce marketing associations owe their existence to this type of financing. The notes are used as collateral to obtain both fixed and circulating capital. Often the amount of the note any member must execute depends upon the volume of business he

<sup>24</sup> CLAYTON and HORNER, *op. cit.*, p. 59.



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transacts through the cooperative. In this manner, investment is gauged by the use to be made of the association.<sup>26</sup>

Not all patrons execute such promissory notes. Frequently, some of the officers or the manager of a newly formed local association give their personal notes as security for loans with which to build and provide equipment. In 1935 forty-four farmers' supply associations in Wisconsin had over \$233,000 indebtedness secured by personal notes of the officers and managers. This is extremely hazardous for the individual officers and somewhat of an indication of a lack of real cooperative spirit on the part of the members. If all members are not willing to bear their prorata share of the financial risks of the association,

<sup>26</sup> In the Keystone Cooperative Grape Association of Pennsylvania each member pays a membership fee and "gives the association his promissory note for \$25 plus \$10 for each acre of grapes which he has agreed to market through it. Associations selling supplies only, generally use a similar promissory note of \$50, \$100, or \$200 from each member for collateral security purposes." HANEMANN, ANDREW H., *Cooperative Buying and Selling among Farmers, Pa. Dept. Agr. General Bul.* 429, p. 25, 1926.

The Cooperative Pure Milk Association of Cincinnati required each member to make an initial loan in the form of a promissory note, payable 30 days after sight, of \$20 for each cow owned and controlled. The Maryland State Dairymen's Association of Baltimore required of each member a promissory note, payable on demand, equivalent to \$1 per cow owned or controlled with a minimum of \$15. *Senate Document 95, op. cit.*, pp. 254, 255.

In CLAYTON and HORNER, *op. cit.*, p. 58, it is reported that grain and potato associations used three types of notes—collateral, investment, and joint. "A collateral note, as employed by cooperative associations, is a demand note given by the individual member, payable to the association. The note is used by the association in accordance with an agreement usually attached to, but sometimes incorporated in, the note, specifying that the note is to be used by the association only as collateral for the purpose of borrowing money from banks or from individuals, and that the note becomes due and payable only upon demand of the party to whom it is negotiated as collateral for a loan." The investment note is used chiefly to raise additional capital from farmers. "These instruments are generally drawn in the form of a negotiable promissory note payable at periods ranging from 5 to 10 years and bearing interest at the prevailing rate. . . ." "The joint note, however, differs from the collateral note in two important particulars. . . . [it is] signed by several members of the association, usually the board of directors, . . . and in the second place it is not employed as collateral security by the association in obtaining loans. The joint note is of the usual negotiable promissory type and given for periods varying from one to six months."

it is questionable whether they should be eligible for the benefits which may appear.

**6. Loans.** It is unusual for cooperative associations to derive from their members sufficient funds to supply the fixed and circulating capital required at all times. Loans from credit agencies and other sources are therefore necessary. Most associations have peak-load periods—the dairy associations in summer, the wool, small fruits and early vegetables in spring, the tobacco in winter, and the grain, cotton, livestock, and fruit associations in fall. It would surely be unwise to attempt to have constantly available adequate capital so as to meet the peak-load needs, when the right amounts can be borrowed for short periods. Adequate financing is not to be interpreted as complete financing by members at all times, but as that degree of support from the members combined with loans from other agencies which will result in the highest efficiency of marketing.

Loans are obtained by: (a) placing mortgages on land, buildings, and equipment; (b) notes of the association secured by warehouse receipts; (c) unsecured notes of the association. Notes personally secured by the officers and directors of the association and the issuance of bonds are other means used to borrow money.

*Amount of Loans.* The loans made to cooperatives vary from year to year depending upon the price level, amount of produce handled, amount of advance payments, size of reserve funds, particular financial policy pursued, and many other specific details that are unlike from one association to another and from one season to the next. From 1929 to 1933 cooperatives everywhere made exceedingly large loans from the Federal Farm Board owing to the low rates of interest that were charged, the ease with which the loans were executed, and the vigorous attempt on the part of the Farm Board to expand the cooperative movement. These loans were for financing fixed capital investments as well as current operations.<sup>26</sup> The magnitude of these Federal Farm Board loans is evident from the fact that on June 30, 1933, total loans outstanding to 144 cooperative associa-

<sup>26</sup> The Federal Farm Board was authorized by the Agricultural Marketing Act of 1929 to make loans to cooperative marketing associations for five purposes. These are listed on p. 288.

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tions amounted to \$181,158,833.56. They ranged in size from \$600 to \$98,827,505, and were granted to local as well as national marketing associations.<sup>27</sup> The loans to cooperatives made by governmental agencies from 1925-1935 are shown in Table XVI.

**TABLE XVI.—LOANS AND DISCOUNTS TO COOPERATIVES OUTSTANDING ON DEC. 31, 1925-1935, FARM CREDIT ADMINISTRATION\***

As of the last day of	Federal intermediate credit banks (direct)	Banks for cooperatives including central bank	Agricultural marketing act revolving fund	Total
1925	\$53,780,152	.....	.....	\$53,780,152
1926	52,704,473	.....	.....	52,704,473
1927	31,990,597	.....	.....	31,990,597
1928	36,174,077	.....	.....	36,174,077
1929	26,072,914	.....	\$14,509,886	40,582,800
1930	64,377,067	.....	136,697,751	201,074,818
1931	45,177,185	.....	156,280,144	201,457,329
1932	9,865,615	.....	158,885,084	168,750,699
1933	15,210,549	\$18,697,149	157,751,909	191,659,607
1934	33,969,171	27,850,593	54,862,901	116,682,665
1935	2,731,280	50,013,329	44,432,766	97,177,375

\* From Economic Information on the Use of Farm Credit, p. 46, Farm Credit Administration.

A few other illustrations suggest the extensiveness of cooperative borrowing. It is reported that a South Carolina association borrowed over \$1,125,000 from its members on 30- to 90-day notes in the early part of one season.

Of sixteen state-wide and regional cotton-marketing associations reporting the source of their borrowings, eleven showed aggregate average yearly loans from Federal Intermediate Credit Banks to the amount of \$26,953,000 for 1924 and 1925. . . . In addition to borrowing through the Federal Intermediate Credit Banks, eight associations reported aggregate average yearly loans from private banks to the amount of \$39,367,000 in 1924 and 1925. The average yearly loans ranged from \$5,000 by one association to \$16,784,500 by another. . . . For the 1924-1925 season the finance committee of the American Cotton Growers Exchange made arrangements with New York City banks for a line

<sup>27</sup> Farm Credit Administration, press release July 10, 1933.

of credit for the (member) cooperative cotton associations to the extent of \$100,000,000 . . . <sup>28</sup>

Seven of the central (grain) marketing agencies report total yearly average *Government* borrowing of \$7,860,000. . . . Thirteen . . . report total yearly average *private* borrowing of \$14,505,000 . . . (and) local farmers' grain elevators to the number of 197 report average yearly borrowing of \$5,205,000.<sup>29</sup>

The tobacco marketing associations have consistently been some of the largest borrowers. Perhaps, next to the cotton associations the tobacco associations showed the largest loans per \$1,000 of business transacted. "For instance, the Connecticut Valley Tobacco Association (Inc.) has . . . secured on an average 5 million dollars through the intermediate credit system, and from 2 to 5 million dollars annually from private sources during the last five years."<sup>30</sup> Illustrations of heavy borrowing by wool, fruit, dairy, and poultry and egg associations could be added to this list. The sources of loans are chiefly local banks and governmental financing agencies, although loans from members, nonmembers, private marketing agencies, and even central cooperative associations are also common.

*Types of Loans.* The types of loans made to cooperatives are indicated by those granted by the Farm Credit Administration. Under the Farm Credit Act of 1935, which amended the acts of the previous two years, the Banks for Cooperatives make available three types of loans to farmers' marketing, purchasing, and service organizations.

a. *Working capital loans* supplement funds provided by the farmers and are made for operating purposes, *i.e.*, to provide a revolving fund to finance current operations, to pay expenses pending the collection of sales receipts or the receipt of a commodity loan; to promote "the effective merchandising of agricultural commodities and food products thereof." The length of time of the loans depends upon the nature of the business transactions that are being financed, although it is a general practice to have the loans repaid at the end of the customary marketing season. "By law the interest rate on working capital loans,

<sup>28</sup> Cooperative Marketing, *Senate Document* 95, 70th Congress, 1st Session, letter from the Chairman of the Federal Trade Commission, p. 261, 1928.

<sup>29</sup> *Ibid.*, p. 258.

<sup>30</sup> *Ibid.*, p. 263.

except those secured by commodities, is fixed as nearly as practicable at 1 per cent in excess of the prevailing interest rate paid by production credit associations to the Federal Intermediate Credit Bank of the district," with a maximum of 6 per cent per annum. "Interest is charged only on the unpaid principal and for the time the principal is actually outstanding." During 1936 the rate was 3 per cent a year.

b. *Physical facility loans* are made to finance the purchase, lease, construction, or refinancing of buildings or other physical property required by a cooperative in its business operations. Usually a first mortgage on the property is required as security although other additional collateral may be required by the bank. Two restrictions upon granting facility loans are: "(a) no loan may be made for an amount in excess of 60 per cent of the appraised value of the security offered, and (b) no loan may be made unless the purchase or lease price is considered reasonable." Accordingly, cooperatives may borrow an amount covering the full cost of the facilities provided sufficient collateral is offered as security. Under the Farm Credit Act of 1933, physical facility loans could be made only up to 60 per cent of the value of the particular facility financed. "By law the interest rate is fixed by the Governor of the Farm Credit Administration as nearly as practicable at the rate prevailing on mortgage loans made by federal land banks to national farm loan associations at the time the loan is made," with a maximum of 6 per cent per annum. During 1936 the rate was 4 per cent per year.

c. *Commodity loans* are made to marketing associations chiefly for the purpose of enabling them to make advance payments to producer-members on commodities delivered to the association and secondarily to pay the costs of marketing. Such loans are made to farmers' purchasing associations principally for the purpose of financing their inventories. They are working capital loans secured by commodities which are represented by warehouse receipts, bills of lading, or other shipping documents. Only staple, nonperishable agricultural commodities, or farm supplies to be sold to members are financed in this manner. Inasmuch as these loans are offered to the Federal Intermediate Credit Banks for discount, thus tapping the resources of these twelve banks, loans can be made only on commodities approved by the latter banks. The staple farm products on the approved

list include: wheat, rice, flaxseed, corn, and other grains; cotton wool and mohair; tobacco; alfalfa, red clover, alsike clover, sweet clover, redbtop, and bluegrass seeds; beans, including soybeans; canned fruits and vegetables, including cold-pack fruits; coffee; raisins, prunes, and other dried fruits; olive oil; extracted honey; maple syrup; broom corn; sugar, raw and refined; evaporated milk, powdered skim milk, and cheese; peanuts and other nuts; and hay.

The basis on which loans are made depends on the character, quality, and marketability of the collateral offered, the management and financial condition of the association, and other such factors. In no event may loans secured *only* by warehouse receipts or shipping documents be made for more than 75 per cent of the market value of the commodity pledged as collateral and usually are limited to a lesser amount in the discretion of the banks. The law provides that the rate of interest on loans secured by commodities is to be fixed by the governor of the Farm Credit Administration, but shall conform as nearly as practicable to the prevailing interest rate charged on commodity loans by the Federal Intermediate Credit Banks. It may not exceed 6 per cent, however.<sup>31</sup>

The loans are made for the usual marketing season varying from three to nine months although renewals are made when justified. The rate of interest was 2 per cent per annum during 1936.

The percentage that can be reasonably loaned on a warehoused commodity depends upon the type of commodity (staple or semiperishable), the nature of the market (constantly ready markets as for dairy products, grain and cotton or more uncertain markets as for tobacco, wool, and mohair), and the existence or nonexistence of a hedging market.

In a brief analysis made some years ago, covering a period of some 25 years of price experience, it was ascertained that the advance, to be absolutely safe under any circumstances, should not exceed about 35 per cent of the market value of the commodity at the time of the loan. Experience also indicates, however, that a 90 per cent advance on a commodity at the low point of a price cycle is a much safer loan than a 50 per cent advance on the same commodity at the peak of prices.<sup>32</sup>

<sup>31</sup> *News for Farmer Cooperatives*, vol. 2, no. 3, p. 4, June, 1935.

<sup>32</sup> WELLS, J. E., Financing Current Assets, *News for Farmers' Cooperatives*, vol. 2, no. 2, p. 7, May, 1935.

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TABLE XVII.—LOANS TO COOPERATIVES AVAILABLE THROUGH THE FARM CREDIT ADMINISTRATION\*

Features of loan	Facility loans to cooperative associations	Operating loans to cooperative associations	Commodity loans to cooperative associations	Commodity loans to cooperative associations
Use of loan	To finance or refinance the purchase, construction, or lease of physical property for cooperative sales, purchase, and service organization	To provide working capital for cooperative sales, purchase, and service organization	To enable cooperative associations to make advances to their grower-members on commodities delivered to associations, and to pay the costs of marketing such commodities, also cooperative purchases of farm supplies	To finance the processing, handling, and marketing of products, and making advances to members thereon; also cooperative purchases of farm supplies
Institution making loan	Bank for cooperatives	Bank for cooperatives	Bank for cooperatives	Federal intermediate credit bank
Amount loanable	May be made up to 60 per cent of appraised value of security pledged	Operating loans (exclusive of commodity loans) and facility loans to any one cooperative at any one time may not exceed 10 per cent of the capital and surplus of district banks. This limitation does not apply to the central bank for cooperatives	May be made up to 75 per cent of the market value of commodities unless hedged or other collateral furnished. Margin of security must be maintained	May be made up to 75 per cent of the market value of commodities unless hedged or other collateral furnished. Margin of security must be maintained
Rate of interest	Minimum, 3 per cent, maximum, 6 per cent. Current rate usually fixed in line with rate paid by borrowers from land banks through national farm-loan associations. Rate Jan. 5, 1936—4 per cent	Minimum, 3 per cent, maximum, 6 per cent. Rate ordinarily 1 per cent above the prevailing interest rate paid by production credit associations to the federal intermediate credit bank of the land bank district in which the principal business office of the borrower is located. Rate Jan. 5, 1936—3 per cent	Fixed currently by Farm Credit Administration Governor. Conforms as nearly as may be practicable to the prevailing interest rate on commodity loans charged borrowers from the intermediate credit bank of the land bank district in which the principal business office of the borrower is located. Rate Jan. 5, 1936—2 per cent	At banks prevailing loan rate which may not exceed 1 per cent above interest rate on last preceding issue of debentures except with approval of the Governor of the Farm Credit Administration. Rate Jan. 5, 1936—2 per cent

\* Prepared by Farm Credit Administration, January, 1936.

TABLE XVII.—LOANS TO COOPERATIVES AVAILABLE THROUGH THE FARM CREDIT ADMINISTRATION.\*—(Continued)

Features of loan	Facility loans to cooperative associations	Operating loans to cooperative associations	Commodity loans to cooperative associations	Commodity loans to cooperative associations
Security	Mortgage on property with such other security as seems necessary	Liens on real estate, equipment, inventories, commodities, accounts receivable, notes, or other evidence of ownership. Unsecured loans made in special cases	Generally—warehouse receipts, bills of lading, shipping documents covering commodities, and chattel mortgages	Warehouse receipts, shipping documents, or such other collateral as may be approved by the Governor of the Farm Credit Administration
Maturity	Ordinarily not exceeding 10 years. May be made for 20 years, however. Payable in annual or semi-annual installments	Ordinarily end of marketing season, or inventory-turnover period, but may be extended to length of time good business practice appears to require	Ordinarily from 3 to 9 months. Renewal at maturity granted in special cases. Payable as commodities are marketed	Ordinarily from 3 to 9 months. Renewals at maturity granted in special cases. Loans payable as commodities are marketed
Remarks	Cooperative association takes stock in the bank for cooperatives equal to \$100 for each \$2,000 or fraction thereof borrowed. Association may retire stock on repayment of loan. District Banks and the Central Bank for Cooperatives may borrow from each other	Total facility, operating, and commodity loans must not exceed 20 per cent of capital and surplus of district bank. This limitation does not apply to the central bank for cooperatives.	Associations may not be required to take additional stock with commodity loans. Borrowers required to hold stock equal to \$100 for each \$10,000 of commodity loans, however. Banks for cooperatives rediscount commodity loans with federal intermediate credit banks	Commodity loan made only on products after delivery to association, for purposes of orderly marketing, not for speculative holding

\* Prepared by Farm Credit Administration, January, 1936.

A concise statement of the loans available to cooperatives and the security, rate of interest, maturity, and other features relating to same are indicated in Table XVII. These loans are available to farmers' cooperative marketing, purchasing and service associations organized in accordance with the terms of the Capper-Volstead Act.

*Security for Loans.* The security for loans depends upon the kind of loan obtained. For facility loans a first mortgage on the physical property of the association is usually obtained, and for



working capital loans warehouse receipts, bills of lading, and shipping documents are pledged as collateral. Some loans are made chiefly on the basis of the confidence that the credit agency has in the management of an association. Great care is ordinarily exercised in granting loans to cooperatives, for ability to repay must be ascertained in advance of making any loan. Each agency that lends money to cooperatives establishes its own criteria for making loans.

The St. Paul Bank for Cooperatives requires substantially the following information from an association prior to making a loan commitment.

1. Nature of business.
2. Evidence that the association meets the requirements of the Capper-Volstead Act, particularly with reference to member and non-member business, producer membership and basis of voting.
3. Specific use to be made of the loan.
4. Detailed description and appraisal of all fixed assets, together with blueprints and photographs, and a complete statement of all prior liens, if any.
5. Basis of repayment.
6. Description of any pending litigation.
7. Certified copy of resolution authorizing directors to make application for loan.
8. Certified copy of Articles of Incorporation and bylaws.
9. Certified copy of marketing and purchasing contracts, including membership agreements.
10. Certified list of officers and their respective addresses.
11. Volume of business in terms of value and units for the previous three years.
12. Copy of audit reports for the previous three years with detailed balance sheets, operating statements, and pertinent schedules with any qualifying statements by the auditors. It is usually required that these be supplemented with monthly balance sheets and operating statements subsequent to the last audit and to close of month preceding application."

A private banker's statement follows:

In a discussion of the safeguards with which banks should surround the financing of cooperative associations, one must differentiate between those cooperatives which, from the very nature of the underlying security

"Cooperation—Principles and Practices, *Wis. Agr. Exp. Sta. Special Circ.*, p. 81, 1936.

they have to offer, are considered a hazardous risk, and those dealing in staple commodities which, while they may be subject to declines in price, are, nevertheless, readily marketable, easily stored, and reasonably nonperishable. An association dealing in staple commodities need not necessarily have either capital or surplus, nor, indeed, any tangible asset whatsoever other than its contracts with its growers. On the other hand, a cooperative manufacturing a perishable product or dealing in a product more or less a luxury either should have liquid assets to fall back upon in case of necessity, or should be able to assure its bankers that its entire output has been sold to responsible wholesalers.<sup>24</sup>

*Repayment of Loans.* A credit agency can be of considerable assistance to a cooperative in devising a plan by which loans can be repaid. Three options of repaying loans may be open to the cooperative; (a) payment of the full amount in one lump sum at maturity, (b) partial payments of fixed amounts on specified dates (once a month) until loan is paid, or (c) payments on a unit of product or percentage of sales receipt basis. If, for example, a cooperative oil station borrowed \$6,000, it could be repaid as follows: (a) \$6,000 at maturity, (b) a fixed amount of \$100, \$200, or some other sum, each month, or (c)  $\frac{1}{2}$  or  $\frac{3}{4}$  cent per gallon of gasoline sold or 2 per cent of the gross sales receipts payable monthly or on fixed dates.

Some plan of repayment should be worked out at the time the loan is granted. Too frequently, however, boards of directors of local cooperatives fail to develop plans of their own and require the assistance of the lending agency. Unless some plan is definitely worked out in advance and payments made accordingly, an association may find that the due date is reached before the amount of the principal and interest payment has been accumulated. Renewal of the loan is essential to save the association from embarrassment. On Farm Credit Administration commodity loans, repayments are made as the commodities are sold.

#### Questions

1. What financing obligations do farmers undertake when they market their products through their own organizations?
2. What reasons can you give for the necessity of a sound financing program in a cooperative association?

<sup>24</sup> Cooperative Marketing Financing, *Monthly Review*, Mercantile Trust Company, San Francisco, Calif., vol. 11, no. 10, p. 187, Oct. 15, 1922.

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3. " . . . . capital of a cooperative . . . will not be found in its stock or its membership liability, but in the commodity which is delivered to the cooperative." Criticize this viewpoint.

4. For what important purposes is capital required by a cooperative?

5. How do you distinguish working capital from fixed capital?

6. What are the advantages of providing the capital needs of a company by the sale of common stock?

7. Do you think it is good cooperative practice to require members to buy shares of common stock on a prorata basis? To have the number of shares anyone may own limited?

8. What types of loans are made by the Farm Credit Administration?

9. What plans for repayment of loans may be followed?

10. In what respects does a nonstock cooperative differ from a capital stock association in securing the initial capital for organization and operation?

## XV

### *Financing Cooperative Marketing Associations.—(Continued)*

*The revolving fund plan of financing—involving the use of certificates of indebtedness—is used by many of America's leading cooperatives. A deduction is made from the members' sales returns and a certificate evidencing the debt of the association is issued for the amount of the deduction. These certificates bear interest at prevailing rates and carry a fixed maturity date, usually 3 to 5 years after their issuance. Today certificates of equity are used which bear no interest and do not mature on any specific date, but are redeemed in the order of their issuance at such times as thought advisable by the association.*

*All progressive associations build up reserves for various purposes that act as buffers in time of need. Few associations depend upon assessments and annual dues to finance their operations. The sight draft is used freely by local and large-scale associations, but relatively few commodity associations today use trade acceptances. Some cooperatives, especially nonstock companies, set up subsidiary corporations which, among other things, finance the fixed investments of the parent association.*

*The principal sources of funds or credit are the members, non-members, credit agencies, and business operations. The central bank for cooperatives and the 12 district banks for cooperatives are member-government owned banks that are today one of the important sources of funds for both local and large-scale associations. These banks are quasi-governmental institutions established by the Farm Credit Administration.*

*Preparation of an annual report including a balance sheet, operating statement, and statistical report is valuable for the membership and management. Adequacy in financing is measured by the efficiency with which the capital is used. Various business ratios can be established to indicate this efficiency.*



## CHAPTER XV

### FINANCING COOPERATIVE MARKETING ASSOCIATIONS.

*(Continued)*

The indirect methods of financing are as numerous as the direct and are used primarily to finance the business operations of cooperatives. Only the more important and commonly used methods will be discussed.

**7. Deferred Payments.** Most of the cooperative associations in the United States use a system of deferred payments as one method of financing their current operations. In fact, payment to the producer *after* the sale of the products by the cooperative is a distinguishing feature of cooperative marketing. Deductions from the proceeds of sale are made to defray operating expenses before farmers are paid. Creameries and cheese factories pay at the end of every 15- or 30-day period, livestock shipping associations after the receipts from the terminal market have been received, fluid milk marketing associations at the end of the month, local fruit marketing organizations at the end of the pool period, egg shipping associations usually at the end of the week, and associations for other commodities at the close of the pool periods. By accepting deferred payments and making it unnecessary for the cooperative to borrow capital between the time of receiving and obtaining payment for the products, the farmers indirectly finance their organization. This is modified somewhat when an advance partial payment is made to producers at the time products are placed in a pool.

The merits of a deferred system of payments rest upon the low costs of financing, reduction of risks, and the prorating of the obligations upon the members according to the volume of business each contributes. Less borrowed capital is required by the cooperative and each farmer bears his prorata share of the financing burden. With respect to operating and sales policies, other advantages and some disadvantages arise which are pointed out in Chap. XVI.

### 8. Revolving Fund Plan—Certificates of Indebtedness.

Another commonly used plan of financing with loans from patrons is through the issuance of certificates of indebtedness against authorized deductions of definite amounts from the patrons' returns.<sup>1</sup> A certificate of indebtedness is a written acknowledgment of the debt of the association for the sum stated on the certificate to the person named therein. It has a fixed maturity date, bears interest at a fixed rate, is either transferable or nontransferable, and is a part of the fixed or long-term liability of the company issuing it. The person holding such certificates becomes a creditor of the association who is neither preferred nor subordinate to other creditors unless it is specifically stated that he is so. In the consolidated balance sheet of the Land O'Lakes Creameries, Inc., for Dec. 31, 1936, under the long-term liability account, certificates of indebtedness due after Jan. 31, 1937, were listed at \$605,212. Certificates are granted for authorized deductions from the sales returns or they may be purchased for cash.

In contrast to the certificates of indebtedness there are also issued against authorized deductions certificates of equity which do not have a fixed maturity date, bear no interest, and are a part of the capital and net worth account of the association. These are sometimes called certificates of interest, but inasmuch as no interest is paid upon the same the authors believe that the term *certificates of equity* is more appropriate and likely less misleading. In recent years cooperative associations have used certificates of equity in greater amounts than formerly. Thus, in the consolidated balance sheet of the Land O'Lakes Creameries, Inc., for Dec. 31, 1936, under the Capital and Net Worth account, certificates of interest (equity) for the amount of \$181,690 were listed. These certificates of equity are in many respects comparable to capital stock inasmuch as the holders of the same do not have any prior claims to the assets of the corporation upon its dissolution to regular creditors. They constitute a proprietary interest in the organization and do not fall into the same category in which the certificates of indebtedness fall. In some associations the certificates of equity are called *certificates of credit*.

<sup>1</sup> These certificates are sometimes called "revolving fund certificates," "redemption certificates," or some other name indicating that they constitute a part of the long-term liability of the cooperative issuing them.

If these contributions are not evidenced by special certificates or set up as special funds on the books of the association, it is assumed that they are part of the undivided assets, and in case of dissolution, the holders of membership certificates [certificates of equity] would receive such undivided assets subject to the prior rights of creditors, providing of course there were no provisions of law or in the bylaws to the contrary. If members' contributions to the finances are evidenced by certificates [certificates of indebtedness] having definite maturity dates, then, in case of liquidation, the members who hold such certificates would generally share in the assets of the organization with unsecured creditors. However, some associations provide in their bylaws that in the event of liquidation or dissolution such contributions to capital, though evidenced by certificates, are subject to the rights of creditors. In some cases the certificates [certificates of indebtedness] definitely state on their face that the holders have prior claim to any assets over membership certificate [certificates of equity] holders. In a few instances, certificates [certificates of indebtedness] issued to evidence capital are so issued as to constitute a mortgage on part or all of the physical assets of the association. If members' contributions to special funds are revolved or rotated, they become a liability of the organization when they are declared due and payable or when they carry a fixed maturity date. If they do not carry a fixed maturity date and are subject to the rights of creditors, they are a part of the ownership capital and are similar to the preferred stock of a profit corporation.<sup>3</sup>

The issuance of certificates of indebtedness is a part of the revolving fund plan of financing, a plan that has been used several decades by some associations and one which is becoming more popular among cooperatives in general. Briefly, the plan contemplates having the patrons during different periods of operation finance their own marketing activities according to the use made of the association, and having patrons at later dates repay the loans made at the earlier periods. To accomplish this patrons are paid partly in cash and partly in certificates representing the amount of the authorized deduction that will be paid in the future. A merit of this plan is that the finances are kept in the hands of the producers and are adjusted to the use made of the organization by each. The certificates may be made payable in annual installments as called for by attached coupons, or payable

<sup>3</sup> STOKDYK, E. A., *The Financial Structure of Cooperatives*, "American Cooperation, 1934," p. 168, American Institute of Cooperation, Washington, D. C.

in full at the end of the usual 2-, 3-, 4-, or 5-year period from the date on which they were issued. Thus, while some certificates are redeemed, others are again issued for lesser or greater amounts to the same or to different patrons. Under a 5-year plan of retirement, certificates issued in 1936 are payable in 1941, those of 1937 in 1942, and so on. From this cyclical arrangement, the appropriate name "revolving fund plan" arises. The certificates usually bear a nominal rate of interest, but in recent years some associations have issued no interest-bearing certificates, certificates of equity in place of certificates of indebtedness. To have no fixed maturity date on the certificates is convenient for an association because it may easily happen that repayment in some years becomes impossible; but for the holder it is less desirable, because the uncertainty of the time of repayment reduces the sales value of the paper. If the marketing contracts permit, deductions may be larger at some times than at others.

*Redemption of Certificates.* The redemption of certificates may take place in two ways, according to a so-called (a) rotating plan, and (b) straight sinking-fund plan. Under the first, certificates are issued in such amounts and for such variable periods as to constitute an approximately uniform yearly financial obligation against the association. As one series of certificates is retired another series of equal size is issued. Under the second plan, which is used less frequently by cooperative milk marketing associations but more often by associations that market annually harvested crops, certificates are issued for fixed periods regardless of the annual obligation which their redemption calls for. Since this plan entails large and small payments, depending on the volume of business and amount of deductions made in years past, special care is required in creating a sinking fund to provide the annual payments.<sup>5</sup>

<sup>5</sup> "The reorganized association (Poultry Producers of Central California) is financed by a revolving fund, accumulated by 1 cent per dozen deduction from the proceeds from sale of all eggs received from its members, deduction being prorated to members on the basis of delivery. When the total deductions for any member reach the sum of \$10 there is issued to him an 'advance fund certificate.' When the total deductions reach \$500,000, members holding the earliest numbered certificates in the advance fund are repaid their deductions with interest at 6 per cent." Cooperative Marketing, *Senate Document 95*, letter from the Chairman of the Federal Trade



The revolving fund plan of financing has some disadvantages. It is apparent that considerable embarrassment may be experienced in meeting redemptions of old certificates in years when the volume of business is greatly reduced or when the prices of the commodities are low. The fact that the amount of deduction may be increased per unit of sales in the years of small volume imposes a burden on members that cannot be easily assumed. Difficulties of this kind arise where the straight sinking-fund method of redemption is used. Although five annual deductions are accumulated before any certificates are redeemed (under a five-year plan), it must be remembered that these loans are made not merely to finance current operations but, as is frequently the case in newly organized nonstock associations, permanent investments as well.<sup>4</sup> If the loans are used to finance fixed investments, then the maturity must be at a later date than if the loans are merely for current operations, otherwise much difficulty may be experienced in meeting payments.

The use of certificates of indebtedness involves an item of financing cost since the cooperative usually pays the current rate of interest on them. To reduce this cost some associations that have operated a considerable time gradually retire the certificates and decrease the amount of their issue. For example, a deduction of 3 per cent of the returns may be made, against which certificates for half that amount are issued—the other half being used to build up a reserve fund for the purpose of retiring outstanding certificates. Objection is sometimes raised to this retirement on the grounds that the certificates are the best measure of each patron's financial interest in the cooperative. In answer to this it may be pointed out that the extent of any person's financial interest in a cooperative is questioned only at the time of dissolution of the association, or upon the death, expulsion, or withdrawal of the member. An appraisal of the property can establish each member's interest. Underlying this

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Commission, 70th Congress, 1st Session, p. 163, 1928. This illustrates a modification of the redemption plans mentioned.

<sup>4</sup> МСКЛАУ, A. W., and W. J., КУНЕТ, Management Problems of Cooperative Associations Marketing Fruits and Vegetables, *U. S. Dept. Agr. Bul.* 1414, p. 28, 1926, state "The 'certificate of indebtedness' plan seems to be the only feasible method of financing fixed investments in a nonstock organization which does not organize a subsidiary corporation."

objection, however, is the reluctantly admitted desire of many members to obtain the interest on their certificates which usually exceeds that paid on deposits in country banks.<sup>5</sup> Wherever possible, it is well to issue certificates of equity without any fixed maturity date and without any fixed interest rate so as to avoid legal difficulties and financial reorganizations that may result from nonpayment of certificates of indebtedness.

**9. Reserves.** To build and maintain adequate reserves to insure the future operations of an association is just as important as to obtain the original capital with which to start a cooperative and, after operations are commenced, to finance its continuation. There is a natural conflict between the members' clamor for immediate returns and the management's obligation to build a sound financial structure. A member's short-time view anticipates high returns, large patronage dividends, and interest on common stock, but such a policy is filled with grave dangers if no provision is made to set aside a portion of the earnings to meet the risks of marketing that are bound to arise. Reserves are the shock absorbers of a business. Sudden losses, obsolescence of equipment, vanishing consumer demand, competition from new producing areas, loss of the market to substitute products, exceptional credit losses—these and many other changes are risks which a cooperative must be prepared to meet with financial reserves.

Some associations set aside certain funds called "reserves" against which individual equities are established, but these are not reserves from a legal and accounting standpoint. In a cooperative, a true reserve is a fund, against which no individual equities exist, set aside for either unexpected or expected losses and changes in business. The reserves are the undivided assets belonging to the association and not to each member according to his patronage. Revolving fund certificates are not issued against such reserve funds. If a reserve fund is systematically created as the business develops and earnings permit, a sizable

<sup>5</sup> Numerous questions concerning the legal rights of holders of certificates of indebtedness arise particularly as to the order of claims against the assets of a cooperative being liquidated and the use to be made of the deductions for which certificates were granted. Some of the legal aspects are discussed by L. S. Hulbert in *Legal Phases of Cooperative Associations*, U. S. Dept. Agr. Bul. 1106, pp. 105-107, 1929.

sum can be set aside in a short period. This adds to the prestige, business standing, and financial rating of the cooperative in community, business, and financial circles. Milk bargaining associations have found that ample reserves strengthen their bargaining positions since such reserves can be used to acquire operating plants when necessary.

*Legal Status of Reserves.* The status of reserves has been clarified by American courts in several decisions. Although the standard cooperative marketing act authorizes cooperative associations "to establish reserves, and to invest the funds thereof in bonds or in such other property as may be provided in the bylaws," nevertheless there was some question as to the property rights of the association in the reserves set aside and as to the necessity of returning the reserves to the growers from whom they were deducted. In 1926 the Supreme Court of Arkansas held that the reserve was a *permanent* fund retainable by the cooperative and not simply a temporary fund to be returned to the growers at the close of each year's business. However, if the reserve is sufficient to meet the reasonable requirements of the organization, it may be enjoined from making further deductions for a reserve. In some associations the marketing contracts not only state the amount that may be deducted for a reserve, but the *specific purpose* for which it may be used. In absence of naming the specific purpose of reserves, the directors of the association may utilize the fund for any legitimate purposes. In Thompson on "Corporations" (3d ed., Chap. 192, pages 1084-1085) the rights of cooperatives respecting the use of reserves is admirably summed up as follows:

Unless specifically provided that this reserve must be returned to the grower, it becomes the permanent property of the association. It may be used for general commercial purposes. It may be invested by the association in the capital stock of a subsidiary corporation. It may be used by the association in financing its re-sign-up campaign when its marketing contracts are about to expire. It may be used to cover losses to the association in the event of its inability to collect on sales made by it. The purpose of the reserve, particularly with nonstock, nonprofit associations, is to give them a degree of financial stability not otherwise obtainable; to have available a source from which may be financed the obtaining of renewal and additional membership contracts when the same expire; and to eventually put the association in a position to finance

the movement of crops through it without depending upon outside financial aid. A member cannot compel the return of the reserve until the expiration of his membership with the association. The reserve may then be redistributed annually, or in any equitable manner, in the conclusive discretion of the directors. In case of nonstock, nonprofit associations, where the membership is for life, the member may not compel the return of the reserve, even though the marketing contract has expired, provided the size of the reserve is reasonably needed for corporate purposes; and for maintenance of subsidiaries. But if the association creates a reserve which is greater than its needs, the member may enjoin further deductions for the reserve from the proceeds realized from the sale of his crops.\*

*Kinds and Use of Reserves.* There are several kinds of reserves of which the following are rather common: (1) valuation reserves—designed to offset the depreciation and obsolescence on buildings, machinery, and equipment; to cover bad debts; (2) liability reserves—designed to meet exceptional liabilities, unforeseen changes in business operations, extraordinary adjustments in operating costs (sometimes called “reserve for contingencies”); (3) capital reserves—designed to provide working capital—for future business expansion and plant extensions, to retire indebtedness; (4) accrued expense reserves—to pay for such accrued expenses as taxes, and the different kinds of insurance.

The purpose of a reserve governs its use. Some reserves are set aside to meet marketing losses. Such reserves constitute what is commonly called a “sinking fund.” Livestock shipping associations invariably create sinking funds out of which losses sustained in shipping livestock to market are paid. A reserve set aside to cover the depreciation of equipment and buildings is theoretically built up at approximately the same rate that the physical property wears out so that a replacement fund is available when new equipment and repairs are needed. Obsolescence must also be considered in creating this reserve. An allowance for depreciation is, however, merely a bookkeeping entry to show how much the physical property has depreciated, and no fund is set aside for this amount. In addition to these two reserve funds just listed, which each association having marketing losses and physical assets should create, others named above are also

\* THOMPSON, SEYMOUR D., and JOSEPH W. THOMPSON, “Commentaries on the Law of Corporations,” Bobbs Merrill Company, Indianapolis, Ind., 1927.

set aside to retire capital stock, bonds, notes, and certificates of interest, to provide for new capital investments, additions, and repairs and for sundry purposes.

Several plans are followed in building up reserves. One is to set aside a portion of the year's net earnings before any dividends are declared. Inasmuch as cooperatives operate on a nonprofit basis, however, it is evident that few associations would be able to accumulate sufficient reserves from this source. Hence, it is necessary to make regular authorized deductions which cover not only the out-of-pocket costs, but an amount for the various reserves. No certificates of equity are issued against such retains. The effects of this plan are to force each patron to finance his cooperative in proportion to the business transacted, to lessen the cost of financing for the cooperative, and to eliminate individual claims against the assets of the association. The marketing contract usually states the amount of the retains that may be made. In some associations the retains are large enough to provide sizable reserves but, too frequently in others, the authorized deductions barely cover marketing costs.

*Amount of Reserve.* The characteristics of the business, the plan of financing, operating policies, as well as form of organization must be examined to determine the amount of reserves needed. In most livestock shipping associations, that do not conduct side-line businesses, a fund which covers approximately the value of one week's shipment of livestock will prove ample. The ability to borrow adequate sums when needed is a conditioning factor. If the association is engaged in a business that is highly competitive, whose products are subject to violent price changes, and whose operations have more than the usual marketing risks, a large reserve is essential. The cooperative marketing law under which the association is incorporated and the bylaws of an association may require a fixed percentage of the earnings to be set aside as reserves until a certain percentage of the capital stock issue or capital investment is reached.<sup>6</sup>

<sup>6</sup> Under the Wisconsin Cooperative Law of 1911, "the directors, subject to revision by the association at any general or special meeting, shall apportion the earnings by first paying dividends on the paid-up capital stock not exceeding six per cent per annum, then setting aside not less than 10% of the net profits for a reserve fund until an amount has accumulated in said reserve fund equal to 40% of the paid-up capital stock . . ." This provision

The amount of the reserves set aside for various purposes must also be justified if questioned by the Internal Revenue Department or exemption from the payment of income taxes may not be obtained. The needs of an association determine the size of the reserves.

*Liquidity of Reserves.* Reserves may be either liquid or non-liquid in character. Those of the first type are, as the name suggests, readily usable. In local associations, reserves of this type are deposited usually in one or more local banks (preferably in several if that is possible) and are quickly available for any emergency. In central marketing associations or in local associations that may have reserves amounting to tens of thousands of dollars, investments in liquid securities such as United States treasury bonds or other immediately redeemable securities will give the funds the liquidity desired. Liquidity is not measured by the existence of the funds per se but by the availability of the funds upon demand. Reserves or surplus funds invested in buildings, equipment, and land are unavailable upon demand and nonliquid. The physical assets so acquired can, however, constitute the security for loans.

**10. Assessments, Dues.** A few associations, such as mutual water companies, finance their operations on the basis of assessments. Funds are borrowed to meet operating expenses and at the end of specified periods each member is assessed for his proportionate share of the costs. The difficulty and expense of collecting the assessments make this plan very unpopular. A different type of assessment from the one just named is made at irregular intervals for a specific purpose to cover a special cost or loss. Such assessment is easily interpreted as an indication of financial insecurity of an association. Yearly dues are also charged in some instances by membership associations. Live-stock shipping associations and some of the bargaining associa-

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was amended in later years by requiring the creation of fixed reserves before declaring stock dividends and in 1923 was changed to read: "the directors in any association organized with capital stock shall apportion the net proceeds of the business at least once annually by first setting aside such an amount for a reserve fund as they see fit or none, in their discretion; . . ." This modification recognizes the desirability of latitude in determining the annual and total amount of reserve fund which each association may wish to set up.

tions (Connecticut Milk Producers' Association, Inc.) levy such annual dues to obtain operating capital. Extra assessments up to \$1 per cow could also be made by the directors of the last-named association.

**11. Use of Sight Drafts.** In order to assist a cooperative in its current financing problems, buyers and consignees often grant the association the permission to draw a sight draft for a substantial portion of the value of individual shipments. For all practical purposes this is a loan from the concern trading with the cooperative, for which interest is paid by the association. Under this plan the association draws a draft on the customer or consignee for as much as 75 or 85 per cent of the market value of the produce shipped, attaches to this draft order bills of lading, and either discounts the draft at once at the local bank or uses it as collateral for a loan. In this manner the association obtains a substantial advance payment for the goods, on the day of shipment, when ordinarily it would be obliged to wait several days or more than a week for the remittances.

Central cooperative associations, as well as independent buyers, grant such privileges to local associations. Many local member creameries of the Land O' Lakes Creameries, Inc., draw sight drafts against shipments of butter to the central organization.<sup>7</sup> Cooperative potato marketing associations, local grain elevators, cooperative creameries, and cooperative fruit marketing associations use this "closed account" method of financing, as it is also called, to a great extent.<sup>8</sup> Sight drafts provide short-term credit of only a few days, frequently for less than two weeks.

**12. Trade Acceptances.** Relatively few cooperative marketing associations now use trade acceptances to finance their operations.<sup>9</sup> Nevertheless, they may become more common in

<sup>7</sup> Approximately 70 per cent of the member creameries of Land O'Lakes Creameries, Inc. draw sight drafts against their shipments of butter. Loans up to 80 per cent of the current value of butter are made.

<sup>8</sup> In contrast to this *closed account method* of financing, in which the association uses all of the capital loaned and pays interest on the amount obtained for the period between the granting of the loan and receipt of remittance, is the *open account method*. Under the latter plan the association borrows from the consignee or creditor a definite amount for a fixed period, usually a year, and is allowed interest on the daily credit balances.

<sup>9</sup> "Trade acceptances have been used in the past to a limited extent by a few associations, but we do not regard this as a prevalent practice," letter

the future judged by the popularity of acceptances in Europe. A bill of exchange or "draft," as it is more commonly called in the United States, drawn by a creditor becomes an acceptance when the drawee accepts it. A bill of exchange or draft is an unconditional order in writing drawn by one party (the drawer) on a second party (the drawee), requiring the person to whom it is addressed to pay to a third party (the payee) a sum certain in money either on demand or at a fixed or determinable future date. Such a draft may arise out of a commercial transaction, as for example when a cooperative wool-marketing company sells wool to a mill. If previous arrangements have been made between the mill and the cooperative, the cooperative might draw a 60-day draft upon the mill for the purchase price of the wool at the time the wool is sold. When the mill receives the draft and writes the word "accepted" across the face of it, together with the date, name, and location of the bank at which it will be paid, and the signature of the acceptor, then the draft has become a *trade acceptance*. The cooperative that receives the accepted bill of exchange from the mill may sell it at once to a banker and receive cash for the wool it has sold. The bank may hold the acceptance until maturity or sell it to someone seeking liquid investments. Upon maturity the acceptance is presented to the mill for payment. Acceptances are in fact two-name papers and comparable in a number of respects to promissory notes. It is apparent that the cooperative's bank or whoever buys the acceptance finances the sale of wool between the time of purchase of the acceptance and payment by the mill. With the use of acceptances, the cooperative that wishes to obtain funds against products stored in warehouses or against foreign and domestic shipments of goods is in a position to tap the

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to authors from President of New Orleans Bank for Cooperatives (July, 1936). The President of the Berkeley Bank for Cooperatives states that wineries, the Fruit Growers Supply Company, and the Challenge Cream and Butter Association use trade acceptances of 30-, 60-, and 90-days (letter to authors July, 1936). The President of the St. Paul Bank for Cooperatives knew only two cooperatives (supply associations) in his district that used trade acceptances. The President of the Spokane Bank for Cooperatives wrote, "Trade acceptances are not used to any great extent by any of the cooperatives in this district." He named two associations, one handling canning peas and another cherries, that used trade acceptances part of the time.



credit resources of money centers and virtually conduct its business on a cash basis.

**13. Joint-account Dealings.** The financing problems of certain local cooperatives are lessened to a small extent by conducting joint-account dealings with terminal operators. Under this arrangement, the local association usually furnishes the buildings, equipment, and labor, and the terminal market operator provides the working capital. In return for his financing service and sales advice, the terminal dealer determines the margins or prices to be offered locally (when the association buys outright from patrons) and handles the produce in the central market. The local association shares its profits and losses on a fifty-fifty basis, surrenders all control over marketing to the central market operator, and reduces its own capital contributions. A few local potato marketing associations have followed this practice.<sup>10</sup>

Closely approaching joint-account dealings is the method by which local associations buy on commission for terminal dealers. Under this plan the terminal operator supplies the working capital while the local association provides the fixed investments and labor. The dealer determines the price to be paid to farmers, assumes all marketing risks, and pays the association a commission out of which the manager and laborers are paid and all other costs of the warehouse are met. This plan naturally reduces the financing burden of local associations.<sup>11</sup>

For many years terminal grain commission firms have financed the operations of local grain elevators in order to obtain their patronage. Such financial assistance lessens the amount of capital which the owners of the local elevators have to supply. It is reported that about one-fourth of all farmers' elevators have open credit accounts with commission houses. Although such financing is not on a joint-account basis but strictly on a loan basis, it, nevertheless, reduces the amount of capital contributions that members must make.

**14. Subsidiary Corporation Financing.** A subsidiary corporation is a corporation organized, owned, and controlled, either directly or through trustees, by a parent corporation for the

<sup>10</sup> See *Minn. Agr. Exp. Sta. Bul.* 195, p. 31, 1921, for a brief discussion of joint-account dealings by potato marketing associations.

<sup>11</sup> *Ibid.*, p. 30.

purpose of taking over certain duties and certain functions of the parent company. Although the subsidiary may appear as a department or branch or agency of the overhead company, it is a legal entity distinct from its parent. Such corporations should be established by cooperatives only if genuine necessity exists and if economy of operations is possible. Reputable legal and financial advisors should be consulted before steps are taken to create them.

There are a number of reasons for establishing subsidiary corporations: (a) to provide a means of financing fixed capital investments, particularly in nonstock organizations; (b) to conduct various types of marketing operations, such as warehousing, processing, packing, packaging, and manufacturing; (c) to buy supplies for the parent corporation and its members; (d) to establish credit corporations for the sake of financing the production and marketing of growers' crops; (e) to effect exemption from the payment of income taxes and (f) of state taxes on foreign corporations; (g) to conduct business in foreign countries, where the parent corporation would find difficulty in operating due to its particular method of organization; (h) to operate in a manner so as not to disclose the identity of the parent corporation for competitive reasons; (i) to limit the legal and financial liability of the cooperative in certain marketing ventures. This lists the principal reasons for creating subsidiaries.<sup>12</sup> It is evident that the purposes served by the corporations are of two major kinds, namely, (a) for the purpose of financing, *i.e.*, obtaining funds, reducing the cost of financing, and restricting the financial risks; and (b) for the purpose of performing marketing functions either at less cost and at less risk to the parent company, or without the knowledge of competitors.

The California Fruit Growers' Exchange has four subsidiary corporations, the Fruit Growers Supply Company which buys supplies in volume lots for members and operates lumber camps and factories, the Exchange Orange Products Company that utilizes cull oranges, and the Exchange Lemon Products Company which utilizes cull lemons. The fourth is in charge of the association's export business. The Florida Citrus Exchange

<sup>12</sup> HULBERT, L. S., *Subsidiary Corporations and Cooperative Associations*, U. S. Dept. Agr. Mimeograph, September, 1926, treats of various legal problems arising with subsidiaries.

has two subsidiaries—the Exchange Supply Company which buys supplies for the members of the parent cooperative, and the Growers Loan and Guaranty Company which lends money to producers and to local associations. The California Walnut Growers Association has also organized a subsidiary warehousing corporation. Some of the cooperative milk marketing companies operate subsidiary corporations which process surplus milk into butter, cheese, and other products. When the tobacco cooperatives flourished some had subsidiary corporations that operated warehouses and redrying plants. Other associations, such as those handling prunes, apricots, peaches, figs, and raisins, controlled subsidiary companies that processed, packed, and warehoused the products of the members of the parent companies.

Since the membership fees in most nonstock associations are generally insufficient to provide the necessary fixed capital, subsidiary corporations having two classes of capital stock are created. Common stock carrying voting privileges is retained by the parent cooperative association, and nonvoting common stock or nonvoting preferred stock is sold to members and nonmembers. Capital stock corporations also organize subsidiary corporations, but not ordinarily for the purpose of financing the fixed capital investments. A subsidiary warehousing corporation that is properly licensed by state or federal agencies can issue warehouse receipts to the cooperative association creating it. These receipts may be used like those from licensed public warehouses as collateral for bank loans. Usually the subsidiary corporation operates under contract with the parent company and frequently has interlocking directorates. But these evidences of association do not in the least detract from the legal entity of the corporation. It has its own set of books, its own officers, its own expenses, and its own profits and losses.

**15. Miscellaneous Financing Methods.** If the payment of trade accounts is delayed, the seller of supplies, materials, and services to the cooperative is virtually forced to finance temporarily a part of the cooperative's operations. Such forced extension of credit is not in harmony with good business practice and should not be encouraged. It prevents the association from taking advantage of the usual trade discounts (2 per cent net

10 days), harms its business reputation, and may increase its cost of financing. It is mentioned here as a minor method of financing current operations.

### III. SOURCES OF CAPITAL

There are three main sources of finances for a newly organized cooperative:<sup>13</sup>

1. Members—individual producers who are ordinary patrons
2. Nonmember investors—individual investors who may or may not be patrons
3. Credit agencies
  - a. Private agencies
    - Local banks and commercial banks in money centers
  - b. Governmental credit agencies
    - Farm credit administration

After an association commences operations there is an additional source:

4. Business operations

Funds from this last source were treated under the discussion of deductions, reserves, delayed payments to members, and delayed payments of current accounts. The other three sources have been named indirectly in the discussion of methods of financing, but their importance deserves special treatment. Sometimes a cooperative obtains funds or the use of buildings through donations or gifts from civic organizations, local communities, and individuals.

**1. Funds from Members.** The principal source of long-time capital is from the members themselves. This is as it should be. It is important that farmers give more than lip service to the organizations they establish. The genuineness of their interest can be shown best by their support of their organization with capital contributions. The requirement that all members must own stock or purchase membership certificates is founded on the sound basis that the members in preference to others should carry the major amount of the financing burden.

There are a number of advantages of having members provide liberally for the fixed and current capital needs of the cooperative.

<sup>13</sup> Capital is ultimately derived from savings which people make either voluntarily or through compulsion. Savings from past and present production provide the capital for future production.

Perhaps the greatest value rests in the increased interest in the cooperative which such investment brings about. If a member has several hundred dollars invested, it is almost a certainty that his patronage will go to the cooperative instead of a private competitor. If the members contribute substantially to the capital structure, there is little danger that the control of the organization will be divested from the membership. There is also the possibility of financing the cooperative at a low cost if the members provide freely for its financial needs. If interest is earned, it can be paid on the common stock, but if it is not earned no cumulative obligation follows. On preferred stock, bonds, and loans the interest rate is not only fixed, but is frequently higher than that paid on common stock as well as cumulative in some cases. If the members do not invest liberally in their own organization, the management is either cramped in its activities or it must borrow freely. This is not only costly, since policies and operations are subject to the approval of the creditors, but it also restricts the operations of the association.

One problem which arises with many old organizations involves the ownership of capital stock by inactive members. Members retire from farming, move to other localities, or otherwise fail to participate in the affairs of the company. In many instances such "dead" stock is a greater detriment than asset to the cooperative. It becomes very difficult to effect legal changes in the organization of the cooperative when the shareholders do not attend meetings and frequently prevents others from buying stock. At annual meetings a much smaller number of members participate in the business of the association than there are stockholders. For these and other reasons associations should provide for the enforced retirement of all inactive stock or adopt a plan of financing in which the common stock is rotated, *i.e.*, as new issues of common stock are made earlier issues are retired. If some old, retired farmer wishes to retain his stock for sentimental reasons and resides in the community so that the association knows at all times where the stock is located, no particular harm results from not calling the stock in; but an active patron should not be prevented from buying stock due to the sentimentality of some retired producer. The difficulty of congregating a quorum of stockholders which is necessary to legally transact business was one of the greatest handicaps in organizing a

federation of cheese factories in Wisconsin a decade ago. In the absence of provisions that the cooperative buy the stock of inactive members, it may easily happen that persons with ulterior motives may buy up the same. Statutory provisions usually permit associations to include in their bylaws a clause to the effect that anyone who ceases to be eligible to purchase stock in the association (*i.e.*, usually a bona fide producer) shall lose the power to vote. This is a safeguard against having outsiders gain control of the stockholdings and should be adopted by associations whose state laws grant this right.

**2. Nonmember and Nonproducer Financing.** Nonmembers, who may or may not be patrons of a cooperative, supply to a small extent part of the capital of cooperatives.<sup>14</sup> Nonproducers of farm products, such as local bankers, businessmen, professional men, retired farmers, and other public spirited individuals, often subscribe to the capital stock of a cooperative to help it get started in the community. They consider the association a community asset and wish to assist it financially if the producer-members cannot provide sufficient capital to "swing the proposition." Nonproducers may contribute to the capital used for either fixed investments or current operations. Nonproducers can often obtain membership in a cooperative if they purchase shares of common stock or membership certificates. Nonmembers, on the other hand, supply funds used primarily for circulating capital, although some preferred stock, financing permanent investments, is sold to them. Many local creameries, cheese factories, fruit and vegetable packing houses, and other local enterprises have been made possible owing to the financial support of nonproducers. In some instances, central cooperative organizations have financed local undertakings or have arranged loans through the central association for the benefit of local enterprises. Thus, the Land O'Lakes Creameries, Inc., negoti-

<sup>14</sup> Some writers confuse nonproducers (*i.e.*, nonagricultural producers) and nonmembers and consider them as synonymous which is not always the case. Nonmembers never own common stock or membership certificates, for such ownership automatically makes them members, but nonproducers may own either. Consequently, nonmember financing is restricted to ownership of preferred stock, bonds, investment certificates, and to granting of loans. Nonproducers may become members without being patrons of the cooperative. It is customary to think of members as being producers and patrons as well.

ated loans from the Federal Farm Board for the use of its member creameries.

There are distinct advantages, as well as some disadvantages, in having nonmembers and nonproducers contribute to the fixed and circulating capital of a cooperative. It develops an interest on the part of these persons in the organization thus making the association a real community enterprise; it enables the cooperative to secure more funds than those which only the members can provide; the association stands to gain from the business experience, advice, and good will of the nonproducers; it may be possible to obtain capital from these sources at lower cost than could be obtained from regular credit agencies. The disadvantages in selling common stock to nonproducers are: (a) It gives voting privileges to those whose interests are not identical with those of bona fide producers, in fact, may be of a strictly opposite nature; (b) it promotes the idea that the association is an investment rather than a strict service institution, consequently nonproducers may desire a high interest rate paid on stock; (c) it invites membership among those who might have little interest in the association. Their lack of initiative, lack of participation, and failure to attend meetings have a "deadening" effect upon the cooperative. There is much less fear of any disadvantages to the association from nonmember financing for their investments do not carry voting rights in the association. It is possible to organize in such a way that the association may obtain all of the advantages listed above without suffering from the disadvantages by adopting as many safeguards as the state laws and articles of incorporation permit.

From a long-time point of view and from the point of view of good cooperative practice, it is better that producers rather than nonproducers finance their organizations. The fixed investments should be provided in a substantial amount by members, and all financing methods should preserve the cooperative character of the association as well as permit the utmost efficiency in marketing the members' products.<sup>15</sup>

<sup>15</sup> In MEARS, E. G., and M. O. TOBRINER, "Principles and Practices of Cooperative Marketing," Chaps. XI, XII, Ginn and Company, Boston, 1926, an analysis of cooperative financing by members and nonmembers is presented. In this analysis nonmember financing relates primarily to financing by nonproducers.

3. **Credit Agencies—Commercial Banks.** Without a doubt local banks play a larger role in financing cooperative marketing year after year than any other agency. Records are not available showing the loans made each year by banks all over the country to nearly 10,000 associations, but very likely the total sum runs into eight or nine digits. Such has not always been the case for several reasons:<sup>16</sup> (a) bankers were unacquainted with the type of business organizations such as that of the cooperatives; (b) the usual measure of a business success, namely, its profits, upon which the banker would adjudge the merits of the borrower were not to be found in a cooperative which avowedly operated without profits; (c) the management and executive personnel changed more frequently in cooperative associations than in private companies which added to the confusion in the minds of the bankers who were trying to appraise the associations' merits by observing the management over a number of years of operation; and (d) some cooperatives attempted to do things, such as controlling price through monopolistic action, which were of a doubtful character in the minds of the bankers. Bankers have now become acquainted with this new type of business organization, and, it is believed that as a class they are serving cooperatives to the best of their ability.

Local associations depend upon local banks for the major portion of their loans for *current* operating purposes. Frequently, however, cooperatives are required to do business with several banks, because statutes in the state forbid lending more than a certain amount of the capital stock or of the loans outstanding to any one organization. If a bank aims to serve its community, there is perhaps no better opportunity to do so than by loaning to a well-operated and managed farmers' association. Many banks have realized this and have given their unstinted

<sup>16</sup> Sam L. Morley, formerly a banker, commented upon the attitude of bankers in Oklahoma toward cooperative marketing in 1920-1921, "So, I feel safe in saying that 90 per cent of the bankers and businessmen of Oklahoma were either opposed to the plan of cooperative marketing, or gave it so little attention that they discouraged the farmers in the movement." But later on this attitude was changed so that Morley commented as follows: "Our own banks in the state have been very considerate and have loaned us money on our bankers' acceptances, secured by cotton, for as much as 3 million dollars per season." "American Cooperation, 1929," pp. 570-571, American Institute of Cooperation, Washington, D. C.



support to cooperatives. Local associations show some differences in the sources of their loans—local grain elevators borrow more from terminal commission firms than they do from local banks, but cooperative creameries borrow almost entirely from local banks.

Central marketing associations deal primarily with large city banks. The size of the loan is much greater as a rule. Being located in the larger centers, the associations are in a position to tap funds in money centers at lower rates than many local associations are forced to pay. Also central associations have their executive officers, treasurers, who give special attention to the financial problems of their companies. This permits greater care in preparing applications for loans, in securing the funds, and in administering the finances.

*Government Financing of Cooperatives.* The federal government has repeatedly shown its approval of cooperative marketing by providing credit agencies that lend heavily to individual companies. Ever since 1921 when farmers' cooperatives found difficulty in properly financing the marketing of farm products during the first postwar depression years, the United States Government came to the rescue through the instrumentality of the War Finance Corporation. Since that time the federal intermediate credit banks, the Federal Farm Board, and the Farm Credit Administration, through the central and district banks for cooperatives, have financed cooperative marketing associations in enormous amounts.<sup>17</sup> Because of the large number and enormous amounts of loans and because of the favorable terms under which the loans have been frequently, although not always, granted, some people believe that cooperatives are of a quasi-governmental character, require paternalistic care, and are the recipients of advantages which certain private businesses do not enjoy.<sup>18</sup> Cooperatives cannot obtain govern-

<sup>17</sup> By executive order of the President of the United States in March, 1933, five separate and distinct governmental credit agencies were consolidated into one under the supervision of a single governor. The newly formed Farm Credit Administration integrates the activities of all former agencies. The agricultural financing activities of the Farm Loan Board, the Federal Intermediate Credit Banks, the Department of Agriculture, the Reconstruction Finance Corporation, and the Federal Farm Board were brought under one administration.

<sup>18</sup> In 1933 the Shannon Committee Report objected to granting of federal loans to cooperatives on more favorable terms than to private organizations.

ment loans for the "mere asking." Federal laws in the interest of social welfare have made it possible, however, for properly qualified cooperatives to secure loans under conditions which would prevent them from securing loans from regular credit agencies.

If there is any indication of paternalism as regards credit to cooperatives, it is well to remember that cooperatives, due to their form, purpose of organization, and method of operations, have sometimes been at a disadvantage as compared with private organizations in securing commercial credit. Although this disadvantage is not so serious today as it has been, yet it has been a justifiable reason for special credit facilities for cooperatives.

a. *War Finance Corporation.* The War Finance Corporation was originally created as a war agency, but during the reconstruction and readjustment period following the World War, it was authorized to extend credit to American exporters and bankers for the purpose of promoting the exportation of domestic products. The collapse of commodity prices in 1920 induced Congress to revive the activities of the Corporation particularly for the purpose of financing the exportation of agricultural commodities. Loans were made at once (1921) to cotton associations and banking institutions in the South to assist in financing the foreign sale of large amounts of cotton. "Large advances were authorized to cooperative associations on wheat, dried fruits, and canned fruits and vegetables, and to exporters or banking institutions on tobacco, condensed milk, and meat products."<sup>19</sup> Amendments were added to the War Finance Corporation Act and were embodied in the agricultural credit act of Aug. 24, 1921.

The act broadened the powers of the corporation, and gave it authority to make advances not only to exporters and banking institutions, but also to dealers in and handlers of, agricultural products, *including cooperative associations*, for the purpose of financing the carrying of such products until they could be exported or sold for export in an orderly manner. Such advances may be made until July 1, 1922, for periods not exceeding one year, but the time for payment may, in the discretion of the corporation, be extended for periods not exceeding three years from the dates upon which the advances were originally made.<sup>20</sup>

<sup>19</sup> *Fourth Annual Report of the War Finance Corporation*, p. 5, 1921.

<sup>20</sup> *Ibid.*, p. 6.

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The Corporation was permitted by later authority to make new loans to cooperatives until Dec. 31, 1924, but no new loans were approved after 1923. Loans totaling \$202,590,000 were authorized to thirty-three cooperative associations handling cotton, tobacco, rice, and wheat, and other staple agricultural commodities. These associations located in twenty states could use the funds for "orderly marketing" but not for speculative purposes. The associations actually used only \$41,162,000 of the amounts authorized and before November, 1927, all loans were completely repaid.<sup>21</sup>

The loans of the War Finance Corporation were primarily of an emergency character and were granted principally to associations handling staple and exportable commodities (such as cotton, tobacco, wheat, and rice, these receiving 96 per cent of all advances),<sup>22</sup> were issued chiefly to associations in the South and western wheat belt, and were sufficiently important to

<sup>21</sup> In the fifth annual report of the corporation the following comment is made, "The experience of the War Finance Corporation with the cooperatives to which it has made loans has been, on the whole, entirely satisfactory. In general, they have conducted their operations in a businesslike way and have willingly met the corporation's requirements and regulations. . . . The cooperative associations to which the corporation made advances last season carried out their program in good faith as a program of orderly marketing and not of holding for speculative purposes."

<sup>22</sup> Loans to Cooperative Associations 1921-1924 by the War Finance Corporation under provisions of the Agricultural Credit Act of 1921.

Commodity	Total amount approved	Amount advanced
Cotton.....	\$ 86,847,626	\$16,311,237
Tobacco.....	56,500,000	11,227,418
Rice.....	13,250,000	6,795,304
Grain.....	36,790,189	2,543,391
Peanuts.....	2,044,634	1,319,034
Canned fruits.....	300,000	293,242
Sugar cane.....	35,000	35,000
Dried fruits.....	1,250,000	
Hay.....	260,000	
Seeds.....	50,000	
<b>Total.....</b>	<b>\$197,327,450</b>	<b>\$38,524,629</b>

restore confidence in the trade of the commodities financed. The mere fact that the government was willing to finance associations engaged in orderly marketing repeatedly encouraged local banking institutions to make loans to cooperatives when previously they hesitated to do so. Partly for this reason only 20 per cent of the authorized loans were actually borrowed. The emergency activities of the corporation with its beneficent effects upon stabilizing and restoring confidence in demoralized markets paved the way for legislation that would provide permanent credit facilities for cooperative associations.

b. *Federal Intermediate Credit Banks.* Under an amendment to the Federal Farm Loan Act, known as the Agricultural Credits Act of 1923, twelve intermediate credit banks were organized as permanent credit agencies in order to supplement commercial banks and other financial institutions in extending credit to agriculture. The banks are located in the same cities as the federal land banks, serve the same districts, and have the same directors and executive officers. By executive order of the President of the United States on May 27, 1933, all of the federal agencies dealing with agricultural credit were consolidated into one organization, the Farm Credit Administration.

The banks extend two types of credit by two distinctly different methods: 1(a) they discount for agricultural credit corporations, livestock loan companies, and state and national banks, with their endorsement, notes of farmers and stockmen, whose financial statements and collateral security entitle them to credit; or (b) (since June, 1920) make loans to such institutions secured by paper eligible for discount; and 2(a) they make loans to cooperative marketing associations on the security of warehouse receipts or shipping documents covering staple agricultural products; (b) since May 19, 1932, the banks also may accept drafts or bills of exchange issued or drawn by cooperative marketing associations, when secured by warehouse receipts or shipping documents covering staple agricultural products. The banks do not receive funds for deposit or do a general banking business, but secure their loan funds by selling their debentures in the investment market. They do not loan directly to individual farmers but indirectly so. They do loan directly to cooperative marketing associations or discount commodity loans made to cooperatives by the banks for cooperatives.

The act of 1923 originally authorized the banks to extend credit for not less than six months or more than three years—the aim being to provide a credit intermediate between the short-term credit of the commercial banks and the long-term mortgage credit of the federal and joint-stock land banks—but since June, 1930, the minimum maturity was removed. This provides for a greater flexibility in service which the banks can now render, particularly to cooperative marketing associations which need marketing credit for two, three, or four months. The dairy cooperatives in particular found it difficult to utilize the services of the banks under the old requirements. Even today only powdered skim milk, evaporated milk, and cheese are the dairy products included in the list of commodities upon which loans may be granted. Loans to cooperatives, however, are not ordinarily made for a longer period than one year and usually for not more than nine months. They are generally arranged to mature at the end of the normal marketing season.

The amount that may be loaned to a cooperative marketing association depends upon the character, marketability, and quality of the commodity offered as collateral, the management and financial condition of the association, and the ability of the borrowing association to maintain an adequate margin of security. In no event may an advance be made, under the law, to exceed 75 per cent of the market value of the commodity pledged as collateral. The banks can make only so-called "primary loans," *i.e.*, loans secured by documents giving them a first lien upon the commodities. The list of staple commodities eligible for collateral is given on page 386. The two heaviest borrowers have been the cotton and tobacco marketing associations, but in recent years grain, wool and mohair, and dried fruit associations have become large users of this credit. Since the establishment of the district and central banks for cooperatives, cooperative associations desiring a loan apply directly to the bank for cooperatives. If a commodity loan is granted, the loan is offered to the federal intermediate credit banks for discount thus tapping the credit resources of these banks. At the same time, it makes it unnecessary for a cooperative to apply at different banks for different types of loans.

Cooperatives have not utilized the financing services of the intermediate credit banks as much as it was anticipated. This

was due partly (1) to the inflexibility of the service; (2) to the fact that many important farm products are not on the approved loans list, including such products as butter, eggs, poultry, fresh fruits and vegetables; (3) to the adoption of more liberal regulations in the federal reserve banks so that agricultural paper of more than 90 days' duration became eligible for discount; (4) to the greater willingness on the part of local bankers to lend to cooperatives on more reasonable terms than in earlier years when cooperative associations were new; and (5) to the fact that the cost of intermediate credit is frequently not less than that of credit from many local banks. The adoption of various amendments in the past few years and the fact that the banks for cooperatives discount their commodity loans through the intermediate credit banks will, no doubt, cause a greater use to be made of the credit resources of these institutions than in the past.

*c. Federal Farm Board Financing.* From 1929 to 1933 the Federal Farm Board, created by the Agricultural Marketing Act of 1929, was a most abundant source of funds for cooperative associations. Under the terms of the act the board was to receive the sum of \$500,000,000 which was to constitute a revolving fund from which five different types of loans could be made to cooperative marketing associations, namely, effective merchandising, facilities, clearinghouse, educational, and commodity loans.

Up to June 30, 1932, total loans to cooperatives, exclusive of those to the two stabilization corporations, were in excess of 356 million dollars. In the second annual report, which covered the heyday of operations of the board, loans up to June 30, 1931, were reported to amount to 662 million dollars including those to the stabilization corporations. Fifty-three per cent of the loans were for merchandising, 42 per cent for commodity, 4 per cent for facility, and less than 1 per cent for educational purposes omitting those made to the two stabilization corporations. On Feb. 28, 1933, Federal Farm Board loans to cooperatives classified by commodities were as shown on page 419.<sup>23</sup>

This shows not only the large amounts but also the diversity of the loans. The total does not include the loans to the stabilization corporations.

<sup>23</sup> Federal Farm Board Press Release, Mar. 30, 1933.

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Cotton.....	\$84,684,322.83
Wool.....	18,569,768.05
Wheat.....	16,798,503.30
California grape products.....	11,182,610.23
Dairy products.....	10,924,844.22
Livestock.....	4,329,931.44
Fruits and vegetables.....	3,455,963.24
Tobacco.....	2,447,443.77
Grass seed.....	1,255,556.23
Nuts and rice.....	1,095,956.43
Canned goods.....	1,051,530.43
Beans.....	502,835.07
Poultry.....	448,647.28
Grape juice.....	188,818.28
Miscellaneous.....	299,592.55
<b>Total loans.....</b>	<b>\$157,236,323.35</b>

There were three distinctive features of the loans made by the Federal Farm Board which distinguished them from loans made by other governmental agencies:

(1) They were made for five different purposes involving uses for which no other federal agencies had previously lent money.

(2) They were made at very low rates of interest to cooperative marketing associations only (a modification of this was the loans to the two stabilization corporations).

(3) They were made in exceedingly large commitments without any restrictions by law as to the maximum percentage which the loans were permitted to be of the market value of the commodities. The facility loans, however, were not to exceed 80 per cent of the value of the security for the loans. This liberal attitude toward lending to cooperatives was inspired by the spirit of the Agricultural Marketing Act which was the Republican administration's hope for helping American agriculture. In this agricultural relief plan great stress was laid upon adequate financing of cooperative marketing agencies. There is no doubt that some loans were of a questionable character, but in the aggregate they served an exceedingly useful purpose of both temporary and lasting benefit to the country.

*d. Banks for Cooperatives.* One of the important governmental credit agencies today is the banks for cooperatives, established under the provisions of the Farm Credit Act of 1933. One Central Bank for Cooperatives in Washington, D. C. and twelve

regional banks were created.<sup>24</sup> The original capital stock of the thirteen banks was subscribed from the revolving fund authorized by the Agricultural Marketing Act of 1929. From this source, on Feb. 1, 1936, 75 million dollars of the central banks' capital stock, and 65 million dollars of that of the twelve regional banks, with a minimum of 5 million dollars for each, was paid in. These amounts may be changed by the Governor of the Farm Credit Administration in accordance with the credit needs of each bank.

Each borrowing cooperative is also required to subscribe to the capital stock of the bank making the loan at the rate of \$100 for each \$2,000 or fraction thereof of operating loans (other than commodity loans) or facility loans obtained. The capital contribution is repaid to the cooperative when the loan is repaid, or it may be kept as an investment by the cooperative at its discretion. For loans classified as commodity loans, the amount of stock which borrowers must own is prescribed by the Governor of the Farm Credit Administration. The rule in 1936 was that an association had to own \$100 of stock for each \$10,000 or fraction thereof of the amount of the loan, permitting stock owned by the cooperative because of other than commodity loans to be applicable on this requirement. If a cooperative is incorporated in a state whose laws do not permit a cooperative to subscribe to the capital stock of such institutions as the banks for cooperatives, then the cooperative is required to pay into a guaranty fund an amount equal to the required stock subscription. Borrowing associations nominate three of the seven directors of the central bank for cooperatives and elect one director of each Farm Credit Administration district board of directors.

A district bank for cooperatives can acquire additional funds by discounting certain paper with the intermediate credit banks and by borrowing from the last named banks and from the central or regional banks for cooperatives. The central bank may also sell its debentures up to five times its paid-in capital and surplus and thus acquire additional funds.

<sup>24</sup> The district banks are located in Springfield, Mass.; Baltimore, Md.; Columbia, S. C.; Louisville, Ky.; New Orleans, La.; St. Louis, Mo.; St. Paul, Minn.; Omaha, Neb.; Wichita, Kan.; Houston, Texas; Berkeley, Calif.; and Spokane, Wash. Loans to Farmers' Cooperatives, Farm Credit Administration, *Circ. 6* (revised August, 1935), explains the set-up of the banks and the types of loans made.



The types of loans, operating (or effective merchandising), facility, and commodity, which are made by the banks, have been described in the previous chapter. The regional banks make loans primarily to local and small regional associations while the central bank makes the large loans to the larger regional and national associations. Under the regulations of 1936, a district bank could have outstanding physical facility and operating loans (other than those secured by commodities) to any one borrower at any one time in an amount equal to 10 per cent of the capital and surplus of the bank. In the case of effective merchandising loans, the amount could be up to 20 per cent of the capital and surplus, which is also the maximum that a district bank can lend to any one borrower at any one time. In August, 1936, the rate of interest on commodity loans was 2 per cent, on operating loans 3 per cent, and on physical facility loans 4 per cent. Since the purpose of the banks is not to encourage cooperatives to get into debt but to help them get out of it, considerable care is taken in granting loans and in working out an acceptable plan of repayment. Table XVI indicates the amount of loans made by the cooperative banks that were outstanding at the end of each of the past several years. In three years of operation the Berkeley Bank for Cooperatives received about 400 applications for loans aggregating 25 million dollars, turned down 55, and made commitments for 20½ million dollars to the others. Loans were divided between cooperatives as follows, 21 per cent to poultry cooperatives, 20 per cent to cooperative wineries, 16 per cent to citrus associations, 11 per cent to mutual water companies, 10 per cent to dairy organizations, 9 per cent to deciduous fruit companies, and 13 per cent to numerous other associations, indicating the diversified list of associations receiving financial assistance in this one banking district.

#### WAREHOUSE RECEIPTS

In 1916 the United States Warehouse Act was passed, which has proved to be of great value to cooperatives in financing their operations. The purpose of the act was to develop a form of warehouse receipt covering stored agricultural products which bankers everywhere and at all times could accept as security for loans. This required that warehousemen of the highest

integrity be selected and the warehouses themselves be so constructed as to prevent deterioration of the products while in storage. In order to accomplish these ends, United States Department of Agriculture officials carefully supervise and periodically examine licensed warehouses. Warehouses are licensed after satisfactory evidence is obtained concerning the financial standing, commercial integrity, and character of the management. The warehousemen are bonded, are required to prepare very complete monthly reports as to the in and out of storage movements, are required to conduct the warehouse properly, and are to issue warehouse receipts in a faithful manner. Such receipts reveal (1) that a product is actually in storage, place and date of the same; (2) that the commodity will stay in storage until the receipt issued against the particular commodities is returned with proper cancellation; (3) that the commodity meets all specifications of description on the receipt, is properly cared for, and will be released from storage in practically the same condition as when it entered. In other words, the warehouse receipt gives all of the information and assurance which a prudent banker would consider in making a loan on the basis of the physical existence of the commodity. It, of course, says nothing regarding the market value of the product, but it becomes a negotiable paper acceptable at banks for a high proportion of the market value of the product stored.

Under the terms of the original law, warehouse receipts were granted for only four products, namely, cotton, wool, tobacco, and grain, but later amendments permitted the Secretary of Agriculture to add nuts, potatoes, beans, dried fruits, canned foods, sirups, broom corn, cottonseed, and cold-packed fruits. Other products may be added. Some cooperatives own their warehouses (usually operated by subsidiaries) in preference to leasing space in privately owned storages, and they use the receipts which their warehouses issue to obtain loans.<sup>25</sup> A

<sup>25</sup> Some of the problems that come up in using public licensed warehouses by cooperatives and suggestions for changes in the regulations of warehouses under the United States Warehouse Act, particularly for those that store wool are found in an article by R. A. Ward, *Necessary Changes in Federal Warehouse Act*, "American Cooperation, 1929," pp. 551-556, The American Institute of Cooperation. He points out that (1) the public character of the warehouses, (2) the inability to secure space at times because of this public character, (3) the difficulty of finding warehousemen of suffi-

cooperative cannot conduct a federally licensed warehouse for its own exclusive use, although it may own the same.

The experience of those that use warehouse receipts of federally licensed warehouses indicates that bankers as a class have confidence in lending on the basis of such receipts. In fact, the additional protection which is secured from this type of collateral has induced some bankers to reduce the interest rates on loans.<sup>26</sup>

In addition to federally licensed warehouses there are also state licensed warehouses whose storage receipts within the respective states have a high rating. As a matter of fact the general satisfaction which has followed the use of receipts of some state licensed warehouses has caused warehousemen in such states to hesitate about switching over to federal licensing. Oftentimes the fear of extra costs and extra "red tape" under the federal plan has been a contributing reason for not changing.

#### ANNUAL FINANCIAL STATEMENTS AND STATISTICAL SUMMARIES

At least once a year every member of a cooperative organization should receive a statement about the financial affairs of his cooperative, as well as a report upon the cost of running the association, the net sales, and a comparison with previous years' business. A financial statement is not only essential in maintaining a well-informed membership but invaluable to the manager and board of directors in deciding upon operating policies. Successful management rests upon the proper use of factual material, such as a well-prepared annual statement should present. Of course, more than a financial statement is needed by the management. Data showing receipts, costs, sales, prices, margins, marketings, as well as certain business management ratios that may be compared with previous years' operations as well as with ratios of other cooperatives in the same business, are essential.

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cient financial standing to store the products of a large cooperative, (4) the excessive costs of operating a federally licensed warehouse, and (5) the loss in storage space are problems deserving attention.

<sup>26</sup> A dried-fruit growers' organization reports that through this type of collateral it was able to get money for 2 per cent less than it could on its former type of collateral. *Yearbook of Agriculture* 1926, p. 289.

An annual statement should include: (1) a *balance sheet* which is a statement of the assets and liabilities of the association and an indicator of the financial standing of the business at a certain time; (2) an *operating statement* which is merely an accounting of receipts and disbursements during a given period of time (usually one year); and (3) a *statistical statement* which reveals pertinent miscellaneous data essential to the management and membership alike for a better understanding of the organization and its operation. Such things as the number of members, number of stockholders, amount and kind of stock held by members, cost per unit of doing business, patronage dividends paid, losses sustained, and other cogent information should be included. Comparisons with previous years so as to denote trends are exceedingly valuable.

The financial soundness of any company is measured by (1) its current solvency, and (2) its ultimate solvency. By current solvency is meant the ability of an enterprise to meet its currently maturing debts and liabilities and, by ultimate solvency is meant its ability to liquidate its long-time maturing liabilities. A balance sheet ought to show both positions of a company. Even though a cooperative may be able to meet all of its long-time financial obligations, if it does not have current assets to meet its current liabilities, or if it does not have cash on hand to pay its immediate debts, it will be financially embarrassed. The current solvency is shown by the so-called "current ratio," and the ultimate solvency by an examination of the net worth account and operating experience of the company.

**Business Ratios.** For the management, the significance of the financial statement and operating statement rests upon the *business ratios* which can be determined from them. Ratios constitute a means of testing and comparing the financial and business activities of one cooperative with another in the same kind of business, or with its own activities of the past, and of measuring the solvency of the enterprise. It is to be expected that with an increase in the number of different commodity organizations, as well as with numerous years of successful operation, both practicable and satisfactory standards of operation for each type of cooperative may be devised. Uniform methods of accounting will be of great assistance in drawing up such standards of comparison. Comparisons of ratios must

depend upon operating similarities to be significant or they may easily lead to erroneous conclusions.

Not all of the many different kinds of ratios will be listed here, but only a few of the more significant ones.

1. Current ratio, *i.e.*, current assets to current liabilities. The greater this ratio the freer the current assets are from debt. Creditors are more certain to receive payments promptly. The current ratio is one of the most commonly used financial ratios to measure the liquid position of a business. It is sometimes alluded to as the "2:1 ratio," (\$2 of current assets to \$1 of current liabilities) and used by bankers as a guide in extending loans. The ratio does not consider the variations in the type and character of current assets of unlike businesses. A higher than 2:1 ratio may not guarantee liquidity for some businesses while in others it may be more than sufficient.

2. Profit and loss ratios or operating ratio, *i.e.*, total cost of goods sold plus the total operating expenses in relation to the total net sales. This ratio indicates the loss or profit in handling the products sold. The difference between the total operating expense and the net sales constitutes the gross profit (or loss).

3. Net worth to total debt (both current and fixed). This ratio shows whether the owners or creditors control the business. As the amount of debt increases relative to the proprietary equity of the stockholders, the position of the company in the event of a crisis becomes weakened and the risk to the creditors becomes greater.

In addition to these three important ratios the following relationships may be examined with profit.

4. Relation of net worth to capital investment of the owners
5. Relation of net worth to total assets
6. Relation of net worth to fixed assets
7. Relation of net worth to receivables
8. Relation of net worth to net sales
9. Relation of total returns to members to net sales
10. Relation of net sales to total capital invested (turnover of total capital)
11. Relation of separate expense items to total expenses
12. Relation of total cost of merchandise to the average inventory at cost, or the relation of total sales of merchandise

to the average inventory at selling prices (measures turnover of merchandise)<sup>27</sup>

Not all of these ratios are ascertainable for all cooperatives, especially the collective bargaining associations. But for associations that perform marketing services most of these ratios can be prepared to advantage. These ratios and annual statements are mirrors that reflect the business of the company.

That business ratios can be used advantageously in analyzing business operations and can become the basis of changes in operating policies is indicated in the following table for a cooperative grain elevator in the state of Kansas. In the table various ratios have been determined for the years 1932, 1933, and 1934 and a desirable ratio for this type of enterprise is suggested in the last column. The progress which this cooperative elevator made over the three years after following the suggestions which were made on the basis of the first year's business ratios is shown in the table.

**What Constitutes Adequacy?** In many publications dealing with the financing of cooperatives, and in many exhortations to cooperatives, one fact is repeatedly emphasized, namely, that a cooperative must have *adequate* capital to succeed. But what constitutes adequacy? Certainly no single formula is applicable to the same cooperative at all times, much less to all cooperatives. Adequacy for a milk marketing association may be gross inadequacy for a cotton cooperative, and adequacy in the slack season of January may be sadly inadequate in May and June. The test of adequacy is efficiency in rendering the service which the cooperative sets out to perform, and the long-time test of this efficiency is shown in the costs of operation and the net price which the members receive for their products in comparison with those producers who market through other channels.

<sup>27</sup> Numerous textbooks and articles on business ratios explain the use of ratios in great detail.

See GILMAN, S., "Analyzing Financial Statements," Ronald Press Company, New York, 1934. BLISS, J. H., "Financial and Operating Ratios in Management," Ronald Press Company, New York, 1923. Articles by GARDNER and by STOKDYK and WHITE in the *Cooperative Journal*, vol. 8, no. 1, p. 5; vol. 8, no. 3, p. 77, 1934, respectively.

Suggestions for Use of Financial Statements and Statistical Information by Cooperative Associations, *U. S. Dept. Agr. Mimeograph*, December, 1927.

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TABLE XVIII.—BUSINESS ANALYSIS OF A KANSAS COOPERATIVE GRAIN ELEVATOR, 1932, 1933, 1934\*

	Years ending May 31			Desirable
	1932	1933	1934	
<b>I. Working capital analysis:</b>				
1. Relation of current assets to current liabilities.....	1.45 to 1	1.69 to 1	17.52 to 1	2 to 1
2. Ratio of cash and receivables to current liabilities.....	0.46	0.35	3.19	1 to 1
3. Ratio of cash to current liabilities.....	0.09	0.06	2.66	0.2 to 1
4. Ratio of side-line sales to receivables.....	8.20	17.06	121.59	12 to 1
5. Ratio of net working capital to inventory.....	0.54	0.545	1.24	1.5 to 1
6. Per cent receivables are of current assets.....	25.72	17.	2.9	40% or under
<b>II. Fixed-capital analysis:</b>				
1. Ratio of sales to fixed assets.....	8.05	8.34	13.58	8 to 1
2. Ratio of net worth to fixed assets.....	1.37	1.43	1.0	1.5 to 1
<b>III. Analysis of capitalisation situation:</b>				
1. Ratio of net worth to debt.....	1.66	2.27	34.76	1.5 to 1
2. Ratio of fixed assets to fixed liabilities.....	No fixed liabilities	No fixed liabilities	No fixed liabilities	2 to 1
3. Ratio of surplus to outstanding stock.....	Deficit	Deficit	Deficit	1 to 1
<b>IV. Analysis of financial results of operation:</b>				
1. Ratio of operating costs to gross income.....	1.004	0.983	0.978	0.97 to 1
2. Ratio of cost of sales to sales.....	0.925	0.893	0.919	0.93 to 1
3. Ratio of cost of wheat sales to sales.....	0.938	0.895	0.935	0.95 to 1
4. Ratio of cost of other grain sales to sales.....		0.89	0.938	0.93 to 1
5. Ratio of cost of side-line sales to sales.....	0.896	0.89	0.884	0.85 to 1
6. Ratio of salaries and wages to total operating expenses.....	0.54	0.41	0.421	0.6 to 1
7. Ratio of salaries and wages to gross sales.....	4.3	3.7	2.4	2%
<b>V. Volume of business analysis:</b>				
1. Membership needed.....	1,404	1,404	1,000	100
2. Capacity turnover.....	9.02	7.3	6.1	10
3. Per cent of membership patronising company.....	64	64	100	100

\* Prepared by Mr. Vance M. Rucker, Kansas Extension Service, and reported in *Extension Service Review*, vol. 6, no. 4, p. 39.

† Includes other income.

Accountants have used a number of ratios to measure the efficiency of the use of capital, *e.g.*, ratio number 10 listed above. A plethora of funds or investments in capital structures is no measure of adequacy, but rather of superfluity.<sup>28</sup> Cooperatives

<sup>28</sup> HARPER, F. A., wrote in *Cornell Univ. Bul.* 544, p. 93, 1932, "Greater financial safety results when a large proportion of the total capital is provided by the members. Reasonable financial safety requires that this be

frequently have too large a portion of their capital in fixed assets, and not enough in current assets or working capital. Such a disproportion may seriously hamper business operations as well as add materially to the costs of conducting the business. The failure of some cooperative meat-packing plants was partly due to this disproportion of fixed and current assets.

In this connection the cost of borrowed capital must be considered (this includes not only interest, but service charges, discounts, and the available balance that must be kept in the bank as some banks require in extending a line of credit), as well as the relation of total capital costs to the amount of business transacted. Efficiency in the use of capital requires a maximum turnover of capital (ratio of net sales to total capital). Much variation is also found in the turnover of total assets (ratio of fixed assets to total net sales). Both are used as measures of efficiency in the use of capital and throw light upon how fully the capital of the organization is used. When in some organizations the turnover of fixed assets during a year's time is five times and in others in the same line of business is ten times, it is obvious that unit sales in the first association must stand twice the capital costs of those in the latter organization. In cooperative purchasing associations the turnover of the merchandise inventory is one of the best indicators of the efficiency in the use of capital. It is apparent that in all of these instances an increased volume of business becomes a significant factor in determining efficiency in the use of fixed and current capital.

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at least 50 per cent of the total assets. Particularly with purchasing associations, a cooperative should seldom be started until this condition can be attained, because the capital needs usually grow rapidly at the start."

The late George O. Gatlin wrote in *Ore. Extension Bul.* 406, p. 13, 1928, "An organization should provide, if possible, its own fixed capital. There is nothing that gives more assurance of stability in a cooperative as does a membership able and willing to furnish funds for the establishment of its own business."

PRICE, H. BRUCE, and CHARLES M. ARTHUR in *Management Problems of Farmers Elevators, Minn. Agr. Exp. Sta. Bul.* 224, p. 73, 1925, answered the question, "What constitutes an adequate financing program for grain elevators?" by stating, "In general, a financial policy should provide for the contribution of sufficient capital by stockholders to permit borrowing at reasonable rates and without restriction of the marketing program."



**FINANCING COOPERATIVE MARKETING ASSOCIATIONS 429**

**Questions**

- 1. What arguments may be advanced for the use of the revolving fund plan of financing?**
- 2. Why do some financial counselors advocate the issuance of certificates of equity?**
- 3. Show how a sight draft and a trade acceptance are used.**
- 4. What principal purposes does a subsidiary corporation serve?**
- 5. What reasons can you advance for desiring members to finance their associations amply with their own funds?**
- 6. Describe briefly the financing operations relating to cooperatives of the War Finance Corporation, Federal Intermediate Credit Banks, Federal Farm Board, and Bank for Cooperatives.**
- 7. Why was the enactment of the United States Warehouse Act of particular value to American cooperative associations?**
- 8. What information about a cooperative should an annual statement reveal?**
- 9. How would you measure the current solvency of a company?**
- 10. What constitutes adequacy of financing in a cooperative company?**

## XVI

### *Pooling Agricultural Products*

*When a cooperative receives products from its patrons, it may buy them outright, sell them for the patron at such time as he orders, or pool them with other patrons' products to be sold whenever the management of the organization deems it expedient. Grain elevators buy nearly all of the grain for cash on delivery by the farmers; cotton cooperatives operate so-called "immediate fixation pools" which, from many practical aspects, are comparable to outright purchasing operations; and dairy, tobacco, egg, and fruit and vegetable associations pool practically all of their products.*

*Buying for cash has certain practical, competitive advantages, but, likewise, a number of disadvantages. Holding farm products for patrons until such time as they wish to sell places the risk of price fluctuations upon the patrons. Such procedure makes it difficult, if not impossible, for a manager to market the products in an orderly manner. Pooling involves (1) the physical mingling of the products, (2) lumping together of the sales returns and apportioning the net returns among those who contributed products to the pool, and (3) combining the expenses of operations, both direct and overhead expenses. Products, sales receipts, and expenses are pooled before patrons receive their individual shares of the net returns. Pooling is an averaging process.*

*All associations pool either all or some marketing expenses, even though they may not pool the products or sales receipts. The associations that are commonly called "pools" are the ones that pool products, sales receipts, and expenses before dividing the net returns among the patrons. Hence, it becomes apparent that all cooperatives are not pools (because they do not pool products and sales receipts), but all pools are cooperative.*



## CHAPTER XVI

### POOLING AGRICULTURAL PRODUCTS

#### METHODS OF HANDLING FARMERS' PRODUCTS

There are three methods which are commonly followed in handling and paying for farm products by the cooperatives: I. paying the farmer cash on delivery for his products which are bought outright by the association; II. paying the farmer what his individual products actually sold for, less the association's charge for operations; III. paying the farmer the net pool price for his products after the products in the pool to which his were added are sold. These methods will now be discussed.

#### I. BUYING OUTRIGHT AND PAYING CASH

It is no indictment of the American farmer to observe that he is usually short of cash when his products are harvested or ready for market. He looks to his country market as a cash market and almost invariably has found it such. Therefore, when he becomes a member of a cooperative association, he may still prefer to receive cash on delivery as he has been accustomed to receive, although his demand for cash payment may increase the financing costs for the cooperative. It is difficult to break away from this custom owing to the need for immediate cash as well as the fear of loss that the old system of trading has engendered. To meet this demand for cash a number of cooperatives throughout the country are buying farmers' products outright.

Such cash buying practice is common for cooperatives handling such products as grain, cotton, potatoes, and cream (handled by cooperative cream shipping stations). To a minor extent poultry associations and livestock shipping associations also follow this practice. In North Dakota in 1928, thirty-one out of thirty-three cooperative cream shipping stations paid cash on delivery for cream and only two paid on a semimonthly pool basis. In Idaho, on the other hand, in 1926 there were fourteen cooperative cream pools which broke away from the general practice of paying

cash on delivery and simply received the farmer's cream, weighed and tested it, and sold it to a distant creamery after which the farmers were paid the pool price. Occasionally, a livestock shipping association buys livestock for cash when it is delivered to the local yards. Two associations in Wisconsin conducted their entire business on this basis. The managers bought the stock for the associations with the association's funds and at the end of the year declared a dividend when such was earned. It is to be noted that this practice differs from a rather usual, yet generally undesirable, practice in which the manager buys livestock on his own account from association members and ships his stock thus purchased with that of the members of the association. In the latter case it is the manager who stands to gain or lose and not the association, and it is the manager's personal funds and not the association's which are at stake. (The association stands to gain or lose indirectly, however.)

Local grain elevators as a general practice buy grain outright from members and nonmembers of the association, paying them the local market price on day of delivery. Competition with privately owned elevators very often forces this upon the association if it wishes to stay in business. The prices paid on day of delivery may be just sufficient to meet the local competition, or they may be higher than those of local competitors if operating costs are sufficiently low to permit such higher payment. Whether the cooperative elevator aims to declare large dividends at the end of the year by virtue of following a conservative policy respecting cash payments, or whether it aims to pay as much cash as possible followed by small or no dividends later is a matter largely influenced by the local competitive situation. Since the elevator manager is constantly in touch with terminal markets and knows what prices are being paid there for the different grades of grain, he knows how much he can pay locally and still meet his operating expenses and transportation costs. It is estimated by some that 95 per cent of the grain handled by cooperative elevators in the Northwest is bought outright,<sup>1</sup> an

<sup>1</sup> "More than 95 per cent of grain marketed by farmers' elevators in the Northwest is probably bought for cash. Most of it is bought at the time of delivery or shortly thereafter; a rather large quantity is bought after having been stored in the elevator; and a small amount is contracted for in advance of delivery." PRICE, H. BRUCE, and CLARENCE M. ARTHUR, *Management Problems of Farmers' Elevators*, *Minn. Agr. Exp. Sta. Bul.* 224, p. 76, 1925.

amount greatly in excess of the cotton purchased by cotton cooperatives.

Following the termination of the rigid pool contracts which were used by the early cotton cooperatives, a more liberal attitude has been taken toward the methods which farmers may follow in marketing their crops. Among these are the options extended to the farmer either (1) to deliver cotton and receive cash immediately from the association, (2) to deliver the cotton to the association, receive a receipt for the same, and reserve the right to announce the date of sale at a later time, or (3) to pool the cotton with other growers and receive the pool price. Many cotton farmers need cash soon after harvest to meet their heavy production loans. To comply with this urgent need and to forestall dissatisfaction which seasonal pooling creates, the cotton cooperatives now regularly receive cotton paying cash on date of delivery. Thus, the association virtually becomes a merchant middleman instead of merely a functional agency. During the 1935-1936 season the Mid-South Cotton Growers Association received 218,500 bales of cotton from its members of which approximately 202,000 bales (92 per cent) were delivered to the "immediate fixation" and "call" pools.<sup>3</sup>

<sup>3</sup> From the farmer's standpoint the "immediate fixation" pool is virtually an outright purchase plan of operation. The following description of the immediate fixation pool will explain certain differences from the usual outright purchase plan.

"Under the immediate-fixation pool, the member is advanced the approximate market value of his cotton at time of delivery. The amount advanced for cotton in the immediate-fixation pool is determined by taking into consideration the price at which the cotton can be sold by the association; less estimated operating expenses and deductions for reserves. In addition, deductions for transportation to probable destination, as well as the usual deductions for hedging, insurance, and warehouse charges which are normally incurred by any agency merchandising cotton, are considered.

"Upon receiving immediate-fixation pool cotton from the member, the association fixes the base price by hedging, *i.e.*, by selling future contracts covering an equivalent quantity of cotton, in order to avoid the risk of price decline. The actual cotton is shipped to a warehouse, classed, and assembled with other cotton in even-running lots for sale throughout the season. When the spot cotton is sold, the futures are closed out and the transaction is terminated. At the end of the season, the member receives any net merchandising income, less deductions for necessary reserves, as a patronage dividend according to the number of bales delivered." FETROW, WARD W., *Cooperative Marketing of Farm Products, Farm Credit Administration Bul.* 3, pp. 13, 14, 1936.

Local cooperative potato warehouses pay cash quite generally, for they find it necessary in many instances to adopt this procedure if they wish to survive. Three and four independent warehouses that conduct a cash business are often located at a single shipping point, in the face of which it is oftentimes impossible for a cooperative to start that does not also offer this service. In Minnesota in 1918-1919 about one-half of the cooperative warehouses bought for cash and about a third handled potatoes on a commission basis. Whether or not the local association was a member of a central exchange greatly influenced the extent of local buying. It was found in 1920 that those local associations which were members of an exchange pooled 89.9 per cent of their shipments and bought only 10.1 per cent, while those which were not members of an exchange bought for cash 81.7 per cent of their potatoes and pooled only 10.6 per cent.<sup>3</sup> The 7.7 per cent was handled in other ways.

**Features of the Cash Purchase Method.** Certain features of cash buying stand out prominently.

1. The grower receives full payment in cash when he delivers his product to the association. In some instances he may receive part payment on his cash sale even before his cooperative receives his product. Such is the case in a large cotton cooperative and is illustrated by this statement taken from one of its circulars issued to the growers,

Option No. 2. Sale Under This Option To Be Fixed By Telephone, Telegram, Or Personal Call The Day The Cotton Is Shipped. Member may sell the day he ships by notifying the Association that cotton is under bill of lading, or delivered to the compress. He may immediately draw the authorized advance (\$35 on 500# bale) of the Association and settlement will be sent as soon as the actual samples are received and classed. The price basis, however, will be upon the day the cotton was ordered sold. All telegrams and telephone messages must be prepaid by the member.

2. The products are received, weighed, tested or graded, and paid for according to the manager's best judgment of what the local market price should be as compared with terminal market

<sup>3</sup> BLACK, J. D., FRANK ROBOTKA, and PAUL MILLER, Local Cooperative Potato Marketing in Minnesota, *Univ. Minn. Bul.* 195, p. 26, 1921.

prices. These prices must be as large as competitors' prices, or in the absence of competition must be sufficiently below terminal market prices to meet all local operating expenses and marketing risks.

3. If net profits are made on the transaction, these are prorated to members on a patronage basis or to stockholders on a stock ownership basis. Some question arises as to whether associations that pay dividends on a stock basis are truly cooperative. Many local elevators and potato warehouse associations pay stock dividends and, though in their organization they may not meet the ideals of cooperation, yet in their practices they are essentially cooperative.

4. The association bears the risks of marketing and price fluctuations from the time it obtains title to the product. The association is in a position to gain with a rising market, but to lose with a falling market. Buying therefore demands keen judgment on the part of the manager and the adoption of carefully planned financing. No dogmatic principles can be laid down as to just when to sell, for each year's market conditions present new problems. Thus, taking a 17-year period, prices of potatoes paid to Minnesota farmers were higher in the fall than in the spring in 7 of the years and were lower in the fall than in the spring in 10 of the years. These years did not alternate and no general workable rule could be followed to tell whether the market price would go up or down, and, what is more important, how much it would vary.

5. Since there are these price risks which the association must assume in place of the farmer, it becomes all the more necessary to have adequate financial reserves in the association to meet losses. Particularly is this necessary for associations marketing products for which no hedging market exists.

6. Modifications of buying outright for cash are found. In some cooperative potato warehouses, purchases are made on commission for terminal market dealers. In such a case the dealer furnishes the funds and takes all risks while the association furnishes the physical facilities, labor, and management. In a few other instances it has been found that associations buy on a joint-account basis with a dealer of the wholesale produce trade. In these cases the dealer again furnishes the working capital, has a voice in determining margins and prices, and shares equally in

losses and gains. The associations in turn furnish the physical plant and equipment, labor, and management.

**Advantages of Buying for Cash.** Numerous advantages result from this practice and these are mostly in favor of the farmer.

1. The farmer knows at once what he is to receive. It removes some of the uncertainty in his marketing operations. Knowing definitely what he is to get and having the option of taking the cash or the chance of getting more or less by pooling or by sales on commission in all likelihood makes the farmer more favorably disposed toward the association when he makes his own decision respecting the sale of his goods.

2. The association that can meet the demand for cash purchases gains the good will of many farmers. Many cooperative associations make substantial advances to members at the time products are delivered, and in this way meet partially the members' requirements for cash. But there are many cooperatives that cannot advance more than 30 or 50 per cent of the market value which is oftentimes too little to satisfy the members. In this event cash purchases seem to be the most satisfactory alternative.

3. Buying produce from members also enables an association to meet competition and thus get a start in business. Competitors of cooperatives have a powerful appeal in their cash offerings which they make, and, unless cooperatives can make substantial advance payments or permit farmers to sell outright, the chances for success are sometimes limited.

4. Since the system is quite similar to the usual practices involved in marketing at country points, it is relatively easy to introduce. Managers of cooperatives are frequently recruited from private businesses, and, since in their former employment cash buying was the custom, it is quite natural for them to readily apply the same practices in their new positions.

5. The association can more readily increase the volume of its business. Associations having no membership contracts can make strong appeals for nonmember business. Whereas a nonmember hesitates about pooling his products in an association with which he is not affiliated, he has far less hesitation about selling to it at market prices. There is a likelihood of getting a larger number of contract signers if selling for cash is one of the options in the contract.



6. Individual farmers can take advantage of their superior bargaining ability. Although this is an advantage to the producer yet it may be distinctly disadvantageous to the association.

7. It reduces the amount of bookkeeping from that which is necessary if products are pooled through an association. The cash deal becomes a closed account, but the pool with its partial-payment plan involves a series of book entries. This advantage inures to the association.

**Disadvantages of Buying for Cash.** Far more cooperative associations do not buy for cash than those that do. Some of the objections are:

1. It places considerable additional risk upon the association. This risk is especially large during periods of price declines. One "bad" year, particularly if it is the first year, may be enough to ruin an association. It is well to remember that the benefits or gains from cooperation are quickly forgotten, but losses and adversities haunt the association continually. These financial risks are minimized on hedged products, such as cotton and grain, but on unhedged products the risks are great. Approximately one-half of the farmers' elevators do no hedging, one-fourth hedge as a general practice, and less than one-fourth hedge only occasionally.<sup>4</sup> Most of the cotton cooperatives hedge their purchases.

2. Outright purchases demand of the association considerably more working capital than would ordinarily be needed. If products are stored and held for better prices, demands for additional capital are thereby increased. Greater financial reserves are also needed. The extra burden of large financial needs is an additional marketing expense, and seriously raises the question as to whether members individually cannot bear this financing burden more economically by waiting for the returns after the products are sold than by requiring the association to carry the financial problem itself.

3. Special ability is required of the manager. He must know market prices if he is to buy intelligently. A higher than usual salary must be paid to obtain a capable man. He must also be able to bargain with the membership in such a way as not to create antagonism. There is also the danger that favoritism

<sup>4</sup> MEHL, J. M., Hedging in Grain Futures. *U. S. Dept. Agr. Circ.* 151, p. 33, 1931.

may be shown to influential members of the association by paying them more than market-warranted prices, or by being too lenient in grading and docking. It takes a strong management to ignore the pressure that is brought to bear by some members.

4. It is inconsistent with the spirit of cooperation and contrary to the generally accepted principles of distributive cooperation.<sup>5</sup> It places the cooperative in the position of a merchant middleman who is more interested in profits than in the highest prices payable to producers. Though the profit motive does not completely displace the service and the highest-price-to-producer motives, yet the latter are submerged somewhat by the former. It is true that the members who sell for cash have cooperated in supplying funds, establishing the association, and contributing their products, but theirs is only partial cooperation. The additional fact that such associations take special pains in attracting nonmember business, upon which additional profits can be made, and also that in many instances profits are declared on a stock basis rather than on a patronage basis (and if patronage dividends are declared nonmembers receive usually only part of what members receive) leads one to conclude that the profit motive is not unheeded. Such companies become largely farmers' stock companies with some features of cooperation

<sup>5</sup>Lord Linlithgow and A. W. Street suggested that the British method of buying pigs outright at market prices was not a desirable practice for cooperative bacon factories, and that the Danish method was to be preferred. They state that a practice which gives producers cash down, and shifts the risk of changing price levels to the society, admittedly has its attractions but that it is not sound cooperative policy. Farmers should assume these risks in exchange for the rewards that come with control and the economies of integration. It is alleged that a price policy along these lines would have saved many cooperative marketing enterprises in Great Britain from disastrous losses. They contend, moreover, that if, after a sufficient trial, the advance payments plus the subsequent settlements do not compare favorably with the net returns which members could have obtained by marketing through other channels, it would always be open to them to make the necessary changes. In view of these considerations, it was urged that every effort should be made to bring home to farmers the significance of this principle of payment in order that it might become the practice of cooperative marketing organizations in the United Kingdom. Report of the Saskatchewan Overseas Livestock Marketing Commission 1927, *Sask. Dept. Agr.*, p. 193.

about them. This is not true, however, of all associations, nor is the above view universally accepted.<sup>6</sup>

A number of other disadvantages may be briefly mentioned—there is the danger of overpayment since the cooperative's funds are involved and not the manager's. Also it is conceivable that overpayment on one farmer's products or on one commodity is made up by underpayment on another's. Still further, it may happen that products are sold by the association more rapidly than would otherwise be done if the demand for ready cash for future purchases were not pressing.

## II. SELLING FARMERS' PRODUCTS ON INDIVIDUAL ACCOUNT

The second method of paying farmers for products differs fundamentally from the one just described. Under this system the identity of each farmer's products is maintained, and, after the products are sold in the terminal market and expenses deducted, the net proceeds are returned to the producer. The farmer, not the association, bears the risk of price changes from the time the products are received until sold in the market. The association simply acts as an agent and not as a merchant middleman.

It is reported that in 1920, three local cooperative potato marketing associations in Minnesota sold potatoes for growers on a commission basis. Cotton cooperatives now permit their members to have their cotton sold separately by the associations under the so-called "call pool."<sup>7</sup> For example, the Mid-South

<sup>6</sup> In BLACK, РОБОТКА, and MILLER, *op. cit.*, p. 30, we find these statements: "Some people object to the method of buying for cash and claim that it is not cooperation at all, or that it is suited to a grocery or supply business, but not to a marketing business. Neither of these objections has much weight. There is little difference in practice between buying for cash and any pooling method properly refined so that it provides for differences in grades, and which arranges for advances to the growers of 80 to 90 per cent of the market value of the produce at time of delivery. . . . The real difficulty with buying for cash is therefore not that it is not cooperative, but that it calls for too good cooperation." Though there may not be much difference in practice in some cases, yet the issue rests upon the difference in spirit and principle.

<sup>7</sup> In describing the "call pool," Fetrow, *op. cit.*, p. 14, writes, "Many members choose to reserve the right to fix the base price on their cotton at their own discretion. For these the call pool is provided. Preliminary advances are made on call-pool cotton at time of delivery. At the same

Cotton Growers Association of Memphis, Tennessee, gave out the following instructions to its members concerning one of the options:

Under this option the member can ship and immediately draw the authorized advance of the association. At a later date, whenever the market price suits the member, he may order the association in writing, or by telephone, or by telegram, to sell all or any part of his cotton. The price will be fixed on the day instructed to sell, and the member will immediately receive settlement, provided the cotton has been classed. The association is obligated in no way to carry cotton in this option beyond July 1st, next.

Also under this option a shipper may notify the association to fix the price on his cotton when it will net him a definite price per pound. When the market reaches a point where the prevailing 'basis' of the association will net the requested price after deducting the expense of carrying to that time, the price will be fixed and settlement sent the member immediately.

Thus the grower under this option may order his cotton sold when a price which he names can be secured or at any time he specifies. In the event the price drops to the amount of the advance payment, the associations reserve the right to call for margins from the growers.

Livestock shipping associations follow the practice of selling cattle for each producer separately whereas calves, hogs, and sheep are ordinarily sold in pooled lots. Occasionally some farmers also wish to have their hogs weighed and sold separately by the association. In the San Joaquin Valley, hogs are sold on an individual basis by the California Farm Bureau Marketing Association through their hog auctions. Grain is stored in some local elevators and sold at a later date on order from the farmer. Some associations handle grain through their elevators and load it into cars for a fixed charge. The Rice Growers' Association of California and the American Rice Growers Cooperative Associa-

time the price which the member will ultimately receive for his cotton is agreed upon as being so many points "on" or "off" the New York futures market quotation for a specified month, the month to be designated by the member. Accordingly, the member may refer to the market quotations for this particular month and fix the price of his cotton at any time he sees fit prior to the first notice day of the futures month selected. He may transfer to a more distant futures month, under prescribed conditions, if he desires. Proper margins must be maintained by the member at all times.

tion some years ago sold each member's rice separately. In some cases the members set a minimum price below which their rice was not sold. The Pacific Egg Producers' Cooperative, Inc., a sales agency for five large-scale Pacific Coast cooperatives, sells its members' products on individual account, but the member associations pool the farmers' eggs on a weekly basis. In the cooperative associations selling deciduous fruits in California sales on the basis of the individual grower's account are most common. Two reasons are given for this: (1) Deciduous fruits are most often graded and packed on the ranches by the growers themselves; and (2) difficulty is experienced in grading some fruits even in community packing houses.<sup>8</sup>

**Advantages and Disadvantages.** There are some definite advantages of this system. (1) It enables the producer of special quality products to receive any premiums which his particular products may bring. In the absence of very narrow grades, the extra price which his fancy products bring would be lost to the producer and shared with other producers if the products were pooled. (2) It obviates the criticisms against average prices which are calculated from prorating pool receipts. Some producers invariably think their products should be in a higher grade or should receive better prices than the average pool price. By having each one's products sold separately, this type of criticism is escaped. All criticism is not, however, eliminated by this means. (3) Contrasted with the cash-purchase plan, this method requires less working capital, less expert management, and entails less risk for the association. (4) For associations that make many daily sales of produce in small amounts, sales on individual account have proved to be more practicable than on a pool basis. Such was the case in the Cleveland market where the vegetable growers' association had originally planned to sell fresh vegetables entirely on a pool basis, but which experience proved to be unworkable.

A disadvantage of the system is that (1) in some instances it requires considerable bookkeeping on the part of the association. (2) Sometimes the cost to the members is increased. In the case of a livestock shipping association's shipment, if each member's stock in a multiple ownership load were to be marked, weighed,

<sup>8</sup> ERDMAN, H. E., and H. R. WELLMAN, Some Economic Problems Involved in the Pooling of Fruit, *Calif. Agr. Exp. Sta. Bul.* 432, p. 4, 1927.

and sold separately, the losses on scale "breaks," extra shrinkage due to extra handling, and the additional commissions that would have to be charged if the practice became universal would, doubtless, offset the gains any individual might logically expect to receive. (3) It is not an organized method of selling and would make it impossible for many cooperatives to market in an orderly way. In this respect it may defeat one of the primary purposes of organizing the cooperative.

### III. POOLING PRODUCTS

Pooling is a distinctive cooperative practice, so much so in fact that the term is incorrectly applied by some to any form of cooperative marketing. Pooling means the commingling of products of many producers and, after deducting average expenses, paying the average price received for the same during a definite period, usually on a basis of established grades.<sup>9</sup> Pooling, a verb, describes a *method* of operation, a mode of settlement with those that contribute products to the cooperative. The noun, pool, is often used synonymously for cooperative. Thus, when one hears of a Wheat Pool, Tobacco Pool, or a Wool Pool, one immediately thinks of a cooperative marketing association. This has led

<sup>9</sup> For a discussion of various phases of pooling see BLACK, J. D., and H. B. PRICE, *Cooperative Central Marketing Organization*, *Minn. Bul.* 211, pp. 41-53, 1924.

CHRISTENSEN, C. L., *Pooling as Practiced by Cooperative Marketing Associations*, *U. S. Dept. Agr. Misc. Pub.* 14, 1929. Christensen describes pooling as follows: "Pooling as practiced by agricultural cooperative marketing associations involves two essential activities: (1) the mingling or grouping together under unified action or control of any function of production or marketing; (2) the determination of the results of such group action and the allocation to each participant in the pool of his share of the sales returns, service, expenses, or risks that may arise therefrom."

Federal Farm Board, *Bul.* 10, 1932, *Cooperative Marketing of Farm Products*, defines pooling as follows: "Pooling is a general term for the joint contribution of working capital by several persons, joint responsibility for risks and costs, and the sharing of profits in proportion to contributions. As practiced by cooperative associations, pooling may involve responsibility on the part of the members for costs, for marketing risks, and proportionate sharing by members in money received from the sale of products."

HULBERT, L. S., *Legal Phases of Cooperative Associations*, *U. S. Dept. Agr. Bul.* 1106, p. 57, 1929, "Pooling should be thought of as an averaging process, an averaging with respect to products, prices, expenses, or returns."

some persons to conclude that all cooperatives are pools and that pooling is a universal method of operation of cooperatives. Such is not the case, however. One can generalize and say that all agricultural pools are cooperative, but all cooperatives are not pools, as this term is narrowly defined, because they do not pool their products and sales receipts before paying farmers for their products. Ordinarily a creamery, a local fruit association, a fluid milk marketing association, or a local nut packing house association are not considered pools, yet on second thought it is seen that they are pools in the fullest sense, and might just as well be called "creamery pools," "milk pools," "fruit pools," and "nut pools."

**What May Be Pooled?** There are three things that may be pooled, (1) expenses, (2) products, and (3) receipts. Because of the universal policy of pooling some or all of the expenses in a cooperative association, this practice will be discussed first.

1. *Expenses.* Invariably expenses are pooled whether products are pooled or bought outright. This is because the marketing costs are not determinable on every unit of goods handled. Expenses of operation may be classified into (a) those directly attributable to the handling and selling of individual lots of goods, so-called "out-of-pocket expenses," and (b) those of a general character chargeable to all products sold throughout the year. Under the first, fall the expenses due to particular shipments such as the cost of ice in cars; fuel used in heated cars; commissions; transportation charges; telephonic and telegraphic expenses; shrinkage and dockage (indirect expenses); packing and packaging costs; extra labor charges; and the like. Under the second grouping, are included such general expenses as salaries, rent, directors' fees, taxes, interest payments, depreciation, repairs, and insurance. The latter are allocated against products sold during certain seasons or throughout the year and constitute the fixed expenses. These "overhead expenses" as they are also called must be pooled and prorated in some equitable manner.

As an illustration of pooling and prorating expenses the Northern Wisconsin Cooperative Tobacco Pool made a uniform marketing charge of one cent per pound of tobacco handled, and in the event that additional services of storing, packing, sorting, and processing were necessary an extra charge was made. In Arkansas, local strawberry associations charged 3 to 5 per cent

of the f.o.b. price for local expenses and made refunds at the end of the year if expenses were less than the deductions. Progressive livestock shipping associations in the northwest oftentimes charge flat-rate shipping expenses of a certain number of cents per hundredweight which are calculated to meet the shipping costs for the year. Owing to varying weights of loads resulting in different expenses per hundredweight of stock shipped, it happens that the charges deducted for particular shipments may just cover, fail to meet, or exceed the expenses for a single shipment. On the average, the costs for the year are defrayed.

The problem of determining and allocating indirect costs is increased if several products are handled, and the difficulties experienced in selling and handling various grades of produce necessitate charging more for some than for others. Whether expenses should be assessed on a percentage of value basis or on a flat sum per crate, per dozen, or per hundredweight basis presents some fine problems of management, answerable differently during periods of stable, rising, or declining prices. Calculating the costs on a value basis may be easily done and may require little adjustment from one year to another, but when one considers that the expenses of marketing and maintenance of an association are not dependent upon the vagaries of price fluctuations, it is apparent that a flat charge per unit of weight or measure is advisable in many instances. Charges on the basis of value are proportionally more burdensome on products of high value—the very ones that may actually require the least sales efforts—and the charge on a physical unit basis is relatively more severe upon the lower grade products.<sup>10</sup>

2. *Expenses and Products.* Besides pooling expenses many associations pool the products of their patrons as well. Products may be classified into (a) those that must be physically commingled in order to be handled economically by the cooperative, and (b) those that may be handled separately. In the former, fall such products as cream delivered to creameries, milk to cheese factories, milk to fluid milk marketing associations, nuts to packing houses, and grain to elevators. It would be economically

<sup>10</sup> BLACK, ROBOTKA, and MILLER, *op. cit.*, p. 35, conclude that "The best rate would seem to be a per hundredweight rate adjusted early in the season on the basis of the probable volume of business" instead of a percentage of value rate for meeting local potato warehouse costs.



impossible to make butter from cream delivered by each farmer. The small amount delivered by each producer, therefore, makes pooling of the physical commodities necessary.<sup>11</sup> In the second class fall such products as livestock, cases of eggs, sacked potatoes, fruits and vegetables in baskets, crates, boxes, and barrels, baled cotton, and crated poultry whose identity may be preserved by the cooperative. It should be observed that products which are mixed together, so that each farmer's products lose their identity, may be bought outright or sold for the individual grower separately as well as pooled with regard to sales. As far as the accounting procedure is concerned, growers who sell outright to the association or direct it to sell their products on separate account are not participating in a sales pool, although their products are physically mingled with other products. In like manner, the second class of products, though they may be kept separately and at all times reveal the identity of the producer, may be handled as pooled lots when the sales receipts are prorated. *Thus, the important feature to recognize is not whether the products of several producers are physically mingled with one another but whether, in their sale and in the distribution of the sales receipts by the cooperative, they are treated as one collective lot or several lots sold on the basis of individual ownership. The method of sale and allocation of receipts are the important factors.*

3. *Expenses, Products, and Receipts.* The chief pooling feature is that of pooling the sales receipts and later distributing these minus the deductions for expenses, reserves, and other purposes to the contributors to the pool. In doing this, any one of three distinct practices may be followed:

1. All products, ungraded, may be placed in one pool  
The same net average price is paid all members
2. All products may be graded, yet placed in only one pool  
Poolers are paid prices for separate grades on a differential basis
3. All products may be graded, and each grade, variety, style, or class constitutes a separate pool
  - a. Payment for each grade or pool may be made according to actual net prices received; or
  - b. Payment for each grade may be made on a differential basis

<sup>11</sup> Pooling of milk for the purpose of making cheese was practiced centuries ago by the Swiss and French peasants of the Jura Mountains in their "cheese rings." This is perhaps the first recorded type of pooling of farm products.

A considerable number of local cooperative associations, particularly those not affiliated with central sales agencies, do not grade their members' produce. This is generally the case in creameries and cheese factories and many livestock shipping associations. Some of the early egg circles did not grade the eggs they handled. Cream is ordinarily brought to creameries, tested for butterfat content and weighed, but not graded as No. 1 or No. 2 cream, or sweet or sour cream. Exception is found in the states where compulsory cream grading is required by law. In the creamery that does not grade the cream, all patrons receive the same average price for butterfat once or twice a month after the butter is sold and the processing costs are determined. In some livestock shipping associations, settlement is made for all calves at the same price per pound although variations in grades exist.

It is easily seen that an association that does not grade the produce, but pays all farmers alike, offers little attraction to the best and largest producers or to those who have the high quality products. Private buyers solicit the patronage of these producers and often pay them according to the superior quality they have to sell. It is to the distinguished credit of nearly all large-scale marketing associations that they have introduced grading systems and have made payments according to grade, which has been a real inducement to improve the general quality of agricultural products.

The second practice enumerated above is rather exceptional, yet is found among some local cooperatives. In some Wisconsin creameries, cream is graded into two grades at the factory, yet the two grades are mixed and churned together. After the butter is sold and the butterfat prices are calculated, the prices paid to producers of No. 1 cream are 3 to 5 cents per pound of butterfat higher than the prices paid to producers of No. 2 cream. The differential in price is determined by the board of directors, and the primary purpose for it is to place a premium on high quality cream. If a creamery has too little second grade cream to churn separately, or has no local outlet for it, or finds it too expensive to ship to distant markets, the company will very likely mix the same with the first grade cream if it is not too much offgrade. Although there is only one grade of butter made and sold, still payment for separate grades of cream on a quality basis serves

a beneficial purpose in that it encourages delivery of better cream. In this case there are several grades recognized, yet only one pool.

The third practice mentioned is the one commonly thought of when pooling is discussed, namely, grading the products, placing each grade in a separate pool, and paying producers the average price received for the products in each pool. Payment to the growers can be made on the basis of the actual returns for each grade, less the prorata expenses, or, as in some cases, on a fixed differential basis less the operating expenses. An illustration of the latter is typified by the Land O'Lakes Creameries, Inc., which grades all the butter received from its member creameries, but instead of paying the creameries the average price netted from each grade pool, a scale of prices is determined by the board of directors comparable, of course, to the actual sales prices. For years,  $\frac{1}{2}$ -cent differential for the grades below the 93 score was paid. Oftentimes these prices are determined before all the butter is sold, but existing market quotations and past experience are guides in determining the monthly prices to be paid for the separate grades. The pool prices quoted in the *Land O'Lakes News* for August of a recent year, were as follows: Land O'Lakes Sweet Cream Butter (tubs), 30.00 cents; 93 score (ripened), 29.50 cents; 92 score 29.00 cents; 91 score, 28.50 cents; 90 score, 28.00 cents. In Arkansas strawberry marketing associations that pooled each day's shipments made a flat difference of 50 cents a crate for the various grades a few years ago.

There are both advantages and disadvantages in using flat differentials. Erdman and Wellman state that

The chief difficulty in fixing a price differential as a basis for pool payments at the beginning of the season is caused by the necessity of forecasting in advance both the relative cost of handling the different grades and the relative prices at which they will sell. (This arises where the advance payment on each grade measures the full difference in price to be paid, and where all subsequent payments in all grades are alike.) . . . A second disadvantage of the arbitrary differential is that final payments on any given grade of fruit cannot be made until all grades of the fruit are sold.

Among the advantages, they point out

. . . where the commodity is extensively processed, and the selling grades are different from the receiving grades, it is evident that an

**METHOD OF ARRIVING AT AVERAGE POOL PRICES**  
**Product (Oranges, Nuts, Tobacco, etc.)**

Receipts from	Variety A			Variety B		
	Grade X	Grade Y	Grade Z	Fancies	Choice	Fair
	Pounds	Pounds	Pounds	Pounds	Pounds	Pounds
Farmer Jones.....	100	200	100	...	200	...
Farmer Smith.....	200	...	300	300	100	100
Farmer Henry.....	300	500	...	100	500	200
<b>Total.....</b>	<b>600</b>	<b>700</b>	<b>400</b>	<b>400</b>	<b>800</b>	<b>300</b>
Sales by cooperative.....	300 lb. @ 10¢ 200 lb. @ 15¢ 100 lb. @ 20¢	200 lb. @ 8¢ 500 lb. @ 10¢	400 lb. @ 4¢	200 lb. @ 20¢ 100 lb. @ 22¢ 100 lb. @ 24¢	400 lb. @ 18¢ 400 lb. @ 19¢	300 lb. @ 15¢
<b>Total sales.....</b>	<b>\$50.00</b>	<b>\$66.00</b>	<b>\$16.00</b>	<b>\$86.00</b>	<b>\$148.00</b>	<b>\$45.00</b>
Operating costs—2 per cent of sales..	\$ 1.60	\$ 1.32	\$ 0.32	\$ 1.72	\$ 2.96	\$ 0.90
<b>Net sales.....</b>	<b>\$78.40</b>	<b>\$64.68</b>	<b>\$15.68</b>	<b>\$84.28</b>	<b>\$145.04</b>	<b>\$44.10</b>
<b>Average price per pound.....</b>	<b>13.06¢</b>	<b>9.24¢</b>	<b>3.92¢</b>	<b>21.07¢</b>	<b>18.13¢</b>	<b>14.70¢</b>
Farmer Jones receives	100 × 13.06¢ = \$13.06 200 × 9.24¢ = 18.48 100 × 3.92¢ = 3.92 200 × 18.13¢ = 36.26 <hr/> 600 lb. = \$71.72	Smith receives	200 × 13.06¢ = \$ 26.12 300 × 3.92¢ = 11.76 300 × 21.07¢ = 63.21 100 × 18.13¢ = 18.13 100 × 14.7¢ = 14.70 <hr/> 1,000 lb. = \$133.92	Henry receives	300 × 13.06¢ = \$ 39.18 500 × 9.24¢ = 46.20 100 × 21.07¢ = 21.07 500 × 18.13¢ = 90.65 200 × 14.7¢ = 29.40 <hr/> 1,600 lb. = \$226.50	
<b>Total received.....</b>	<b>\$441.00</b>					
Expenses 2 per cent.....	8.82					
<b>Net.....</b>	<b>\$432.18</b>					
<b>Total paid out.....</b>	<b>432.14</b>					
<b>Difference.....</b>	<b>+.04</b>					

arbitrary differential must be established. . . . A second advantage . . . is that it enables the association to adjust the prices between the various grades, so that the returns to the growers will reflect the prices which the buyers are willing to pay for each grade.<sup>13</sup>

This is particularly the case if, as a result of rising prices, inferior products at the end of a season sell for more than did higher grade products net at the beginning of the season.

How average pool prices are calculated can be shown by a hypothetical illustration shown on page 448. In the illustration, the association credits each farmer with weight and grade delivered, and the price payable is determined from the sales actually made.

A so-called "seasonal valuation pool" has been devised to overcome some criticisms which the equidistribution of sales receipts in seasonal pools has caused especially during periods of rising prices. The handling of sales receipts in this type of pool was inspired by the desire to return to farmers a price comparable with that which they would have received if they had sold for cash on day of delivery. This particular problem arises in the event the pooling period is relatively long, if optional sales methods are available, and if the price level fluctuates. An illustration of the operations of a seasonal-valuation pool follows. A delivers one 500-pound bale of cotton on Sept. 20. The cash price on that day is 8 cents. He pools it and receives a 7 cent advance. B delivers one 500-pound bale of cotton on Oct. 10. The cash price on that day is 9 cents. He pools it too and receives an 8 cent advance. Both bales are sold in November for 10 cents net. A was advanced \$35.00. B was advanced \$40. Both sales are made for \$100. A and B are each given 1 cent a pound further advance so that each obtains the equivalent of the cash price ruling on day of delivery. Thus \$5 more is given to A and B. This leaves \$15 still to be divided of which A gets \$7.50 and B gets \$7.50. Thus A received \$47.50 and B received \$52.50. In a regular seasonal pool each would have received \$50.

#### Questions

1. Why do some farmers prefer to sell for cash to the cooperative rather than pool their products?

<sup>13</sup> ERDMAN and WELLMAN, *op. cit.*, pp. 40-42.

2. From the standpoint of the cooperative, are there any disadvantages of buying products from farmers upon their delivery? Any advantages? How would you answer this question from the standpoint of the producer-member?

3. In what important respects does "selling farmers' products on individual account" differ from "buying for cash"? From pooling the products and sales receipts?

4. Why is it that *all* cooperatives pool either all or part of their operating expenses even though they may not pool the products and sales receipts?

5. What three operations does pooling involve?

6. What advantages are there in the seasonal-valuation pool over the usual seasonal pool involving equidistribution of net receipts?

7. What practices are sometimes followed in dividing the net sales receipts among the members who delivered different grades of products?

8. Examine the house organs or reports of different cooperative associations and list the different kinds of pools that are conducted.

9. For what class of farmers do you think it would be especially advisable to pool their products if the option of pooling or outright sale were available?

10. How do you explain the fact that pooling is an averaging process?

## XVII

### *Pooling Agricultural Products.—(Continued)*

*Pooling, to be successful, must treat all contributors in an equitable manner, must operate economically, and must make efficient merchandising possible. Its chief purposes are to distribute marketing risks among the pool contributors, to enable the management to market in an orderly manner, and to effect economies in distribution. To do these things necessitates careful consideration of the area to be included within a pool, the length of time over which a particular pool is to operate, the accurate grading of the products placed in the pool, and a judicious allocation of the costs of marketing over the products pooled. Usually a partial payment, called an "advance payment," is made to patrons when products are placed in a pool. A final payment is made when all of the products in the pool have been sold.*

*Agricultural marketing pools differ from the early railroad and industrial pools which were declared illegal with the passage of the Interstate Commerce Act and the Sherman Antitrust Act. Statutes on cooperative marketing permit pooling. Some early leaders of cooperative marketing considered marketing pools as media of market manipulation, but in the recent decade the intelligent cooperative leaders have not considered pooling as an effective method for arbitrary price fixation.*

*Farmers' purchasing associations often pool members' orders for farm supplies before any goods are bought. Pools for the purchase of feeder cattle, calves, and lambs have been in operation since 1925. In some countries compulsory pooling of farm products is required by law, but such compulsion is the antithesis of cooperation.*



## CHAPTER XVII

### POOLING AGRICULTURAL PRODUCTS.—(*Continued*)

#### PROBLEMS OF POOLING

Pooling problems run the entire gamut of being very simple to exceedingly complex. The simplest kind of pool would be one in a local association handling only one kind, variety, class, or grade of product for one market day in a small local area. But complexity is increased by an increase in (1) the kinds of products handled; (2) varieties of each product; (3) the number of classes or grades of each variety; (4) by an expansion of the territory or area served by a cooperative; and (5) by an extension in the length and number of the pooling periods. Pooling problems of a local association are fairly simple in comparison with those of a central marketing association. Financing of pooled products also becomes more complicated as the pooling operations become more involved.

Erdman and Wellman state very well the numerous economic problems that arise in pooling in the following terms:

The selection of a pooling plan involves a decision as to the number of grades to be used as a basis for pooling, the amount of territory to be included in the pool, and the length of the pooling period. Each of these is capable of independent variation; thus a grade may be wide or narrow, the area in the pool may be confined to one locality or it may extend over the entire state, and the length of the pooling period may be for a day or even less or it may be for the entire season. Consequently, it is necessary to analyze the ways in which variations in the grades, the area, and the pooling periods affect the functioning of the organization; in particular their effect upon the following points must be given careful attention:

First, will the pooling plan enable the association to operate in a way that is fair to the members? That is: (1) does it provide the proper differential between members, when variations exist in the quality of the product and in the time of maturity because of varying efficiency of the individuals and because of the differences in climatic and soil conditions? (2) Does it distribute the marketing risks equitably among the members?



(3) Does it provide for the equitable prorating of the expenses among the members?

Second, will the pooling plan enable the association to operate adequately and efficiently? Does it give the management the necessary control of the product as to time, place, and new markets, and the power to bargain advantageously, and does it tend to reduce the costs of operation?<sup>1</sup>

To this may be added a third consideration, will the benefits of pooling offset the additional costs that may be incurred?

In order that all producers may be treated as fairly as possible, it is necessary (1) to have as many separate grades as are recognized by the buyers in the market and for which different prices ordinarily exist; and (2) to have sufficient products of a marketable quantity within each grade so that the additional costs of selling the individual grades do not exceed the extra returns. The narrower the grades, the greater is the possibility of returning to each producer the price which his individual products netted, but from a practical marketing standpoint, the number of grades should relate to those recognized by the buyers and to the number that can be economically handled by the association. To rely upon the good products to sell the poor would certainly dampen the interests of the producers of high quality products in an association indiscriminately following such practice.

Successful pooling is predicated upon: (1) carefully grading the products; (2) having proper length of pooling periods; (3) delimiting pooling areas to proper sizes; (4) instituting accurate accounting systems; (5) correctly allocating costs; (6) paying according to grade; (7) adequate financing of the pooled products; (8) skillfully merchandising the products during the pool periods; and (9) treating all areas and individuals equitably and impartially at all times. Modifications or additions to these general requirements will be found in individual instances. Thus the merits of any pooling plan are judged (1) by the fairness with which each pool contributor is treated; (2) by the efficiency with which the marketing is effected; and (3) by comparing pooling expenses with the returns.

<sup>1</sup> ERDMAN, H. E., and H. R. WELLMAN, Some Economic Problems Involved in the Pooling of Fruit, *Calif. Agr. Exp. Sta. Bul.* 432, p. 5, 1927.

## LENGTH OF POOLING PERIOD

Products may be pooled for different periods of time, varying in length from the shortest or single-shipment pool to the longest or annual pool. Variations in the length of pooling periods are for the purpose of equitably distributing receipts to producers. Different pool durations and typical illustrations of each are the following:

1. Single-shipment pool—livestock
2. Daily pool—strawberries, many vegetables
3. Semiweekly pool—potatoes
4. Weekly pool—eggs, onions
5. Semimonthly pool—butter
6. Monthly pool—butter, cheese, citrus fruit
7. Seasonal pool—peaches, prunes, apples, cotton
8. Annual pool—wool, tobacco

The period in which prices are pooled does not always coincide with the period for pooling expenses. It would create much dissatisfaction if, for example, high shipping charges were exacted of shippers in lightweight, "mixed" cars of livestock, and lower charges of those who happened to ship in heavy, "straight" carloads. While it is better to pool shipping expenses for livestock on a seasonal or yearly basis, it is advisable to pool the sales receipts of each shipment.

The factors that influence the length of the pooling period for sales receipts are (1) the character of agricultural production, (2) the kind and characteristics of the commodity, (3) market conditions, (4) the wishes of the producer-members, and (5) the judgment of the management. Whether expenses are out-of-pocket costs or general overhead costs will determine the length of the pooling period for expenses. The former will coincide with the length of period in which the sales receipts are pooled and the latter will cover usually a 12-month period.

1. Pool periods for certain products are determined by the nature of agricultural production. Thus, for products such as tobacco, wool, walnuts, pecans, and cotton that are harvested once a year, the seasonal pool has been practicable. For products produced continuously throughout the year such as milk, livestock, poultry, eggs, butter, and cheese, the pooling period is influenced by other factors such as monthly or seasonal price

changes. Similarly for products that are not all matured at the same time, such as early and late potatoes, early and late cranberries, fruits, vegetables, and berries, different pooling periods are needed than for those commodities mentioned above.

2. Characteristics of the commodity itself are important. Perishable commodities have shorter pool periods than products easily stored. Strawberries, tomatoes, peaches and pears are on the market for a short time as compared with oranges, nuts, and dried fruits. Products that are perishable and must be sold immediately after harvest, and have extreme price fluctuations, have very short pool periods. If part of a crop such as fruit is sold as fresh fruit and a part is processed, cold packed, or quick frozen, the pool period can be lengthened as a result of the longer marketing period. Semiperishable and nonperishable commodities that can be stored also have longer pool periods.

3. The nature of the market is also to be considered. If the market is characterized by relatively sharp and sudden changes in price, or by distinct early-, mid-, and late-season prices, the pool periods must be adjusted accordingly. If a grower takes special pains to obtain the advantages of early-season prices, it would be unwarranted to require him to take an average price of a long pool period. For him a daily pool or single-shipment pool would be most equitable, and possibly even necessary to attract his membership. Thus, in a livestock shipping association prices are pooled most fairly on a single-shipment basis or at best on a weekly basis, because prices fluctuate so much. Cooperative egg marketing associations in this country pool on a weekly basis as do the Danish cooperative butter-export associations. A daily pool is used for strawberries.

In some instances pooling becomes absolutely necessary as a result of differences in prices in various markets. If an association sells in more than one market on the same day and these markets return different net prices for the same grades of products, it is only fair to all shippers that the returns from the several markets be pooled and the average prices and the average expenses be prorated. To do otherwise would certainly cause dissatisfaction. This problem rarely arises for a commodity such as fluid milk which has only one regular city market outlet, except as the individual dealers may pay slightly different prices within the same market.

4. The length of the pool period is also influenced by the wishes of the members of an association. Following the termination of the first contracts among the cotton producers which required pooling on a seasonal basis, new contracts containing optional selling methods were drawn up. These optional sales methods were provided to meet the demands of growers, part of whom could not very well wait until the final settlements were made in the seasonal pools. In one instance a daily pool was adopted by an egg marketing association in order to meet the demands for immediate cash. Some of the early large-scale cooperative potato-marketing associations failed partly because the pool periods were on an annual basis, whereas special shorter pool periods for particular varieties of potatoes would have been more desirable. The interests of the potato growers, the nature of the market, and the special characteristics of the products were not sufficiently considered.

5. The judgment of the management of the association must also be considered in determining the length of the pooling period. The task of the management is to market the crop of the growers to the very best possible advantage. It faces a dual problem, (a) to get the highest average net price for the *whole crop*, and (b) to secure as good or better prices for the individual growers as they could get from other sources. Though it faces these two problems, it will ordinarily attempt to obtain the first, knowing that a cooperative cannot meet the exceptional bids tendered a few producers. To secure the highest average net price for the whole crop of its members requires that the management must be permitted to time the movement of the crop to the market in such a way as it believes will achieve this result. Short pooling periods may defeat a well-planned merchandising program. The withholding power in a bargaining transaction is greater if the management of the association has considerable time to market the commodity.

Some illustrations of different pooling periods may be cited. The table on page 457 shows different pooling periods for fruit and vegetable associations.

Cooperative creameries and cheese factories usually pool on a monthly basis. The eggs received each week by the egg and poultry associations in Washington, California, and Utah are pooled by grades and each week's receipts are paid for separately.

Most of the local strawberry marketing associations in the Ozarks pool on a daily basis, while about 5 per cent use a seasonal pool. In the turkey marketing associations of the West single-shipment pools, Thanksgiving pools, Christmas pools, and postseason "clean-up" pools are found. One organization's

TABLE XIX.—RELATIVE USE OF POOLING PERIODS OF DIFFERENT DURATIONS MADE BY 478 FRUIT AND VEGETABLE MARKETING ASSOCIATIONS, 1922\*

Commodity groups	1 day, per cent	2 to 3 days, per cent	1 week, per cent	8 to 15 days, per cent	1 month, per cent	One-fourth of season, per cent	One-third of season, per cent	One-half of season, per cent	Season, per cent	Number of associations reporting
Apples.....		2.6						10.2	87.2	39
Citrus fruit.....		0.7	7.3	12.0	22.0	15.3	8.0	4.0	30.7	150
Grapes.....			35.7		7.1				57.9	14
Strawberries.....	59.2	7.4	7.4						26.0	27
Peaches.....			14.3	14.3					71.4	7
Cranberries.....			20.0						80.0	5
Miscellaneous fruits.....								25.0	75.0	4
Several fruits.....	11.2		12.5	2.5			1.3		72.5	80
Potatoes.....	14.6	12.5	29.2	8.3	10.4		4.2	2.1	18.8	48
Sweet potatoes.....			8.0		8.0		4.0		80.0	27
Watermelons.....		83.3		16.7						6
Onions.....			75.0						25.0	4
Miscellaneous vegetables.....	18.2		9.1	9.1	9.1				54.5	11
Several vegetables.....	33.3	4.2	20.8	4.2	4.2				33.3	24
Fruits and vegetables.....	21.9	6.3	15.6	3.1	18.7				34.4	32

\* MCKAY, A. W., and W. J. KUERT, Management Problems of Cooperative Associations Marketing Fruits and Vegetables, U. S. Dept. Agr. Bul. 1414, p. 36, 1926.

Christmas turkey pool opened on Nov. 27 and closed Dec. 12. Preseason pools were also considered. Such short-term pools are due to the fact that turkeys are a specialty and obtain specialty prices. The Mid-South Cotton Growers Association in 1931 announced a so-called "suspense pool" in which the member placed his cotton until such time when he chooses one of the optional sales methods (not later than Dec. 1). All potatoes sold by the Michigan Potato Growers Exchange and the Colorado Potato Growers Exchange are pooled daily. The local potato growers' associations that are members of the former exchange have pools of varying length—carlot, weekly, monthly, and seasonal.

## AREA COVERED BY POOLS

The area covered by a pool may be that served by a *local* association, a whole *district*, or even the *entire producing area* served by a large-scale cooperative. The reason for having pools serve different areas is to recognize differences in the quality of products, trade preferences, and local considerations which a system of grades, that may be ever so fine, does not bring out sufficiently. The ultimate purpose is to treat members of the entire association on the most equitable basis. Particular varieties, influences of certain geographic factors upon a product, peculiar care which a certain class of growers may give to a commodity, and special market outlets are factors that a general grading system may fail to recognize properly and yet are important to the producer and buyer. The sheer difficulty of having identical grades used throughout the area served by the cooperative makes it desirable to have separate pools for each of the distinct areas. Smaller area pools thus tend to perpetuate local distinctions. The problem of differences in area pools arises very largely in the federated and centralized types of associations.

In the Federal Trade Commission's Report on Cooperative Marketing, the comments on pages 304 and 305 relative to the defunct Minnesota Potato Growers' Exchange illustrate the necessity of having pools for different areas served by the association.

The organization ignored the existence of three separate potato-raising districts in Minnesota, each with distinctly different marketing problems. The best known district is the Red River Valley, in the northwestern part of the state, where the famous Red River seed potatoes are raised. The states southwest of Minnesota as far as Texas depend largely on the Red River district for their seed potatoes. It is estimated that about one-half of the potatoes raised here are warehoused, to be placed on markets in various districts for early spring planting. In the eastern part of Minnesota, where the soil is sandy, a different kind of potato is raised, which cannot be stored for winter use and must be marketed in the fall. It is generally sold in Chicago territory because of favorable freight rates. In the central part of the state a good winter eating potato is raised, which is stored after harvest for winter consumption. This district does not have as favorable freight rates to Chicago and other markets, and is at a disadvantage in this respect.

In the same publication on page 308, it is pointed out that one of the serious weaknesses of the Dark Tobacco Growers' Association was the failure to recognize five distinct producing areas in the dark tobacco district. Each of the five types of tobacco produced in the respective areas had its particular market outlets and required special treatment to meet the demands of the market. Some types sold more readily than others. Much dissatisfaction was created by putting the products from all areas in one pool for some growers believed they were sharing the burdens of other sections whose tobacco was stored a longer time. Five separate pools on the basis of area would very likely have been better than one all-inclusive pool.

Advantages of local pools have been mentioned, and it may be added that the smaller the pool area the greater is the risk and responsibility which each area must carry. The grade, pack, and general condition of the products determine each area's returns, for these will not be averaged in with the products of other areas. Each area, therefore, stands on its own reputation. This factor also points out one of the possible disadvantages of local pools, namely, that in absence of central authority which is usually found in larger area pools grading, packing, sorting, and general preparation for market may not be so rigidly or intelligently carried out as the central management desires. From the point of view of the management, it may be far better to have larger pool areas so that the products of each area do not have to be sold separately and thus complicate a merchandising program. On the other hand, it may cause very little difficulty as is indicated by the experience of the California Fruit Growers' Exchange that recognizes local and district pools. Local pools are found primarily among associations that handle fresh citrus and deciduous fruits, while pools covering large areas are found principally among associations handling dried fruits and nuts.

In the Utah Poultry Producers Cooperative, Salt Lake City, eggs from its 20 local receiving stations are pooled weekly in one large sales pool, but the expenses of operation, aside from that of the central sales organization, are pooled for each receiving station separately. In cases of this kind expenses are pooled by local areas, but sales are pooled for the entire membership area.

## LEGALITY OF POOLING

The legal right to pool farm products is not specifically stated in the cooperative marketing statutes, but that privilege is granted by indirection. The Standard Marketing Act states that: "Each association incorporated under this act shall have the following powers: (a) To engage in any activity in connection with marketing, selling, preserving . . . of any agricultural products produced or delivered to it by its members . . ." Nowhere in the section is anything stated specifically about pooling, but as an activity in connection with the marketing of agricultural products, it, no doubt, can be considered legally sanctioned. The Capper-Volstead Act does not mention pooling directly as one of the powers of an association, but it is, no doubt, to be inferred from the statement, "such associations and their members may make the necessary contracts and agreements to effect such purposes" (collective processing, preparing for market, handling, and marketing). Nowhere is pooling prohibited in the cooperative statutes.

Generally considered, the pooling of products, expenses, and receipts is valid in a cooperative association provided the members have approved it in their bylaws or membership contracts. The producers' contracts usually state whether the products will be pooled or what options are open to the members. Unless an association is given the authority to pool its members' products, it cannot do so legally. Yet there are some legal problems of pooling that have not been decided by the courts. Since the operation of a pool that is organized on an extensive basis may be a decided factor in the determination of the price of a product to the trade, by what measure may it be considered as *unduly enhancing* a price prohibited by the Capper-Volstead Act? Must each separate grade and area pool be conducted as a distinct financial entity or may the deductions for operating costs of one pool be used to help defray the expenses of another?

To these may be added: May an association neglect to deduct operating expenses from the pool sales receipts of low priced products in order that producers of such products may receive higher prices than were netted in the market and deduct the marketing expenses from the pools of the higher priced products?



**Prominence of Early Industrial and Commercial Pools.** Pools among the railroads of the United States became so prevalent during the seventies and eighties of the past century and aroused so much public opposition that in 1887 the Interstate Commerce Act was passed which forbade all types of pooling operations. Combinations among manufacturers of steel, whiskey, tobacco, and meat products, among elevator operators, and among producers of many other products precipitated so much general antagonism toward the so-called "trust movement" that in 1890 the Sherman Antitrust Act was passed which declared all contracts and combinations in restraint of trade as illegal. The purpose of these industrial and commercial pools was to eliminate competition. Gross or net receipts were sometimes pooled, territory allocated, and prices agreed upon. Pooling contracts under the common law in America have been considered as against public policy and in restraint of trade. Hence, these contracts have been considered extra-legal agreements not enforceable by the courts. With the passage of the legislation in 1887 and 1890 all railroad, industrial, and commercial pools, trusts, or combinations in restraint of trade have been declared illegal by statutory law. Size of a corporation is not in itself any indication of illegal operations. In order that the principles of the Sherman act might be modified and become enforceable Congress enacted the Clayton Act and the Federal Trade Commission Act in 1914. The "rule of reason" in interpreting antitrust act violations was established in 1911 in the Standard Oil and American Tobacco Company cases.

The Transportation Act of 1920, however, permits certain types of pooling agreements among railroads if they receive the approval of the Interstate Commerce Commission. In the industrial field, cooperative export associations operating under the Webb-Pomerene Act are permitted to pool their operations in order to compete more effectively with foreign cartels in foreign markets. In 1936, forty-four Webb-Pomerene associations were in operation. Other indications of a liberalization of public opinion toward industrial and commercial pools is shown in the passage of the ill-fated National Industrial Recovery Act (NIRA). Today, the tendency is again toward concentration in business to escape the fatal consequences of cutthroat competition. This is clearly indicated in the organization of the holding companies,

integrations of operations, giant twentieth century corporations, and numerous mergers of the decade of the twenties.

The industrial and commercial pools differ from the agricultural cooperative pools in several respects. The former have used devious ways to restrict competition, limit production, allocate territories, and fix prices, while the latter cannot limit the production on the farms of their members and are not in a position to fix prices arbitrarily. Competition among farmers is not eliminated—each still can exercise his prerogative to produce what he wishes.<sup>2</sup> Whereas the industrial pools and trusts were feared for their monopoly influences in the market, the agricultural marketing pools are generally approved as beneficial marketing agencies. In foreign countries, notably in Europe, manufacturers' pools are permitted by law. Many German cartels,<sup>3</sup> French *comptoirs*, and English business associations of both national and international scope are found in all important branches of industry.

#### ADVANTAGES OF POOLING

The advantages of pooling usually outweigh its disadvantages in either local or terminal markets. Some outstanding failures, suspensions, or reverses have befallen commodity pooling in the history of cooperative marketing. Among these can be mentioned the failures of several large tobacco pools, and the reverses of the Canadian Wheat Producers' Association, Ltd. (the Wheat

<sup>2</sup> Cooperatives can and do modify production to a degree. The large milk producers' associations with their base-surplus plans of payment in a measure affected production, but the control is not nearly so rigid or so effectively accomplished as in some industrial pools. The difficulties which the Agricultural Adjustment Administration had in adjusting production equitably and at the same time promoting the efficiency of production on separate farms attest the complications that are encountered.

<sup>3</sup> BURN, BRUNO, "Codes, Cartels, National Planning," McGraw-Hill Book Company, Inc., New York, 1934, "A cartel is a voluntary (rarely compulsory by law) contractual association, recognized by law, of independent enterprises engaged in the same field of business for the purpose of a planned regulation of the market, either in buying, marketing, or production of goods," p. 146.

"A pool is an agreement among independent enterprises to pursue a uniform policy in the field of either production, prices, or marketing; but it is not enforceable in court under common law, in contrast to cartels, which are recognized by the courts in many European countries," p. 38.

Pool). The significant fact to be found in the obituaries of these and other defunct pools is that the failures were caused by overpayment in advances, delays in payments, faulty management, disloyalty of membership, nonmember problems and relations, and many other direct reasons, rather than inherent weaknesses in pooling itself.

1. Pooling spreads marketing risks. Some farmers may possess an uncanny ability to market their products at the "top" of the market. For these, pooling has less to offer than for the thousands who consider each sale a gamble, fraught with grave uncertainties. Pooling eliminates few risks of marketing—it principally spreads them. Risks of price changes, of proper market selection, of timing the flow to market, of physical losses, shrinkages, and thefts, and of others complicate the task of marketing. In the pool all prices are averaged for each grade, the returns obtained from consigning to different markets are lumped together, and the physical losses in shipping are prorated over all pool members rather than borne by those whose products were actually affected. A pool would have little appeal to the farmer who delights in personally higgling in the market. The David Harums crave all the excitement that the risks of the market involve, but, for the thousands of growers that are satisfied with an average price, the pool has a real appeal. To the latter the cooperative pool is a type of collective insurance at cost. Instead of having each farmer be a price cutter of the other, the competition is shifted to the buyers by a pooling arrangement and a much stronger strategic position in selling farm products is achieved. In order to make the most of this averaging process, it is desirable to have pools spread over wide areas, of long duration, and include a large amount of farm produce.

2. The management is enabled to merchandise the products according to a program it considers desirable. Selling each member's products separately or buying for cash-on-delivery with the necessity for immediate resale in order to avert speculation does not permit much latitude in planning a well-laid-out sales program. Such necessities tie the hands of the management. As far as local associations are concerned such sales methods involve no difficulties, for the associations aim to show their merits in local economies of operation rather than in elaborate sales policies. For large-scale associations in which effective

selling as well as economies in handling are important, the value of pooling arrangements is significant.

Pooling permits the management to use more precaution in placing and in timing shipments to market. It enables the management to develop new markets. This is most often done at a loss when first started. In the absence of pooling, such introductory sales in new markets would be nearly impossible, for no individual member would care to sell in such new markets when others at the time are more profitable. The pool, however, faces a long-time program and must consider its sales policies from this standpoint.

An essential element in establishing prices is the withholding power of the parties to the transaction. The greater the withholding power, the more effective bargainer one can be. Pooling arrangements, in which the pool periods are long, place the cooperative in a more strategic bargaining position than the individual producers can ordinarily attain. One illustration will be cited. A certain tobacco pool unfortunately had to market many millions of pounds of low grade frozen tobacco for its members following the 1923 harvest. The tobacco buyers were anxious to take all the good tobacco, but none wanted any of the frozen. The next year's crop was even more inferior in quality and tobacco stocks in the dealers' hands became short. When the good quality crop of 1925 was cured and ready for sale, there was a great demand for it. The management of the pool, realizing its opportunities and bargaining position, required all the buyers of the 1925 crop to take fractional amounts of the 1924 and 1923 crops with each purchase of the 1925 crop. In this way the low grade tobacco was sold, owing almost entirely to the withholding power of the association.

That effective selling is oftentimes jeopardized by granting several options to the growers is summarized by Prof. William R. Camp in the following manner.

Any combination of pooling with individual consignment which permits growers to elect whether they individually will control the distribution of their product, or leave its distribution to the specialists employed is lacking in the essential elements of cooperation. . . . No policy of gradual marketing can be realized when everyone is free to sell locally or to ship when and where he pleases. Such freedom is the essence of disorganization. In selecting his own time and place of sale each grower

bears his own risk. Without pooling there is no cooperation on the part of the growers to distribute the risks, and cooperation to secure a coordination of shipments becomes impossible.<sup>4</sup>

If cooperatives are ever to stabilize prices, pooling and centralized sales control on a large scale are absolutely essential.

Through a pooling system the management can maintain a better morale of the membership. The Dairymen's Cooperative Association found that the payment of standard prices (as a result of pooling all the milk under central control) for the same grade of milk, although some was condensed and some made into cheese, butter, or sold as fluid milk, was prerequisite to successful operation. The advantages of such pooling practices were: (a) it provided a continuous market for the producer; (b) it permitted one price to all producers without discrimination; (c) it took care of the surplus; (d) it was a protection against failures of the dealers; (e) it assured the consumer at all times of a continuous supply of milk.<sup>5</sup>

3. Pooling enables the association to finance its operations more easily. Associations that pool usually make a partial payment to growers at the time of delivery of products. The products in the pool become the security for the loans obtained from banks in order to make the advance payments. The right of an association to pool its members' products and to pledge the products as security for a loan are demanded by the larger banks, such as the bank for cooperatives, before large loans are made. With access to the central money markets, it is to be expected that the large-scale association will obtain credit at lower rates than would the individual farmer were he to finance the marketing of his own crop over as long a time as taken by the pool.

The cooperative organization does not assume the financial risks of price changes for commodities in a pool, as it does for those bought outright. To this extent the problem of financing

<sup>4</sup> CAMP, WILLIAM R., *Agricultural Pools in Relation to Regulating the Movement and Price of Commodities*, *Proceedings of the Academy of Political Science*, vol. 11, no. 4, pp. 200-201, January, 1926. The authors recommend the entire article for the student's careful reading.

<sup>5</sup> MILLER, SEWARD A., *Conference on Structure of Dairy Cooperatives*, "American Cooperation, 1925," vol. 2, pp. 116-117, The American Institute of Cooperation, Washington. D. C.

is eased—particularly for those products for which no futures market exists. Under a pooling arrangement in which a partial payment is made to the grower on delivery, the producer in fact bears part of the burden of financing.

4. When a cooperative operates on a relatively large scale, it may be an important factor in determining the price of the product in the market. A number of cooperatives that pool their products and control a substantial portion of the entire output dominate the price and trade with their products either regularly or at certain seasons.

#### DISADVANTAGES OF POOLING

1. In some instances products of different qualities are mixed and settlement is made on a flat-price basis. This occurs in many cooperative creameries that do not grade the cream. To the extent that this practice is condoned by the membership, no feeling of injustice is felt by the producers. In many organizations it is difficult to educate the membership to appreciate the value of grading. The importance of grading to successful pooling of most farm products has already been mentioned.

If the grades are not sufficiently fine to pay the producer according to the market value of his particular product, his patronage may not be secured. His high-quality produce receives a lower average price, and the produce just good enough to be included within the grade receives a higher price in comparison. Such a condition suggests the advisability of restricting the area of the pool to include such producers as have a high degree of similarity in soil conditions, weather, and cultural skill. If this is not done, either the best producers will not join the cooperative or the general level of the quality of produce of the region may be lowered.

2. Many grades and variety pools may easily cost more to operate than is gained from having them. The Burley Tobacco Pool, for instance, had 52 grades and a pool for each grade. It is reported that the Dark Tobacco Growers Association had four major pools with each of these subdivided into 230 grade pools. Some pools had less than 1,500 pounds of tobacco in them while others exceeded 7 million pounds. The Mid-South Cotton Growers Association had 210 grade and staple pools. A similar problem arises from having numerous short period and small

area pools within a large-scale association, all of which contributes materially to the cost of selling and accounting for the products.

3. It happens, too, that in pooling products, short time changes in demand are not always taken into account. By adjusting the length of pool periods an attempt is made to recognize the more important changes in price, but there are often short time changes for which separate pool periods are not arranged. The prices received during such periods are averaged with the prices received during the remainder of the pool period. The seasonal valuation pool described on a previous page is one method of adjusting payments to producers who deliver products to the pool at different price levels. The difficulty of determining pool areas with precision causes some to look upon pooling with dissatisfaction.

4. In the early development of cooperative marketing in this country pooling was considered to be the key to successful market control, price fixing, and monopoly power. The early tobacco pools and cotton pools considered the possibility of market control rather than distributive efficiency as the achievement of large-scale pooling. At that time the greatest exponent of cooperative marketing held out to the members, in glowing terms, the power, the monopoly influence, and the coercive position which large commodity pools give the producers. This conception of pooling which experience has proved to be unsound in the long run is not being accepted by progressive cooperative leaders today as the greatest opportunity that pooling offers.<sup>6</sup>

5. Pooling causes a delay in payments to producers. Some tobacco growers have had to wait for their final payment on their pooled tobacco for more than five years. This invariably works a hardship on many farmers, and materially contributes to a breaking down of the membership loyalty. In some cases shorter pool periods have been adopted to overcome the short-coming of waiting so long for final pool payments.

6. Pooling may easily lead to speculative operations, which often are ruinous to an association. Pooling in itself is not synonymous with speculation, but the abuse of management

<sup>6</sup> Nourse, E. G., "The Legal Status of Agricultural Cooperation," The Macmillan Company, New York, 1928. In Chap. VII, pp. 156-161, Nourse describes this use of the pool as "The market-adjustment or manipulative pool."

privileges may lead to speculation. The management is easily accused of speculating when, during a declining market, sales are made slowly and the average net prices do not compare so well with early season prices. Where orderly marketing ceases and speculation begins is about as difficult to determine as the exact beginning and end of any color in the spectrum.

#### REACTIONS TO POOLING AT DIFFERENT PRICE LEVELS

The attitude of growers toward pooling operations is influenced partly by the character of the price level during the pooling period. Prices may be considered as being (1) relatively stable, (2) increasing, or (3) decreasing. The growers depend upon the publication of price quotations for a knowledge of these conditions. For some commodities for which no regularly quoted market prices appear in the daily press, such as tobacco and cranberries, the membership would not know with much exactness the trend of the market, and for these the following remarks are less applicable. The statements do apply to such organizations as wheat pools, cotton pools, butter pools.

During a period of relatively stable prices, members would have little occasion to find fault with the average pool price. A few would be somewhat perturbed over the fact that the pool did not sell at higher prices; but generally little dissatisfaction would be encountered. The graph (Fig. 7) indicates that market prices at times are below and also above the average prices received by the pool, the assumption being that the association sells at high and low prices during the pooling period.

During a period of rising prices, most members would be satisfied with the prices finally netted by the pool and payable to the members (assumption being that sales are made periodically during the pool period). In such a period the average pool price is above the early season's prices, but below the highest prices (Fig. 8). No doubt, some would be certain that, if they had not pooled their products, they would have held them until the end of the season and would then have sold them at the

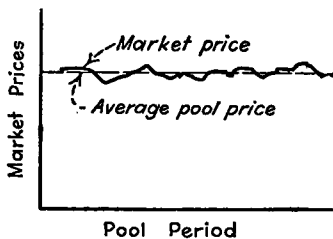


FIG. 7.



season's high. They do not realize that if many producers had done likewise, prices probably would have been higher earlier in the season and lower later. A minority will contend that the pool sold too early and should have waited until the market reached its peak before unloading the pooled products. There would be other growers, no doubt, who would remember the relatively low prices which ruled in the market early in the season and who will go so far as to credit their association with having elevated prices through their pooling operations. That the attitude of members toward the cooperative is good during a period of rising market prices is evident from the fact that the membership of many cooperatives increases during such years. The associations during such periods have few losses, their financial standings become improved, membership loyalty is manifested, and credit is attributed to the cooperatives (even if unwarranted) for the favorable price level.

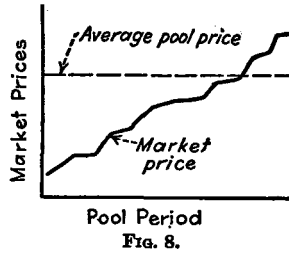


FIG. 8.

It is quite different during a period of declining prices. During such a period the pool's average price will be less than the early

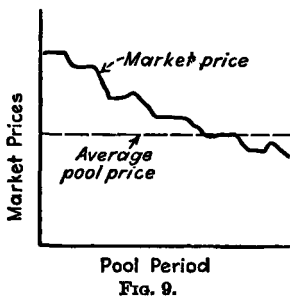


FIG. 9.

season's prices (assuming sales are made periodically during the pool period) (Fig. 9). Many producers are confident that they would have sold their products at the early part of the season when the prices were high and cannot understand why the association did not sell all of its products soon after the products were received. Others accuse the management of speculating with

their products. Nonmembers who fortunately sold at the higher prices of the season kindle the discontent of pool members by making known the higher than pool prices which were received. Consequently, many members find it to their advantage to sell as early as possible in preference to pooling their products. This is a trying period for the pool. The fateful

experiences of a number of pools during the depression period of 1930-1933 attest the general reactions of members at such times. Numerous wheat pools were discontinued for this reason shortly after 1928.<sup>7</sup>

#### POOLING AND THE PRICE LEVEL

What effect does pooling have upon the general level of prices for particular commodities? There are those who believe that a cooperative which pools is in a position to fix prices. It is also stated that if pools are sufficiently large, they will be in a position to eliminate the operations of exchanges for staple commodities, to sell directly to millers, processors, packers, and exporters, and to obtain better prices for their members than if such prices were established on the exchanges.

It must not be forgotten that prices are established fundamentally on the basis of the interaction of the forces of supply and demand. These forces determine the price level at which products will move into consumption during the usual marketing period. A cooperative may influence buyers to bid more for well-graded, packaged, uniform, and branded products that are placed with care on the market as to quantity and quality and as to the time. This is no greater opportunity, however, than is open to all food distributors. In this respect the demand is influenced. Respecting the supply, it will be seen that pooling arrangements in no way place restrictions upon the kind or amount of commodity produced, except that they do at times influence the quality or variety of the product (largely through

<sup>7</sup> FERROW, WARD W., Cooperative Marketing of Agricultural Products, Farm Credit Administration, Cooperative Division, *Bul.* 3, p. 49, 1936. "Several factors may be said to have contributed to the discontinuance of the wheat pools. One of these was the difficulty of satisfying the member with respect to the price received for his grain. A large proportion of the grain moves out of the hands of producers a few months after harvest. On an advancing market the grower takes a lower price when he sells immediately than if his grain were held for him by the marketing organization, providing storage charges; interest and other expenses do not amount to or exceed the difference. On a declining market, it is to the advantage of the producer to sell as quickly as possible. Declines in grain prices after 1928 were a decided handicap to the pool movement. Prices continued to decline and freedom of the producer to select the time for selling his crop pressed for recognition rather than the idea of orderly marketing of the grain."

the practice of paying for products on a graded basis). The same freedom respecting production exists after the pool is operating as it did before. Consequently, with regard to the total supply and its subsequent effect upon prices, the cooperative that pools exerts as little control as any large food distributor. Therefore, it is highly improbable that a cooperative using a pooling system should be in a position to elevate the price level for a long period. In this respect manufacturers' pools differ from farmers' pools for they can control production more easily and thus affect the level of prices. Farmers' pools that control the available supply may do so for only a short period, such as one marketing season or perhaps a few years. But enlarged crops, greater imports, and the increased use of substitutes will curb such influence quickly.

It is questionable whether *wholesale prices* of staple agricultural products could be elevated above those which would exist as a result of exchange (produce exchange) operations if large pooling operations are followed. *Farm prices* may be. Whether the estimate of the manager of a pool as to what is the "proper" price at which to sell is better than that of hundreds of speculators in numerous commodity exchanges is questionable. In the absence of specific comparisons, it is difficult to state which would result in higher prices. For nonstaple agricultural products for which no regular exchanges exist, there is greater opportunity for a large pool with efficient centralized control to favorably affect market prices and to return to farmers better prices than they would receive in the absence of a pool.<sup>8</sup> Successful cooperative selling of certain fruits has virtually taken these fruits out of the class of specialties and has placed them in the class of staples.

#### POOLS FOR PURCHASING SUPPLIES

In addition to the use of pooling methods for the purpose of selling farm produce, similar methods may be used for purchasing farm and household supplies. The "feed pool" conducted by farmers in the eastern states and the extensive pool operated by the Cooperative Grange League Federation Exchange (G.L.F.) of Ithaca, New York, are illustrations of the kind suggested.

<sup>8</sup> In some markets where the cooperative handles a large share of the surplus, as in some milk markets, for instance, the cooperative pool may actually pay less to its members than companies, which do not have to handle surpluses, pay to their patrons.

Under the "pool" arrangement many farmers agree to buy their feeds through their cooperative organizations, for ninety days or six months ahead on a monthly quota basis at a fixed price. Mills are thus enabled to gauge and cover their market requirements by "futures" contracts, and the farmer is relieved from price uncertainties. Being assured of a market for several months ahead, feed mills can afford to operate on a closer margin than formerly, and the farmer secures his feed more cheaply than if he bought individually.<sup>9</sup>

For many years local societies of general farm organizations have pooled the orders of their members for farm supplies and have effected appreciable savings thereby. The savings result from the wholesale price quotations obtained in place of the usual retail prices paid by farmers and from the low expenses involved in such pooling arrangements.

Since 1925, and more especially since 1930, pools for the purpose of purchasing feeders in the western range country for mid-west cattle- and sheepmen have been in operation. Each year, thousands of cattle and sheep are shipped direct from the West to corn-belt feed lots on the basis of orders that have been pooled by the cooperative livestock marketing associations.

#### COMPULSORY POOLING

Legislation providing for compulsory cooperation, which includes pooling, has existed in Queensland, Australia, since 1923. In Ireland, every dairy farmer is compelled to become a shareholder in the cooperative creamery to which he ships his cream. In New South Wales and in Canada, agitation for compulsory pooling was rife in 1928, and since 1927, all dried fruits are marketed through compulsory pools in Western Australia. In South Africa legislation provides for compulsory cooperative marketing when 75 per cent of the growers favor the same. Such compulsory action imposed upon the minority is the antithesis of cooperation, and, in fact, calling it cooperation is a misnomer.

#### Questions

1. By what tests would you judge the successful pooling of farm products?
2. Why is it important to have pools of varying lengths of time?
3. What factors must be taken into consideration in determining the area which a pool should cover?

<sup>9</sup> HANEMANN, ANDREW H., *Cooperative Buying and Selling among Farmers*, Pa. Dept. Agr. Bul., vol. 9, no. 11, p. 19, 1926.

4. In what respects did the early railroad and industrial pools differ from the agricultural marketing pools of today?
5. Why were the wheat pools of the United States discontinued?
6. Explain what is meant by the statement that the "pool is a type of collective insurance at cost."
7. Have city consumers economic justification for fearing cooperative marketing pools?
8. Would you favor legislation requiring all producers of a commodity, *e.g.*, wheat, wool, tobacco, or cotton, to market their produce through a pool conducted by a cooperative association? Give your reasons.
9. What shortcomings can you point out in the methods of conducting agricultural pools which have undermined their importance in some instances? Cite cases within your own experience.
10. Is pooling the *sine qua non* of successful cooperative marketing?

## XVIII

### *Sales Policies*

*The rise of the middleman is spontaneous wherever consumers and producers are willing to remunerate him for performing specialized marketing services which they do not choose to do themselves. In many countries, particularly in the more primitive rural areas of the world, the market place is as much a social center as it is a place to barter. Likewise, American agricultural markets in earlier times were simple in structure and almost primitive in methods of operation.*

*In the early stages of commercialization, the middleman generally found himself in an advantageous position to appropriate the conjunctural gains and take a large share of the profits resulting from the improvements made in the technique of distributing agricultural products. As a class, they zealously guarded their position from encroachments by other types of marketing agencies which jeopardized their profit margins. Their efforts to maintain a status quo has been a retarding influence in the development of a more effective distribution system.*

*The cooperative associations that were formed in the last quarter of the nineteenth and the first few years of the twentieth centuries were too localized to have influence in the central price-making markets. They provided the means, however, for producers or consumers to work out a superior technique in handling and preparing products for market as well as in perfecting a sales program. Since 1921, local associations have rapidly consolidated their position by forming central organizations, and the integration in agricultural marketing agencies has been extended both horizontally and vertically.*



## CHAPTER XVIII

### SALES POLICIES

One who is accustomed to living in an industrial and commercial center today is amazed at the simplicity of early exchanges negotiated at pioneer crossroads and is impressed by the fact that our present complex commercial system has grown out of the barter transactions of the past. The growth of commerce and the effects of trade upon our civilization are a theme dramatized in the numerous pageants presented at centennial anniversaries.

It is commonly assumed by laymen that it takes only two persons, buyer and seller, to consummate a bargaining transaction. The simplest transaction involves no less than four persons, buyer and seller, as well as potential buyer and potential seller. The fifth figure, the court, remains in the background, ready to arbitrate any disputes that arise from the intercourse. The bargaining transaction is defined as a voluntary agreement between two persons of equal legal rights to transfer title of ownership in economic goods or services from one to the other.

Surpluses are produced in the ordinary routine of a self-sufficing economy because of frugality on the part of the husbandman, favorable growing seasons, chance selection of crops and seeds, and, in some regions, because of precautions that are taken against the possibilities of starvation resulting from crop failures. In earlier days, when surpluses exceeded anticipated needs, the producers within a community began to exchange goods in kind. Thus, the man with too much corn arranged a trade with the individual who had more wool than he needed. This type of transfer is called "barter."

The barter transaction is characterized by a simultaneous transfer of physical goods and legal title to the goods from one person to another. The aphorism, "Possession is nine points of the law," has its origin in the fact that physical possession was regarded as the best evidence of legal title. During centuries of primitive trade, the necessity of possessing and displaying physi-

cal goods at the place and time of the sale or exchange restricted an individual and hampered him in arranging transfers in ownership. While individuals were thus shackled, commerce languished within narrow confines.

The invention of a medium of exchange enormously facilitated trade. The use of gold, silver, and other precious metals universally accepted as superior in portability, stability of value, durability, malleability, divisibility, and cognizability, and the use of simpler forms of exchange media ranging from amber beads to zinc disks, created an opportunity for a middleman to negotiate between individuals trading articles not needed by them for others which they wished to possess. By the use of a medium of exchange, the barter transaction was divided into two component parts. The middleman's function made it both feasible and possible to transfer titles independent of one another, with respect to both time and place. After this step was taken, it was not long before man realized that transactions tend to cancel one another, thus permitting much greater economy in the use of a medium of exchange. Instead of incurring the risk involved in carrying and transferring large sums of money after each transaction, traders substituted records of the credits and debits. These were balanced daily, weekly, or monthly, and the difference between income and output was transferred from the debtors to those having credit balances in their favor. This system of trade required confidence in the credit rating and integrity of those receiving goods or extensions of credit. It was necessary, therefore, to introduce an element of safety for the rights of the individual who was willing to divorce himself from physical goods or money and to deal exclusively in titles to goods. Such safety was provided by trade guilds and commercial organizations which established their own code of rules and regulations. The State, through its power to maintain law and order, helped to adjudicate disputes in its courts.

The local buyer system for the assembling of farm products is prevalent in farming districts throughout the world. The individual enterpriser who buys products from the agriculturists, either for himself or others, is inclined generally to grasp whatever advantages he can in the bargaining transaction in order to offset losses and compensate himself for his time and effort. The farther back the trader journeys into the hinterland, espe-



cially into the undeveloped regions where commercial methods are novel, the more imperfect the market becomes. The sellers lack the necessary information and alternative market opportunities to develop a keen appreciation of market values. Wide variations in price prevail wherever there is a dearth of market information. As soon as the producers in a given area realize that they may improve their economic status by giving closer attention to methods in trade, as well as to adjustments to market requirements, they begin making progress towards a more perfect market, a market in which transfers are arranged with the maximum degree of efficiency.

#### A PERFECT MARKET

*A perfect market is one which is open to all who wish to trade. It is an institution in which the buyers and the sellers at any instant enjoy equal bargaining power as well as complete freedom in transferring titles to ownership.* The Marshallian type of perfect market is limited to an area in which uniform prices prevail and in which allowance is made for small variations in transportation costs.<sup>1</sup>

The economic status of bargaining groups may vary greatly within large metropolitan markets like London, New York, Berlin and Chicago. Even within a few city blocks farm products of identical quality may sell at the same time at different prices. Price spreads may be the result of chance meetings of buyers and sellers and are neither necessarily consistent in amount nor characteristic of particular places. Likewise, trade in wheat or cotton futures of the same grade on the same exchange may vary appreciably in price within a few minutes, and these prices will have no semblance of uniformity in successive transactions.

As one might expect, gross inequalities in bargaining power exist between the nomadic Tibetans living on the steppes of Asia and the traveling merchants from Turkey, China, or Russia. However, similar inequalities are to be found between

<sup>1</sup> MARSHALL, ALFRED, "Principles of Economics," 8th ed., p. 325, Macmillan & Company, Ltd., London, 1925: "Thus the more nearly perfect a market is, the stronger is the tendency for the same price to be paid for the same thing at the same time in all parts of the market; but, of course, if the market is large, allowance must be made for the expense of delivering the goods to different purchasers, each of whom must be supposed to pay in addition to the market price a special charge on account of delivery."

Iowa farmers and certain local hog buyers. It is as possible to justify a dollar per hundredweight difference in simultaneous transactions for the same grade of cattle at the same place in pastoral Tibet, as it is to justify a difference of a dime per hundredweight in an agrarian American state.

Inequalities occur in markets not only because of the lack of information but also because of the jealous guarding by a select group of persons of the rights to trade under the guise of established customs or rules such as those formerly imposed by commodity exchanges. (Chapter XI, pages 285 and 286, describes some of the difficulties producer associations encountered in gaining recognition in the great markets of the world.) Other restrictions against either the transfer of title to goods or the physical delivery of goods often limit the freedom of a market and affect transactions unfavorably. Large numbers of producers and consumers here and abroad have shown a preference for a type of corporate control which enables them to direct purchases in their own interest. These enterprises began as small local associations but after attempting to organize sales cooperatives, many producers learned that the problems of selling were much more involved than had been apparent during the middleman's performance of the function.

#### SALES BY LOCAL ASSOCIATIONS

Local associations usually follow the path of least resistance in their sales policy. They sell to any individual or agency, with the exception of private competitors in the local market, and at any place or time that an acceptable agreement as to price and terms of settlement can be made. The usual market outlets for local sales are:

1. To consumers direct—private individuals and institutions
2. To local assemblers—livestock buyers, grain dealers, and truckers
3. To local manufacturers—processors of meats, milk, and fruits

Local associations affiliated with central sales associations sell their products through the latter.

Unaffiliated local associations which receive a volume of products in excess of home requirements generally sell the surplus through terminal sales outlets, such as:

1. To middlemen in central markets—wholesalers, brokers, jobbers, and commission men
2. To auction companies
3. To large buyers direct—manufacturers, public institutions, and retail organizations

After a period of time the various markets are roughly classified according to such characteristics as: expenses incurred in making sales, special commodity preferences, difficulties in making collections, risks of rejections, inconveniences in settling claims and making credit adjustments. The various sales agencies are likewise evaluated for their effectiveness in making favorable returns and in rendering marketing services.

The organized apple growers, for example, may choose one or more of the several market outlets to bring their crop to the consumers. They may sell carload lots of apples, which are packed in boxes, barrels, or baskets, to a wholesale dealer in a major market, who in turn sells to jobbers or retail organizations. The association could in this case eliminate one step by selling directly to the jobber. A large volume of apples is sold through a receiver who represents the shipper in the fruit auctions. Auction organizations selling apples are found in thirteen different city markets of the United States. In some of the largest cities from fifty to ninety per cent of the sales are made through them. The receiver's usual charge is 5 per cent of sales, 2 per cent of which he pays to the auction company. Since the motor truckers have recently become important factors, new outlets have been opened in such markets as Boston and Philadelphia, where truck sales may exceed 40 per cent of the total receipts. Brokers are often active agents in bringing buyers and sellers together for a fee of \$20 to \$30 per car. The local associations in some instances sell directly to chain stores and independent retail outlets, including both roadside stands and large consumers. Local associations may make sales through their own central sales companies. Finally, sales can always be arranged on a consignment basis to a commission house. The potential market for most commodities is so great in contrast to the portion which can be supplied by a small local association, that the seller becomes confused in a maze of market data and administrative detail.

Extensive sales are more subject to conjunctural gains than intensive sales because of the inaccuracies in collecting market information, and because of such unpredictable natural causes as floods, sleet storms, and fires which result in shortages of supplies and high prices to the buyers. The conjunctural gains, however, may be offset by unforeseen losses. It is not an uncommon occurrence for prices to fall 10 to 25 per cent in fruit and vegetable markets because of heavy shipments from growing areas and the concentration of such supplies in a few markets.

Sales costs are generally much higher where a policy of extensive distribution is adopted. When the sales effort is confined to an irregular group of buyers in an extensive market area, competitive resistance must be overcome; moreover, transportation costs are higher, and repeat orders may be much less frequent. Local associations have a tendency to gravitate toward a small corner of a large market area where business relations can be maintained more satisfactorily.

In determining a policy, certain economic conditions must be taken into consideration as well as whether or not the association has certain natural advantages within the specified demand area. What will be the nature and the severity of competition that is certain to be encountered? Will any changes be required in methods of handling, grading, packaging, and delivering the product in order to satisfy customers? Such questions must receive consideration in the formulation of a sales policy.

After determining the characteristics of a market and the ability of the organization to supply products of a certain quality within a particular period of time, the manager and directorate can then select the agencies to assist the local association in the sale of its products and in the development of potentially advantageous markets.

*The bargaining leverage which producers are able to exert through their local associations tends to decrease as the distance to delivery point becomes greater and as the size of the market increases.* While this rule may not apply in all cases, it does, however, in most markets, because the control of supply is difficult and the costs of administering marketing functions tend to increase in proportion to the distance to consuming centers. Equality in bargaining power is approached by concentrating a larger part of the supply under the control of one sales organization. The use

of modern scientific methods in merchandising will also avert selling commodities on buyers' terms. This point of view is expressed in an annual report of one of the well-known fruit exchanges of the country:

In order to get the full value of any crop it must be distributed with due regard to general marketing conditions, in proper proportions and at suitable times, to the various consuming sections. This is a problem which cannot be solved successfully by individuals or agencies acting independently. Only by that unified control of distribution which cooperation makes possible can we avoid waste and achieve success.<sup>2</sup>

Furthermore, the degree of control recommended by the president of this seasoned cooperative organization cannot be easily accomplished by an inexperienced group of federated local associations. It would be useless to talk about reform in market practices and the substitution of order for chaos in directing the flow of commodities to the millions of consumers of the country without first obtaining the *intelligence* necessary for such a sales program.

Producers sensed the fact that the possibilities of local organization were limited primarily to efficiencies in assembling, grading, processing, and performing other similar marketing services. They have always believed that the golden opportunities for organized agriculture rest in active participation in the function of determining prices in the central markets. One of the most exciting chapters in the history of sales associations in North America is the account of their bitter struggle against entrenched interests in the central markets. In such agrarian regions as the wheat producing provinces of Canada and the dairy and livestock states of the Middle West, the attack against boards and exchanges *where prices are made* had been along a broad front. The reforms which were induced by indirect means, such as commissions of inquiry, legislative hearings, discretionary orders, mandatory laws, and governmental regulations, did not suffice. They petitioned the market barons for seats on the boards where they might see how prices are made as well as participate in the function which so vitally affects their welfare. They sought to

<sup>2</sup> BRIGGS, G. R., *Annual Report Crop Season, 1928*, American Cranberry Exchange, New York.

reform market institutions from within as well as from without.<sup>3</sup> Those who served agriculture in this cause did so with an ardent zeal and an earnest devotion to the principle, *that no individual or group in society has any rights which supersede those of the producers in naming the price of agricultural products*. Naming the price, however, is not tantamount to fixing it. In all fairness to the practical-minded farmers of the country, it can be said that only a minority (a very few) expected to realize miraculous results from a seat owned in some central market. Nevertheless, the majority saw no harm in *maintaining someone* on the exchanges; in fact, most of them heartily approved of the idea. They accepted the principle of prior rights with scarcely a dissenting vote.

The mere presence of the farmers' representatives on grain exchanges, livestock terminals, and dairy boards is doubtless of more significance than the influence exerted by the volume of sales or the number of transactions completed. It is not implied in this statement that association memberships on exchanges had a beneficial psychological effect on other traders. Neither is it intimated that producers' suggestions for changes in the corporate organization and management of these markets, excepting the rule prohibiting rebates of commissions in the form of dividends, were forced upon an unwilling trading fraternity.

Organized agriculture did not fully anticipate the wealth of information that could be released in an uninterrupted flow to farmer members throughout producing areas by virtue of the association's position on the exchanges. The forces which make for price determination are focused at a limited number of primary markets such as Winnipeg, Liverpool, Chicago, New Orleans, and New York. Wide public interest in buying and selling is made possible by an efficient system of disseminating information. Many large corporate groups, however, may regard such general information as an inadequate and unsatisfactory basis for making purchases and sales. Veteran professional traders would be reluctant to make commitments on such meager information. Therefore, these corporations and indi-

<sup>3</sup> For an excellent account of the dramatic struggle of Canadian wheat farmers for recognition and a place on the Winnipeg Grain Exchange see Harald S. Patton, "Grain Growers' Cooperation in Western Canada," pp. 43-44 and Chap. V, Harvard University Press, Cambridge, 1928.

viduals provide for supplementary sources of market statistics and additional assistance in interpreting all available data. A thorough knowledge of the conditions of supply and demand makes advantageous buying and selling possible and prevents "rigging the market."

#### **PRICE DETERMINING MARKETS REQUIRE A HIGH DEGREE OF ORGANIZATION**

The less organized and the more diffused a market system is, the more imperative it becomes for sellers and buyers to rely on their own resources in gathering facts from which to form judgments on the relationship between supply and demand. Agricultural producers regard the wholesaler's position as the nerve center of either a discrete or integrated series of marketing agencies. It constitutes the narrow pass at which commodities from farming areas converge and from which they are distributed to consumers. Since the World War, agriculture has suffered a depression, and producers everywhere have felt the need for organization to influence prices and maintain equality in bargaining power. Encouraged by favorable legislation and numerous agencies created for the purpose of fostering and developing integration in cooperative sales, large numbers of independent local associations have been combined in district, regional, and national organizations.

The general sales policies adopted by some of the large-scale cooperatives are briefly described to illustrate the heterogeneity in methods of approach in consummating transactions for some farm commodities. Each method may be the most effective one known for favorably influencing prices in the particular type of market organization evolved for marketing certain products.

#### **SALES POLICIES OF LARGE-SCALE ASSOCIATIONS**

Sales policies adopted by cooperative associations are so variable that they defy a rigid classification. Nevertheless, it is desirable to divide them into separate categories for convenience in comparison. One way of contrasting the various methods is illustrated in the following outline:

1. Cooperative selling through the existing middleman system

2. Cooperative selling through the existing middleman system with supplementary services provided by the associations

3. Cooperative selling through facilities that are integrated, owned, and controlled by the associations

(A discussion of this classification follows the description of the sales policies and procedures of various commodity sales associations.)

**Cheese.** Wisconsin cheese is ordinarily sold directly by the factories and delivered to local buyers on quotations established by the two cheese boards at Plymouth, Wis. The quotations of these boards are accepted as the going market price in all parts of the United States.

The Cheddar cheese producers of Tillamook County, Oregon, have for some years attracted the attention of dairymen in other states, particularly that of the Wisconsin cheese producers, because of their achievements in production and merchandising of cheese. Previous to the year 1919, the dairymen of Tillamook relied upon competitive cheese buyers and ordinary market outlets. During this period of time, Tillamook cheese did not gain prominence in the markets nor was there anything to distinguish it from other ordinary Cheddar cheese shipped into the markets. Consequently, the prices which were paid at the factories in Tillamook were no higher than those received by factories in other cheese producing areas. In Fig. 10 a comparison of prices for all styles of Tillamook cheese, as well as the Wisconsin Cheese Exchange quotations for Twins, is shown for the years 1910-1936. After the organization of the Tillamook County Creamery Association and the selection of capable management for this organization, there was an immediate improvement in sales prices. This association has had noticeably high receipts throughout the years from 1919 to 1936. From 1921 through 1935, the Tillamook association has consistently maintained an advantage of approximately four cents per pound over prices quoted on the Wisconsin Cheese Exchange. The differences between the weighted average annual prices of Tillamook and those of the Wisconsin Cheese Exchange range from 1.89 to 5.93 cents per pound. A partial explanation of Tillamook's success in merchandising cheese may be attributed to the fact that the Tillamook farmers have developed a merchandising program. Moreover, they have made considerable progress in



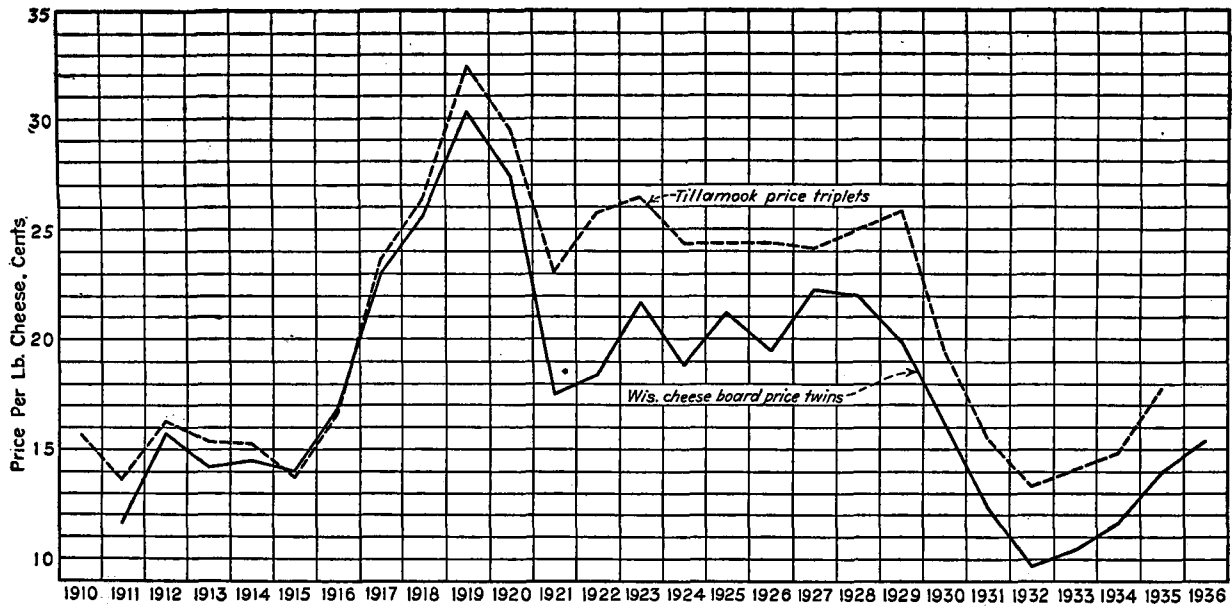


Fig. 10.—Tillamook and Wisconsin cheese prices compared 1910-1936.

improving production methods by reducing the number of factories from 43 to 17, by hiring more efficient cheese makers, by initiating a factory and farm field service, and by encouraging better plant management.

The quality of the commodity makes it possible to advertise the association's brand in the principal Pacific Coast markets and to urge customers to *look for and insist upon getting* the famous cheese identifiable by the mark, "Tillamook on the Rind." Tillamook farmers have profited greatly by their enterprising methods and have received \$4,550,000 in excess of Wisconsin Cheese Exchange quotations for the 109 million pounds of cheese produced in the 15 years from 1921 through 1935. This total difference in returns divided by the number of dairymen in Tillamook County, would amount to a considerable sum for each producer.

Freight costs from Tillamook, Ore., to Pacific Coast markets are no greater, on the average, than freight costs on Wisconsin cheese to its principal markets in the eastern and southern states. Assuming, however, that the Pacific Coast has special advantages as a market because of its location and that the average differential cost is 2 cents per pound for transportation by freight, Tillamook producers still realized \$2,360,000 more than other dairymen for the 109 million pounds cheese produced.

The Tillamook Association sells cheese to all jobbers who have a favorable credit rating and no exclusive sales contracts are given. The difference in price which Tillamook has been able to maintain as compared with that of Wisconsin might be because of the fact that since Tillamook became an aggressive factor in the market, it scarcely pays the Eastern bulk cheese firms to maintain a sales organization in any one of the Pacific Coast cities.

**Tobacco.** The Maryland Tobacco Growers Association sells approximately 50 per cent of the tobacco grown in that state. The growers pack the tobacco in hogsheads and ship it to Baltimore, where samples are taken by a government grader and sealed bids are submitted to the association by buyers representing foreign and domestic manufacturers. The association reviews all bids submitted at the end of the day and announces to the highest bidder the sales, subject to the growers' approval and acceptance. The growers are provided with information that can influence their acceptance or rejection of bids on specific

consignments of tobacco. This is one of the few cooperative marketing associations in the United States that does not assemble, grade, pack, sort, or pool its members' products. It is exclusively a sales organization whose function it is to effect a price agreement between buyers and sellers.

**Wool.** Since 1920 the wool growers in 20 different states have formed 26 associations for assembling, grading, and storing their product. The sales are centralized in one agency, the National Wool Marketing Corporation, which maintains a sales office and a sample floor at Boston. (For a more complete description of the national organization see page 232 of Chap. IX.) The National Corporation makes direct contact with the mill buyers, a large percentage of whom represent woolen and worsted manufacturers and top makers whose factories are located in the Eastern States. This method of selling wool eliminates the competition between growers' local associations and has the advantage of concentrating a large volume of supplies representing all grades of the product which makes it possible to fill orders of all types.

The association attempts to sell the wool on hand throughout the year as it is demanded, but sales are less active in periods when the management considers market prices unsatisfactory. The capital reserves of the corporation are adequate to permit liberal advances to growers and to prevent distress selling.

The corporation is in a position to market wool throughout the normal marketing period. It attempts to avoid disposing of the wool at prices which are not in accordance with general economic conditions and the world demand for wool. However, there is no single factor in the marketing of raw wool which is sufficiently strong to establish the value over a period of time. Definite services are rendered to wool producers in the United States, whether they consign their wool to the corporation or not. The corporation controls the sales through its Boston office which has the largest single concentration of wool in this country. This control supported by a strong financial structure has a tendency to eliminate many of the peaks and depressions which would otherwise occur in day to day market transactions. The activities of the marketing corporation throughout the wool-growing sections of the country have helped to bring about

a greater uniformity in the prices paid to growers in the West and the current market values in Boston.

**Potatoes.** The Colorado potato growers in 1923 formed a sales organization composed of twenty-two local associations located in five different districts of the state. They established the policy of making all sales f.o.b. shipping point. This applies in all cases except when it is necessary to clear the warehouses and tracks of supplies delivered by growers who are unwilling to follow the suggestions of the exchange or local managers in withholding supplies. Cars coming to the market are routed by a traffic manager through points where the greatest number of buyers may inspect them on stopover order. Only a few cars reach the central markets before being sold. When the market is dull, shipments may be directed to markets unsold. The association then informs its representative commission firm on that market of the consignment. When sales are made, a full remittance must be sent to the central office of the association at Denver. Once a month the central office remits to its representatives at the various markets the commissions earned. The usual commission charge ranges from \$12 to \$18 per carload. The Colorado Potato Growers' Exchange has perfected an accurate and detailed card index system giving a full description of each carload, *i.e.*, the grade, size, range, variety, brand, kind of pack, point of origin, date of shipment, number of car, number and points of diversions and stopovers, date of sales, price, name of buyer, freight and commission charges, and other necessary information required to make intelligent sales and to ascertain the best methods of packing, shipping, routing, and selling potatoes. This association is one of the few organized in the United States that has for any length of time successfully marketed potatoes.

**Livestock.** In 1934 there were 44 large-scale livestock sales associations, practically all of which sold livestock on a commission basis for the consignors. Sales in nearly all cases are made by the commission firm in the market where the firm is located, *i.e.*, at East St. Louis, Kansas City, Chicago, Fort Worth, or some other leading public market. In only exceptional cases is livestock reconsigned to a second market where prices may actually net the shipper more than in the market of the commission firm first receiving the shipment. Each firm is naturally interested

in securing for itself the commission for selling the livestock, although, theoretically, it should be interested primarily in obtaining for the farmers the highest net returns. It is evident that the cooperative livestock commission firms can do very little about marketing livestock in an orderly manner, since they do not have the control of the livestock in the feed lots. Each farmer sells when he wishes and sales must be made whenever the consignments are received, since there can be no storing of live animals for advantageous market bulges, as can be done with many pooled farm products. The timing of shipments to markets can be influenced only through market information.

With the development of interior packers, concentration yards, and direct buying by packers located at public markets, the need for cooperative selling agencies to direct livestock shipments (chiefly hogs) from rural points to any one of a half dozen potential markets has become especially apparent since 1925. To meet this need, a number of regional livestock sales agencies have been organized. Thus, the Illinois Livestock Marketing Association maintains a central sales office at Decatur, Ill. and sells hogs for seven cooperative concentration yards located in different parts of the state. The Pacific States Livestock Marketing Association with offices in San Francisco sells cattle direct to packer buyers or feeders for about 700 ranchmen of the far west.

Selling livestock on an auction basis, particularly at country points, has within recent years become a common practice in many states. The California Farm Bureau Marketing Association, organized on a large scale, has sold hogs on a weekly auction basis at several points in the San Joaquin Valley since 1918. It is interesting to note that one cooperative livestock sales association now sells hogs on a dressing percentage basis to eastern packers. Although the purchase of hogs on a dressing percentage and quality-of-carcass basis is common practice for Danish cooperative bacon plants, it is still on an experimental basis in the United States.

It is difficult to analyze the comparative effectiveness with which commission firms sell livestock. There are so many variable factors that comparisons soon lose all value. However, one study made of a cooperative commission company concluded with this remark,

As a result of the analysis of the proportions of the total daily sales of cattle, calves and hogs, the conclusion seemed justified that the sales organization was competent to meet the demands occasioned by large volumes of business.<sup>4</sup>

Of . . . 35,833 hogs, sale prices for 96.1 per cent fell within the range of daily prices for medium-weight hogs of varying grades reported at the National Stockyards market by the market news service of the Bureau of Agricultural Economics of the United States Department of Agriculture. Two and six-tenths per cent of the number were above the upper limit of the price range and 1.3 per cent were below the lower limit of the price range.<sup>5</sup>

**Grain.** Regular shipments of grain to market have been disturbed in recent years by short grain crops. The result has been erratic price relationships between cash and futures markets making it necessary for a sales association to adopt a policy flexible enough to make the necessary adjustment. The Farmers National Grain Corporation endeavors to grasp opportunities in the market that may prove advantageous to its members. Therefore, it maintains agents at the export markets to consummate sales when the price or the exchange rate is favorable.

The cooperative sells a large percentage of its receipts direct to milling concerns. The volume it handles makes it necessary for the association to provide terminal and subterminal storage for approximately 33 millions of bushels.

Most local cooperative groups are not under contract to sell through the national corporation. The sales facilities and services of the national corporation, however, provide it with a very large volume of trade. The locals are kept informed of market conditions by branch offices of the Farmers National, and, since they are autonomous, they sell whenever they feel it is to their advantage. Some local associations buy grain for the corporation at the corporation bid. The bid price is based on the market price at the time of the transaction. The grain when purchased becomes the property of Farmers National. The handling margin of the local depends on the price it pays the farmers or elevators under the corporation's bid price.

<sup>4</sup> GARDNER, KELSEY B., *A Business Analysis of the Producers Live Stock Commission Association of National Stock Yards, Illinois, U. S. Dept. Agr. Circ. 86*, p. 28, November, 1929.

<sup>5</sup> *Ibid.*, p. 25.

**Cranberries.** Not many cooperative sales associations have succeeded in coordinating marketing services to the nice degree of perfection that has been attained by the American Cranberry Exchange of New York City. This organization controls sales for approximately 65 per cent of the cranberry crop grown in Massachusetts, New Jersey, and Wisconsin. Prior to the holiday season, it makes careful inquiry into the extent of production, consumer purchasing power, quality of berries, and volume in the hands of independent sellers. Likewise it inquires into the size of the turkey crop, in order to better estimate an acceptable opening price to the trade. In years when there were large crops, the organized cranberry growers have been unusually successful in extending the normal marketing period for this fruit at sustained prices through judicious advertising. The exchange has maintained favorable relations with the trade, and it has an enviable reputation in standardizing grades and packs. It has also made possible the effective timing of the shipments of the numerous varieties. Late Howes are not permitted to compete with the Early Blacks within the same markets and at the same stores.

**Eggs.** In 1923 four western coast cooperative poultry associations formed a central organization called the Pacific Egg Producers Cooperative, Inc., to consolidate and direct sales activities east of the Rocky Mountains and in foreign countries.<sup>6</sup> It sells to wholesalers, jobbers, independent retailers, and chain-store companies. When the organization was first formed a large percentage of sales was made through an egg auction maintained by the Pacific producers in New York. After their trade brands had become known, sales were made directly to buyers who bought on a large scale. About 50 per cent of the shipments are purchased by chain-store organizations. Very few f.o.b. sales are made; the organization assumes the risks of selling on a

<sup>6</sup> The four cooperatives that formed the Pacific Egg Producers Cooperative, Inc., were:

1. Poultry Producers of Central California
2. Washington Egg and Poultry Association
3. Poultry Producers of San Diego
4. Poultry Producers of Southern California

More recently the Pacific Cooperative Poultry Producers at Portland, Ore. has joined the Pacific Egg Producers Cooperative, Inc., and markets its eastern shipments through this organization.

delivered price, basing them on the market price of the day of arrival. From November to February some sales are made at auction on sample with delivery at a railroad pier.

The heavy seasonal production of the spring months makes it necessary for the Pacific Egg Producers to put eggs in storage and make sales on an allotment basis to the trade. When eggs are put in storage, prices are forecast on the basis of probable production, consumption, comparative food prices, and general economic conditions for a period from six to eight months. From March through June customers must apply in advance for their requirements and specify when they desire shipment. After all applications have been received, the company estimates anticipated supplies, and, approximately five to ten days before the week of shipment, the prices are announced. If prices are not satisfactory, the customer has a few days in which to cancel his order. Spring prices are quoted f.o.b. shipping point, and drafts are drawn in full.

The Pacific Egg Producers Cooperative, Inc., tries to anticipate the market in such a way as to avoid noticeable fluctuations in price. Gradual price changes tend to narrow the margins between wholesale and retail prices. Available supplies are apportioned to the important eastern markets in accordance with their immediate requirements and anticipated demands. The association's control over the supply and its influence on demand tends to stabilize daily fluctuations in prices and facilitate orderly distribution.

**Walnuts.** The California Walnut Growers Association sells as directly as possible through the established middlemen in the market. Approximately 1 per cent of gross sales is allowed in trade discounts,  $1\frac{1}{2}$  per cent for brokerage,  $2\frac{1}{2}$  per cent for advertising, and  $1\frac{1}{2}$  per cent for a series of items such as salaries, rent, taxes, interest, insurance, and office expenses. The association handles 87 per cent of the California crop. The walnuts it packs are of three grades with two or three sizes for each grade. Its brand names are Diamond, Emerald, and Suntand. The organization specifies an opening price at the beginning of the season, but it may change the quoted price from time to time in attempting to move the crop into the hands of the consumer during the normal market period, and thus avoid an accumulation of supplies from successive crops. The association commands



the respect and the confidence of the trade, because it has followed the policy of guaranteeing the trade against a decline in price to date of arrival. The market is so well stabilized, in fact, that the association has voluntarily extended protection to the trade by crediting jobbers with differences in inventory values on floor stocks owing to changes in prices initiated by the association. The success of walnut growers in managing their business, regulating the flow of supply into the markets, and protecting the trade against losses from fluctuations in price is the result of a sound sales program. The gains of the growers in this industry have been wider market distribution, lower costs, and higher prices.

**Citrus Fruits.** Californians have been cooperatively selling their citrus crops for nearly 50 years. The California Fruit Growers' Exchange is one of the largest sales cooperative organizations in the country. It markets annually about 75,000 carloads with a f.o.b. packing-house value which sometimes exceeds 100 million dollars depending on price levels. It sells approximately 70 per cent of the total orange and grapefruit crops of California and Arizona and about 90 per cent of the lemons. The management of this organization has adhered to the policy of distributing through all existing middlemen agencies and of cooperating with the trade in merchandising citrus fruits.

The exchange maintains its own salaried sales organization. It has fifty-seven district offices in the principal markets of the United States and Canada, as well as representatives in Europe and the Orient. About 45 per cent of the sales are made in eleven major market centers where citrus fruits, like other fruits and vegetables, are sold at auction. The remaining forty-six sales districts, extending from Halifax to Honolulu and Edmonton to Atlanta, are termed "private sales" markets. Through them, carloads of fruit are sold to over 4,500 wholesalers in 800 cities and towns.

**Butter.** The Minnesota and Wisconsin cooperative creameries formed an organization in 1921 to consolidate services and unify local creameries in a program of assembling, standardizing, grading, and shipping their products. The first experiments in checking the internal economies of creameries and in collective handling of the products were so outstandingly successful that the dairymen urged that their organization include selling as an additional service to the creameries. Before 1924 it was the

custom for local creameries to sell their output in excess of local requirements to brokers, jobbers, commission merchants, or retail firms in the metropolitan centers of eastern United States. Approximately 13 per cent of the butter was sold to farmers and villagers near points of production. Ten per cent was sold in large nearby consuming centers, and the remaining 77 per cent was shipped to New York, Philadelphia, and other markets on the Atlantic seaboard. In 1924 the Land O' Lakes Creameries, Inc., began making direct contacts with important wholesale jobbers in various cities for the sale of limited quantities of butter. The object was to avoid, if possible, the concentration of large supplies in the central price determining markets. The new sales organization followed the policy of making direct contacts with the trade for three reasons. In the first place, it shipped butter to points of consumption to avoid duplication in physical handling and transportation. In the second place, it minimized the number of transactions and decreased the middleman's margin by directing butter through different channels. In the third place, it reduced the volume of butter flowing through the primary price-making markets by direct shipments.

Two years after the association organized its sales department, it began making contracts for the distribution of Land O' Lakes brand butter through chain-store organizations. In 1928 there were as many as twenty-five chain-store organizations selling butter in more than 20,000 retail stores throughout the eastern and central states.

The Twin Cities, Minneapolis and St. Paul, became the experimental situs in the retail jobbing of butter under the supervision of the new sales department. This market, in the heart of the cooperative creamery region, was largely supplied by private centralized creameries. It was an ideal market for ascertaining the possibilities of expanding sales for quality products, as well as to acquaint the management with the problems of merchandising their products. Ten salesmen with trucks covered the territory tributary to the headquarters office. They solicited orders, made deliveries, and reported difficulties in establishing trade connections and in meeting the requirements and preferences of consumers. In the first two years after an initial introductory period of 10 months, the volume of sales was doubled, and by 1932, 5 years later, it was quadrupled.

Formation of large private corporations gave middlemen more complete control of dairy products from the farm to the consumers. The vertical integration of production and marketing facilities required other agencies in the field to make radical changes in their operating methods. To meet this competition, the Land O' Lakes Creameries, Inc., deemed it advisable to establish its own jobbing service. The association found by experience that it could maintain branch offices in many of the important city markets east of the Mississippi valley. These offices job butter and allied products such as cheese, eggs, dressed poultry, powdered milk, cream, milk fat, casein, maple syrup, and evaporated milk to all classes of buyers in twenty-six cities, including suburban markets within their trade zone. Butter is still being sold in large quantities to chain stores, but the association is no longer solely dependent on these outlets for sales.

Recently the Land O' Lakes Creameries, Inc., a cooperative association, has entered into a business agreement with one of the big meat-packing corporations of the country for the distribution of its products throughout the midwestern and plains states where the packer offers jobbing services to retailers. The reason for this move, it is explained, is to cover the territory effectively where the number of retail outlets is too sparse and scattered to justify branch jobbing offices. The Land O'Lakes association consigns butter to the packer at prices determined by the seller. The packer fixes the handling margin with the approval of the association. In this way sales to the packing corporations are made on practically the same basis as sales to any other account. At any time an open account ceases to be valuable, the sales manager may discontinue sales through an agency and close the account. No exception will presumably be made for the packer's account. Butter, cheese, and other products are to bear the association's trade brand name. If at any time the packer's jobbing services are not performed satisfactorily, the association is at liberty to withhold supplies from the packer for distribution in that area. It is also at liberty to provide its own means of performing marketing services without interference from the packer. It is too early to predict the outcome of this type of sales program designed for the distribution of cooperatively manufactured and branded dairy products.

## SUMMARY OF SALES POLICIES

The above reports describing the general procedure of selling products by cooperative associations are indicative of the many variations that exist in sales policies. The three classes listed under Sales Policies of Large-scale Associations merit further explanation.

1. A large number of cooperatives sell through the middleman system in terminal markets and points removed from the specialized area of production. Some adopt this method as a temporary means of obtaining sales services during the time the association is formulating its own program and attaining maturity through isolated sales experiences and market observations. Others sell through the regular channels of trade because the management believes that the existing system is as efficient and effective as any substitute agency might prove to be. When exclusive agents are appointed or a large proportion of the business is directed through a particular firm, some attempt is made at selectivity on the basis of credit rating, reputation for fair dealing, and skill of the personnel in meeting buyers and making sales. Few of the cooperative associations, however, have worked out reliable and systematic plans for determining the integrity and skill of these agents. For example, there are over 700 wholesale distributors of fruits and vegetables in New York City. Of these, the majority specialize in handling one commodity or several closely allied commodities. But New York is only one market, and the mortality rate in this class of business is relatively high. It is almost an impossible task for a cooperative association to keep pace with the changes in the personnel staff and the fortunes of the different firms bidding for patronage on markets where its products are sold.

It has been observed in sales obtained through private middlemen that the middleman's influence on the system of distribution is usually not very great, except in situations where collusion exists. Most of their energies are devoted to self-preservation, which depends upon their securing a sufficient volume of business. Fees and commission charges are based on the volume of sales rather than on the quality of services rendered. Their charges remain remarkably uniform irrespective of the price received for the commodity and returns made to the shippers. There

has never been a strong bond of identical interests between the agricultural producers and the principals in the middleman system. As a result middlemen encourage shipments into a market as long as the sales price covers freight costs, commissions on the sales price,<sup>7</sup> inspection fees, and other incidental charges. The old type competitive middlemen who are dependent upon commissions from irregular consignments are of necessity self-centered and show only slight concern for the welfare of the growers or the interests of the consumer.

When quotations are made f.o.b., all buyers are placed on an equal competitive basis. Theoretically, they assume the risks of buying on accurate description and quality, cost of transport, damage in transit, and other incidental costs in transferring the product from the producing area to consuming centers. Practically, however, the buyers are reluctant to assume these risks, and the history of f.o.b. sales is replete with rejections, reinspections, claims, adjustments, and allowances. The associations which do not develop proper facilities for following their shipments through to the market have been exploited repeatedly by unscrupulous and unprincipled buyers. From such experiences, the conclusion which they logically drew was that if they must assume the risks of transfer, even though the products are sold on an f.o.b. basis, they might as well completely integrate their organization in order to reap the gains, as well as assume the losses, in marketing which result from quoting prices on the delivered basis.

2. Many cooperative sales associations supplement the existing middleman system. They direct and time shipments into consuming areas recognizing the limitations of the established middlemen to evolve a comprehensive system of distribution. The cooperatives usually retain the title to the product. Consequently, they are permitted to direct shipments and control sales up to the last stages of distribution. The fact that the association approves or rejects all sales gives it a larger measure of control over prices. It also permits discretion in choosing both the buyers and the retail markets. This system discourages speculation, blind consignments, market gluts, price demoralization, and hidden commissions or profits. These pre-

<sup>7</sup> Commissions based on sales prices at points of destination include a percentage on the freight costs.

cautions are essential to jobbers and retailers if large losses are to be avoided. The same safeguards are used by the producers in markets where keen competition exists. In addition, cooperative organizations supplement the system by creating branch sales offices in all of the important consuming areas. The primary function of the branch office is to relay to the central exchange information concerning the condition of the market receipts, quality of produce from competing sellers, consumer purchasing power, prospective customers, and many other valuable sales leads that will aid the association in determining the date and place of shipments. In addition to these duties, the branch office is in charge of sales promotion work. Representatives call on the trade, interview customers, assist retailers in setting up attractive displays, distribute advertising matter, and advance the interests of the association wherever and whenever they can.

3. A number of cooperative sales associations have settled on a policy of integrating sales through their own wholesaling and jobbing services which make direct contact with retail outlets. In this way the cooperative sales company exercises more complete control over the distribution of its products. It may sell to whom it wishes, render the necessary services to attract trade, and name a delivered price, all of which secures for it any premium which it can command for a superior product or a desired service.

The orthodox point of view is that competition in agriculture is pure to the extent that there is a total absence of monopoly influences. Those who hold this opinion may be correct if they refer only to farm production, but even then they must exclude the breeders of pure bred stock and the growers of pedigreed seeds. It may apply to the market if (a) the number of buyers and sellers are large, and (b) the product is standardized. The former condition is more easily met than the latter since most agricultural products are not similar.

Price theories have followed, in the main, the two extreme channels, without (conscious) recognition of a middle course. Quantitatively, competitive theory has dominated—indeed, the theory of competition has been so generally accepted as the underlying explanation of the price system that the presumption is in its favor; its inadequacy remains to be proved. Hints at the ubiquity of monopoly elements and at the

possibility of an intermediate theory are not entirely lacking, however. Thus Prof. Knight remarks that "in view of the fact that practically every business is a partial monopoly, it is remarkable that the theoretical treatment of economics has related so exclusively to complete monopoly and perfect competition," and Veblen "it is very doubtful if there are any successful business ventures within the range of modern industries from which the monopoly element is wholly absent." Such fragmentary recognition of the problem is not hard to find. Yet, with the exception of the theory of duopoly, the middle ground between competition and monopoly remains virtually unexplored and the possibilities of applying such a theory relatively little appreciated.<sup>3</sup>

The formation of agricultural sales associations tends to greatly reduce the number of competing sellers. Distinction is given to the product handled in an effort to create a special demand for it. Distribution is directed and timed to give the association the greatest advantages of market opportunities. Direct shipments to consuming centers diffuse the supply. Because of the increase in the number of competing buyers, the sales associations rather than the specialized middleman are given greater opportunities to influence the price. In the process of integrating sales services the producer's control of the supply and influence on prices are extended marketward. Quotations tend to be made at the point of destination rather than at the point of origin, where all buyers would theoretically compete on equal terms.

Cooperative sales associations provide a means by which agricultural producers may enjoy a partial monopoly in the distribution of a given market supply but their control of the volume of production and the quality of the products is not so great as that of manufacturers who have a monopoly of a given product. For a limited period of time, the farmer's status is somewhat similar to that of business corporations and industrial groups in that he can determine the date of shipment of his supplies and, to a less extent, the price he will receive. It is doubtful that this condition will exist when consumers are organized into powerful bargaining groups which deal with similarly organized producers' groups. The producers through their organization attempt to obtain the largest possible price

<sup>3</sup> CHAMBERLIN, EDWARD, "The Theory of Monopolistic Competition," pp. 4-5, Harvard University Press, Cambridge, 1933.

consumers can be induced to pay and at the same time dispose of all of their produce. This is necessary in order to compete with private corporations. The latter may always resort to reserves to attack cooperatively organized areas in an effort to discourage the movement and discredit the existing poorly organized associations.

#### Questions

1. Define a perfect market. What are some of the limitations of the Marshallian concept of a perfect market?
2. Outline the procedure that local associations usually follow in determining their sales policies.
3. Do local sales associations have a wide range of choice in market outlets?
4. What is meant by the term "bargaining leverage"?
5. Comment on the statement, "that no individual or group in society has any rights which supersede those of the producers in naming the price of agricultural products."
6. Classify the various markets to which agricultural products ordinarily flow.
7. Did the Tillamook farmers gain any benefits by initiating an aggressive sales program? Have the cheese producers in Wisconsin followed a similar sales program? Explain.
8. Give a brief chronological résumé of the sales policies adopted by the Land O'Lakes Creameries, Inc.
9. Have the cooperative sales associations which sell through existing middlemen agencies any degree of control over marketing services?
10. Do cooperative associations attain any monopolistic powers through coordinated sales programs?

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## XIX

### *Industry Plans for the Control of Production and Distribution of Agricultural Products*

*The generations of the past century found great natural resources in the virgin forests, rich mines, and fertile lands of this country, and the abundance was so great that they appropriated it without compunction. Food, clothing, and shelter became relatively inexpensive during this period of agricultural development, and the tillers of the land owing to their disorganization could not retain much of their conjunctural gains. All society benefited, and especially those who engaged in trade.*

*Consumers became so accustomed to abundance in production that they began to assume that producers were socially obligated to put on the market the entire supply whether or not the prime costs of production and distribution were returned to agriculture. Likewise agricultural producers have not been considerate of the welfare of consumers when they occasionally found themselves in a superior bargaining position. Whatever the virtues may be of such an economic order, it has been difficult to keep the system balanced and in nice adjustment. There have been both starvation among industrial workers and impoverishment of the agrarian class in this land of plenty. The chaos and disaster in agriculture following the World War produced new price-raising schemes. The recent trend has been toward economic isolation. A lower plane of living is inevitable if the policy of economic nationalism is continued even though men have the capacity and the will to possess abundant material wealth.*



## CHAPTER XIX

### INDUSTRY PLANS FOR THE CONTROL OF PRODUCTION AND DISTRIBUTION OF AGRICULTURAL PRODUCTS

The cataclysm of disorder that swept over all economic enterprises during the dismal years of the World War has left an indelible imprint upon the agricultural industry of the world. The fields abandoned by able-bodied peasants and the hills and meadows consecrated to battle numbered more than 40 million acres. With these millions of tillable acres fallowing in Europe, the increased demands for foodstuffs and for tribute to the insatiable Mars abnormally stimulated agricultural production in other parts of the world, particularly in the United States.

During the decade 1910-1920, 31 million acres in the United States were reclaimed for cultivation, an appreciable percentage of which was in the arid plains states ordinarily devoted to grazing. Breaking the sod in this arid region was one of the great blunders of the decade, if considered from the standpoint of the conservation of natural resources. Canada, Argentina, and Australia added 26 million acres to their cultivated lands to swell the total of newly plowed acres to 57 million, an increase which was offset by a decrease of 40 million acres in Europe.

The reconstruction period following the war brought 37 million acres of arable land in Europe back into cultivation, and since there was no corresponding retrenchment in agricultural production in other parts of the world, the battle for markets was intensified. Production surpassed consumption requirements at profitable prices in many countries. The intense nationalism induced by the war and the reparation terms stipulated in the treaties of Versailles, Neuilly, Saint-Germain-en-Laye, Sèvres, Trianon, and Lausanne resulted in the throwing up of tariff walls and other trade barriers on every side. Thus international trade was dangerously impeded and the surpluses impounded in the nations where they were produced.

In North America, the highly specialized agricultural producers, such as the cotton and tobacco farmers of the South and the wheat producers in the prairie states and provinces of the West, suffered seriously from these dislocations in trade. In Europe the consumers taxed themselves to subsidize the growing of grains in their own countries, while in America the surpluses became so burdensome that the farmers burned corn and wheat as fuel. In Germany, France, and Italy the price of wheat during the late spring of 1931 was maintained at \$1.60 to \$1.85 per bushel when Canadian wheat was selling at Winnipeg for 50 to 55 cents per bushel.

To meet these worldwide crises, production and marketing control schemes have been initiated, economic plans projected, and international agreements concluded to direct and regulate production and distribution in the various industries as: cotton, cheese, and cinchona; peanuts, pigs, and pineapples; rubber, rice, and rye; sugar, silk, and seals; tin, tea, and tobacco; walnuts, wheat, and whales. For the industries that require colonial coordination or international cooperation for their protection and preservation, there is the prospect of improving the relationships between foreign powers and developing institutions that may exert an influence toward promoting trade. The problem of controlling production on a regional or national basis for domestic consumption presents many of the same perplexing administrative problems as are encountered in the international regulation of commerce.

#### COMMODITY CONTROL SCHEMES IN THE UNITED STATES

Evidence of unrest in American agriculture became apparent shortly after the end of the World War. The activities of the Federal Food Administration in regulating prices and controlling consumption of staple commodities during the war period caused producers to conclude that if the federal government could limit prices from rising unreasonably, it could also be called upon to prevent prices from falling below the cost of production. And since the postwar depression the spokesmen for agriculture have exerted even greater pressure upon the government to avert an impending disaster. The relative advantage which industrialism held over agriculture is reflected in the low level to which agriculture descended in the prolonged

depression from 1921-1936. The cash returns to agriculture decreased 66 per cent from 1929 to 1933, owing to decreased consumer buying power in the cities as represented by the 63 per cent decrease in factory pay rolls and to the fact that the stock of food and other raw materials in the world had increased about 62 per cent. The agricultural population, which constitutes one-fourth of the total population of the United States, received less than seven per cent of the total national income.

Of the many proposed laws prompted by the breakdown of agriculture some were passed that were of special significance. In 1921 the War Finance Corporation was authorized to make its funds available to agriculture for financing the exportation of farm products. In the same year the Emergency Tariff Act, the Packers and Stockyards Act, and the Grain Futures Act went into effect. In 1922 congress passed the Capper-Volstead Act providing a more secure legal basis for the organization of farm cooperatives engaged in interstate commerce. The Tariff Act of 1922 also provided for higher tariff walls on many farm commodities. The need for greater facility in financing farm cooperatives was recognized in the Agricultural Credits Act of 1923. Funds were made available for market research work by passage of the Purnell Act in 1925, and in the following year congress created the Division of Cooperative Marketing. Before the passage of the Agricultural Marketing Act in 1929 which created the Federal Farm Board and provided it with a 500 million dollar revolving fund, there were several bills designed to benefit the agricultural industry.<sup>1</sup> Two of the most notable among these were the McNary-Haugen bill which provided for an equalization fee, and the McKinley-Adkins bill which proposed paying, in the form of debentures, a bounty on exports.

During this time, the domestic allotment plan for controlling agricultural production was widely discussed. Its basic features

<sup>1</sup> In 1935 when the status of the Federal Farm Board revolving fund, including its earnings, could be fairly accurately determined, the fund was divided as follows: approximate losses 143 million dollars, gifts 198 million dollars, salvaged for reinvestment by the Federal Farm Credit Agencies 177 million dollars; total 518 million dollars. Third Annual Report of The Farm Credit Administration 1935, p. 169, U. S. Government Printing Office, Washington, D. C., 1936.

were incorporated in the Agricultural Adjustment Act of 1933. The deliberations of congress, however, were generally confined to a consideration of exportable surpluses. The thousands of farmers engaged in the production of specialty crops distributed in domestic markets received a sympathetic ear but not a helping hand. They were encouraged to seek their own salvation through voluntary efforts.

#### CLEARINGHOUSE SCHEMES

Agricultural income was as seriously affected in many specialty crop production regions as in some of the principal crop production areas. The agricultural situation was so extraordinary that all income receiving groups in the community felt that they must take a hand in planning alleviation for the farmer. The experiments of such groups during the postwar decade is of more interest for the study of cooperative enterprises than the grand schemes of governmental control, because they were self-initiated and managed by the producers and the cooperative and private shippers.

The harvesting, assembling, packing, and shipping of crops in which surpluses were a disastrous certainty called for immediate action. There was no time for producers who were favorably disposed to cooperative organization to form enterprises which would be sufficiently influential to forestall a ruinous marketing season. Moreover, the problem confronting the community was so general in nature that united action was necessary on the part of all concerned with gaining a livelihood in that section. Many of the distressed areas already had local cooperative sales associations, which formed a part of the competitive marketing system of the community. In such times of distress it was declared good public policy to eliminate all undesirable types of competition. Therefore, it was proposed that all growers and shippers coordinate activities to avoid spoiling the market for their products.

All handlers were prevailed upon to unite in forming clearinghouse associations which were designed to temper localized competition and eliminate undesirable market practices. The clearinghouse organization provided a type of horizontal integration in which each grower, shipper, buyer, and cooperative association operated independently in handling products and

competing for patronage, but mutually exchanged information about market conditions and transactions in accordance with the prescribed rules of the association. A composite picture of this type of planned production and market control can be best seen through its objectives, which aimed to:

- Advance the mutual interest of growers and shippers
- Regulate the flow of products to the market
- Collect and disseminate information of production and distribution
- Correct trade evils and abuses
- Secure uniformity in sales contracts
- Adopt a uniform accounting system
- Eliminate local competition in purchasing and assembling products
- Provide for uniform commission charges
- Adjust grievances and differences by fair and equitable means
- Prorate shipments among producers
- Limit supplies in all markets
- Name minimum prices
- Record all transactions and conditions affecting cash sale
- Report all rejections, allowances, and adjustments on shipments
- Stimulate demand and confidence on the part of the purchasers

The divergent groups which had traditionally pursued an independent course of action in directing their enterprises and in competing against rivals of old standing were reconciliated temporarily to withstand emergencies when external forces appeared more formidable than those which their own machinations could contrive in the struggle for survival. The outcome of several ventures of this type is reviewed briefly in the following paragraphs.

Private business operating for profit encounters difficulties when it competes with cooperatives which operate at cost. This fact became apparent to producers when all information relating to transactions was collected through a central agency. Usually, the cooperatives gain patronage under this plan of operation if the efficiency of the management compares favorably with that of private business. The independent dealers and shippers considered a withdrawal from such an arrangement a measure of self-preservation even though benefits might have been obtained

through united action and the objectives listed above might have been achieved. Clearinghouses failed because the various groups seemed incapable of generating enough cohesive force to hold them intact.

Such a plan requires unanimity of action, and if a small minority refuses to cooperate, their withdrawal effectively destroys all further possibilities of cooperating. There is little chance for furthering social interests successfully without a centralized authority which directs and enforces agreements that are entered into for the execution of the plan.<sup>2</sup>

#### CONTROL PROJECTS WITHIN AN ORGANIZED INDUSTRY

Market research was furthered by another group of producers who were experimenting with the plan of controlling sales and sharing markets at the time the clearinghouse associations were being formed. In the efforts of the citrus growers it is possible to isolate the factors essential for success in this type of collective action. The 1924 crop of citrus fruits in both California and Florida was large and the prices of \$2.61 per box of oranges and \$2.59 for lemons f.o.b. California were considered decidedly unsatisfactory in view of the favorable reports on consumers' purchasing power for that year. It became obvious that either production or distribution control would be necessary.

The organized citrus growers in California recognized the practical difficulties involved in surplus control, since they had already been experimenting for several years with previous crop excesses. A committee of lemon growers was selected to study the possibilities of closer coordination in production and distribution on the part of those engaged in the industry. The growing of lemons suitable for commercial purposes is restricted to a

<sup>2</sup> A few of the associations that were formed to accomplish these aims are as follows:

The Gravenstein Apple Growers Clearing House of California

The Florida Citrus Growers Clearing House Association

The California Vineyard Association

The Imperial Valley Lettuce and Cantaloupe Clearing House Association

The Northwest Fresh Prune Clearing House Association

The Del-Mar-Va Eastern Shore Association (potatoes)

None of these organizations has survived. Many of them failed within a few months after their formation.

small area in southern California, and at least 90 per cent of the orchard owners, as members of the California Fruit Growers' Exchange, were accustomed to working together for the common interest of the industry. They readily came to an agreement and presented a plan for regulating the marketing of the lemon crop. It was put into effect in 1925 with the provision that the quantity of lemons to be shipped each week should be limited to a volume which could be sold at prices acceptable to the growers and at a price that would not seem exorbitant to the consumers. The amount any shipper or grower was permitted to ship to market in any given week was fixed by the distribution committee. It met once a week, or more frequently if occasion demanded, and determined the quota each shipper was permitted to forward to market. Twice a month a representative from the cooperative association inspected the fruit and counted the number of boxes held in the storage sheds and packing houses. This information was used in determining quotas which were based on a given percentage of the total quantity of lemons held in storage at the time they were counted.

When this plan was first proposed, many growers doubted its soundness. They believed that there would be numerous difficulties in making equitable allotments because of the great differences existing in the quality of fruit, the time of maturity, the length of time that the fruit can be held in storage, and the capriciousness of the demand for lemons. Many growers were willing to have their freedom in making shipments restricted in all seasons except the one in which they filled spring orders. The growers' final conclusion was, however, that all would profit more by cooperating in a restriction program. Ninety-five per cent of the growers in the exchange signed the necessary contracts to make the lemon agreement effective for the season of 1925-1926. The concerted action on the part of the lemon growers was so satisfactorily administered that nearly everyone in the industry gave support to the agreement which had proven so beneficial to them.

The organized orange growers, who controlled a smaller portion of the total supply than the lemon growers, were not so fortunate in the outcome of their experiments in surplus control. In 1934, the price for Navels averaged \$1.39 and for Valencias \$1.84 per box f.o.b. California, in contrast to the much more



advantageous price of \$3.43 received by the lemon growers. Ten years earlier the orange growers had appointed a committee to work out plans for controlling the shipments of their commodity the same as the lemon growers had done. The objectives of the two committees were the same, but the obstacles encountered in applying the plan for control of orange shipments were greater. Oranges, with the exception of one variety, are grown in different states and over a wider area than lemons. Under these circumstances, it is difficult to effect an agreement for restricting shipments, since differences arise over the allotments to be made each area. The Valencia orange growers were encouraged by the success of the lemon control plan, and the occasion for another attempt at control of shipments for the variety occurred in 1932, the dreariest year of the depression, when it became apparent that California would produce one of the largest crops of Valencias on record. Prices were sure to fall to new lows in view of the decreased consumer purchasing power. The Valencia growers and shippers finally arranged to prorate shipments. The agreement, however, between the principal shipping concerns terminated after 30 days duration even though concerted action had resulted in increasing the price during that period more than 50 cents per box. For opportunistic reasons two shippers destroyed all possibilities of continuing the market-sharing plan. It was estimated that if the plan had continued in operation during the full season that the returns to the Valencia growers would have been increased approximately 4 million dollars. The brief experience of 1932 gave these growers the courage to attempt another agreement in 1933,<sup>3</sup> and shipments were prorated throughout the season.

Some of the difficulties in working out a program on a voluntary basis for the orange and grapefruit crops have been tersely summarized by one of the spokesmen for the industry:

1. Oranges and grapefruit are produced in all the citrus states, which makes a coordinated national plan imperative for all except the Valencia variety.

2. No one marketing organization is in dominant position as is the case with lemons.

<sup>3</sup> Growers' Committee Announces Termination of Proration Agreement, *California Citrograph*, vol. 17, no. 10, p. 382, 1932.

3. Volume prorates are necessarily based on tree-crop estimates, which are neither as specific nor as satisfactory as the lemon prorate based on fruit actually in storage.

4. The seasonal and varietal differences as to maturity and shipping period greatly complicate the prorate application under surplus conditions.<sup>4</sup>

[Oranges may be left on the trees and their supply permitted to accumulate throughout the growing season. This surplus tends to depress the price even though only the best grades and sizes are sent to market. A well-conceived plan of control should eliminate the excess of oranges as the season advances.]

#### MARKET-SHARING PLANS

Another short-lived experiment in restricting the flow of a commodity to market was attempted by the growers of Tokay grapes in the San Joaquin valley in 1932. The grape crop in that year was likewise large, and the growers of Tokay grapes thought that they might minimize their losses by allotting shipments to each grower according to the productive capacity of the vineyards and by determining the percentage of the total prospective production that could be sold in the markets of the country. The proration program was in effect only four weeks, because nonparticipating growers and shippers attempted to capitalize on the market opportunities that were being created by limiting supplies.

The lettuce growers of the Imperial Valley have on different occasions restricted shipments by the simple expedient of conferring on the secretary of their association the exclusive right of placing all orders for shipments with the railroad. The secretary is in possession of records on shipments of former years which makes it possible for him to estimate the number of cars that should be loaded each day during the harvest season. The production of this commodity, like that of lemons, is limited to a small area in which there are relatively few growers, all of whom readily appreciate the problems of the industry and, therefore, manifest a willingness to cooperate with one another. The Imperial Valley cantaloupe shippers also organized an association for prorating the shipments of melons during the

<sup>4</sup> ARMSTRONG, PAUL S., "Cooperative Self-regulation," pp. 22-25. The Marketing Conference, Pomona College, Claremont, Calif. Marketing Conference Executive Committee of Cooperatives, Modesto, Calif., 1934.

season of 1932. It was reported that large losses would have been assumed by the growers of this crop if regulation had not been effected.

Similar schemes of limiting market supply were attempted by the cling-peach growers and the grape growers of California during the seasons of 1930 and 1931. The grape growers were partially successful in 1930, but the 1931 attempt failed, owing to the individualistic bent of the producers and the difficulties of working out an administrative program for an equitable division of the markets since grapes are diverted into so many products. In addition to being used as fresh fruit for the table, they are also used in manufacturing raisins, wines, juices, and several by-products. An assessment was made on the quantity marketed to establish equality with the price of the grapes diverted into by-products. The amount collected in 1931 was not sufficient to remunerate the growers who withheld their supplies, and the plan failed.

The experience of the peach growers in limiting the supply was somewhat more encouraging. A unit assessment was levied on all canners for the purpose of paying the growers who did not harvest their crops. The curtailment programs of 1930 and 1931 were sufficiently satisfactory to cause the growers to take steps to curtail the number of trees, discourage new plantings, and wherever possible to prevent expenditures for pruning, spraying, cultivating, and irrigating orchards on the portion of the crop that would create a surplus in the market season. The 1932 cling-peach program failed because a few of the canners and growers refused to participate. The failure of the growers to fully support this program resulted in a marked decline in the price realized by the growers who harvested their crops.<sup>5</sup>

All proration schemes are temporary in nature in that they are applied to agriculture in years when supply and demand are not balanced because of favorable growing seasons, decreased consumer purchasing power, or a combination of the two. The crops that are most conducive to the development of plans for restricting acreage, controlling shipments, and sharing market opportunities are those that are:

<sup>5</sup> For an excellent discussion of the various proration plans read Stokdyk, E. A. *Economic and Legal Aspects of Compulsory Proration in Agricultural Marketing*, *Univ. Calif. Agr. Exp. Sta. Bul.* 565, 44 pp., 1933.

Grown in restricted areas

Produced under intensive cultivation

Transported long distances to markets

Stored with difficulty owing to their perishability

Possessed of high values in relation to bulk

Packed and distributed by specialized commercial enterprises

Dominated by the agricultural producers

The production of tree and vine crops in the Pacific Coast states most nearly corresponds to these conditions, and it is in this area that the most notable instances of voluntary crop control plans have been conceived and tried.

When the Agricultural Adjustment Act was passed, representatives of the various industries began considering ways and means of enlisting the services of the federal government in supervising the enforcement of their marketing agreements on a firm and impartial basis. The citrus growers seized this opportunity to overcome certain inherent weaknesses in their former agreements. The California-Arizona Citrus Agreement has brought such order into this industry that it is now possible to move a larger quantity of fruit into markets in the fresh form at favorable prices than would otherwise be possible without demoralizing the markets. The shipments of citrus fruits from California were increased in the period of 1930-1935 nearly 35 per cent over the average annual shipments in 1920-1930. The citrus shippers of Florida entered into a marketing agreement in 1936. The regulation of orange and grapefruit shipments now includes about 95 per cent of the total marketings.

#### COMPULSORY MARKET PRORATION

Because 80 to 90 per cent of the growers of several California crops had repeatedly attempted to work out some control program only to be thwarted by a few shippers and growers, a strong drive was made for compulsory cooperation, resulting in the enactment of a series of laws designed to control the production and marketing of agricultural commodities in intrastate commerce. The following laws were put on the statute books of the state of California within the past few years:

California Agricultural Adjustment Act—effective Aug. 4,  
1933

Agricultural Prorate Act—effective Aug. 21, 1933

Amendments to the Agricultural Prorate Act—effective  
Sept. 15, 1935

California Marketing Agreement Act—effective Sept. 15, 1935  
(terminated September, 1937)

California Marketing Act of 1937

All of the above acts except the Agricultural Prorate Act are administered by the State Director of Agriculture. The Prorate Act is under the administration of a commission consisting of 9 members and it provides that growers may control shipments and share markets if two-thirds of the producers choose to invoke the provisions of the law. The state law was patterned after the federal act relating to marketing agreements and was intended to supplement the federal act in the control of intra-state shipments. It is particularly adapted to certain commodities because they are grown and sold almost exclusively within the state. On Mar. 5, 1937, the Agricultural Prorate Commission submitted to the governor of California a report of the activities of producer groups operating under the act.

Two hundred and forty lettuce growers in the Imperial Valley zone, cultivating 30,000 acres, instituted a program, January, 1934, to aid the industry in coping with a serious market situation. The growers terminated the plan by their petition of August, 1935. In Zone 2, comprising Santa Barbara and San Luis Obispo counties, the growers of lettuce invoked the act in April, 1934. There were 105 growers tilling 5,194 acres, and the plan has been in effect every year since its inception.

The Gravenstein apple growers of Napa and Sonoma counties, whose orchards cover about 10,000 acres, chose to apply the prorate plan in 1934. The plan was not put into effect that year owing to the insect infestation in the orchards which reduced the crop to 40 per cent of its normal size. In 1935 an unfavorable lower court decision stopped control plans, but in 1936 the prorate act was finally put into effect for Gravenstein apples.

The Concord grape growers of Santa Barbara, Ventura, Los Angeles, and Orange counties are few in comparison, numbering not more than 66 in all. Their acreage is correspondingly small, including 235 producing acres. Even with this small acreage the growers produced about twice as much as the limited

markets could be made to absorb, and in 1934 and 1936, they too applied the prorate plan.

The artichoke growers had been ready for three years to invoke the act, but the supply and demand for this product have been favorable.

Tomato growers of Zone 1, including eight counties, with more than 13,000 acres, petitioned for a program of control in the Southern California market in 1934 and again in 1936. The tomato growers in Zone 2, which includes 14 California counties, exercised the right to prorate shipments for the 1936 crop.

TABLE XX.—ADMINISTRATION OF AGRICULTURAL PRORATE PLANS IN CALIFORNIA 1934-1937

Program	Year	Cost*	Estimated gain to producers
Lettuce No. 1.....	1934	\$ 8,657.71	\$ 500,000.00
Lettuce No. 2.....	1934	6,719.19	250,000.00
	1935	13,777.82	250,000.00
	1936	14,318.68	400,000.00
Apple No. 1.....	1934	2,652.79	(Not available because of limited control)
	1935	2,025.86	(Stopped by court decision)
	1936	3,714.49	400,000.00
Grape No. 1.....	1934	1,109.84	15,000.00
	1936	500.75	(Not available because of limited control)
Tomato No. 1.....	1934	5,112.52	100,000.00
	1936	24,216.31	250,000.00
Sweet Potato No. 1....	1934	2,464.85	12,500.00
Sweet Potato No. 2....	1934-1935	7,239.80	150,000.00
	1935-1936	4,429.79	50,000.00
	1936-1937	8,205.71	200,000.00
Celery No. 1.....	1934	1,929.90	100,000.00
	1935	1,012.62	50,000.00
	1936	3,961.71	300,000.00
Tomato No. 2.....	1936	18,984.24	200,000.00
Total.....		\$131,034.58	\$3,227,500.00

\* Includes Commission's allowance.

A small group of sweet potato growers in the Los Angeles area were stopped in their program of market control by an unfavor-

able court decision in 1935. However, they applied the plan again in 1936-1937. Another group of sweet potato growers in Zone 2 in California shared markets in 1934. Their program was interrupted in 1935 but resumed again in 1936. A similar program was instituted for the celery growers in the San Joaquin-Sacramento delta and has been of great advantage to these growers ever since its inception.<sup>6</sup>

Injunctions were obtained by minority groups to prevent the act from being put into effect until the case was finally carried to the state supreme court. On Feb. 29, 1936, the court handed down a 17,000 word decision which declared the act constitutional.<sup>7</sup>

The estimated gains to producers in the preceding tabulation are calculated upon the most authentic information available. While some may dispute the accuracy of the estimates, none will deny that the actual gains have far exceeded what it cost to obtain them.<sup>8</sup>

#### CONVERSION OF RAW PRODUCTS AND BY-PRODUCTS UTILIZATION

In many production areas the decision to limit shipments of farm produce in the original form by any organized group, either by voluntary action or compulsion, still leaves the problem of surplus disposal. Surpluses may be avoided by limiting plantings, pulling up trees or vines, plowing under growing crops, permitting inferior grades of the produce to go to waste, developing foreign outlets, or diverting a portion of the crop to the manufacture of by-products.

The growers in the citrus industry are sufficiently well organized to divert surpluses to their own by-products plants or to markets which have little or no influence upon domestic fresh fruit prices. The lemon growers first began the manufacture of

<sup>6</sup> ABEL, EDSON, California Agricultural Prorate Commission. Some Aspects of the Agricultural Prorate Act, *California Cultivator*, vol. 82, no. 5, pp. 123 and 147, Mar. 2, 1935.

<sup>7</sup> *Agricultural Prorate Commission v. Superior Court*, 5 Cal. (2 d) 550. 55 p. (2 d) 495.

<sup>8</sup> McFADDEN, A. J., President of the Agricultural Prorate Commission for California, Report of the Commission to the Governor for the period Sept. 1, 1933-Feb. 28, 1937, State Office Bldg., Sacramento, Calif.

by-products in 1915 by utilizing a portion of the lemon crop that was too inferior in quality to be marketed in the fresh form. They have been singularly successful in discovering other uses for citrus fruits and in developing markets for the numerous by-products manufactured from the surpluses. The result of these discoveries has facilitated the control of fresh-fruit shipments.

Since 1931, a large percentage of the total crops has been diverted into by-products as is shown in the following table.

TABLE XXI.—PERCENTAGE OF THE TOTAL RECEIPTS OF THE CALIFORNIA FRUIT GROWERS' EXCHANGE MANUFACTURED INTO BY-PRODUCTS (1931-1935)

Year	Oranges, per cent of total crop	Lemons, per cent of total crop
1931	6.7	26.4
1932	8.3	27.5
1933	8.7	15.2
1934	7.5	14.7
1935	10.5	33.5

A few of the by-products that are manufactured from oranges and lemons are pectin, orange and lemon oils, citric acid, orange and lemon juices, and orange meal. When the surpluses become too great, the limits of profitable market disposition for various by-products are reached; then the market problem may become more acute in the sale of the by-products than in the sale of fresh fruit. It is possible to manufacture a sufficiently large quantity of certain by-products from the surplus of a single large crop to supply purchasers for the succeeding five years at current rates of consumption.

Although the number of cooperative organizations which have engaged in the manufacture of industrial by-products is not great, nevertheless, much attention has been given to the possibilities of more completely utilizing the commodities handled by them. The poultry and egg associations avoid waste by grading out all checked and cracked eggs. These are broken and separated in packs of egg yolks and egg whites for the convenience of bakers, candymakers, and other commercial



users. The quality of eggs placed in storage may be better preserved by submerging them in a special oil which fills the pores of the egg shell and prevents evaporation without affecting the flavor of the egg. Dirty eggs are made marketable by sandblasting the shell.

Many dairy associations have constructed flexible milk plants which divert milk into several manufactured products, such as various types of cheese, butter, evaporated and condensed milk, milk powders, cream, and casein. Recently, the process of powdering whey has been perfected. This is a most useful discovery, since the handling or disposing of whey in liquid form has always been a problem of the cheese industry.

New products and new uses for old products are constantly being discovered by inventive geniuses in commercial organizations. Mechanical appliances and new machines are being perfected for the efficient conversion of a common commodity into many products. The hulls and linters from cottonseeds, for example, provide the base for thirty different products varying in kind from writing paper to gunpowder, while the meats of the seed can be used in manufacturing about fifty different commercial articles. The Farm Chemurgic Council and the Chemical Foundation, Inc. are performing a noteworthy service in directing chemical research to advance the industrial uses of farm products. The diversion of grain crops into fuel and fiber products promises to become increasingly important. The cooperative marketing associations of the nation will in all probability continue to assume their part in establishing plants and developing markets for the many new and unusual products that may be made available to consumers when the need for them is recognized.

#### **JOINT USE OF SALES AND PURCHASING AGENCIES**

The antagonists of cooperation contend that society will not escape the evils of the competitive system in business by adopting the cooperative technique. They hold that one can find evidence of as much duplication, waste, and perversion in the new methods and ideas adopted by the management of a cooperative as can be found anywhere. Competition is the antithesis of cooperation. Rivalry exists in communities where private corporations and local cooperative associations bitterly struggle

for survival. Apparently, cooperatives have not yet become immune to that contagion of competition induced largely by the methods of private corporations.

The large central sales associations are capable of avoiding conflict in performing services and sharing markets. In fact, they tend to enter into reciprocal business relationships which increase their effectiveness in rendering services within given market regions. For a number of years now the Land O'Lakes Creameries, Inc., Minneapolis; Challenge Cream and Butter Association, Los Angeles; and the Washington Cooperative Dairies, Seattle, have tacitly confined their sales efforts to natural regions of distribution. If sales exceed receipts for one of these associations and it is necessary to ship butter from one region to another, preference in purchases is given to the other cooperative associations. The management of large-scale associations recognize that, in a program of service for agriculture, the points they hold in common merit emphasis. Their differences can be minimized through a mutual understanding of one another's problems. The Wisconsin Cheese Producers' Federation consolidated its sales department with that of the Land O'Lakes Creameries, Inc., in 1934 as a measure of economy and in an attempt to avoid any possible competition between the two great dairy cooperatives which, by reason of their location in the Middle West, distributed similar dairy products to the same markets.

One of the finest examples of cooperation between large organizations is that between the deciduous and citrus fruit growers of California. The same sales organization has been used for more than 30 years by the California Fruit Exchange, an organization of 3,500 deciduous fruit growers, and the California Fruit Growers' Exchange, composed of 13,300 citrus fruit growers.

**Consolidation of Locals into a Central Exchange.** The local cranberry companies, originally organized as separate sales agencies in Wisconsin, New Jersey, and Massachusetts, use the same selling agency, the American Cranberry Exchange, to coordinate their services in directing advertising, controlling the time and flow of various varieties into the channels of trade, and providing market and production information to the growers in the different states.

**Consolidation of Central Exchanges.** The various poultry associations on the Pacific Coast, as was pointed out in Chap. XVIII, use the same sales agency, the Pacific Egg Producers Cooperative, Inc., for marketing the poultry and eggs shipped to the metropolitan centers of eastern United States.

**Combination of Large Purchasing Associations.** Among the purchase-type associations one can cite the classic example of cooperation between the Cooperative Wholesale Societies of Sweden, Norway, Denmark, and Finland which have organized an international cooperative wholesale society, the Scandinavian Cooperative Wholesale Society, Ltd., Copenhagen, Denmark, which purchases numerous products for its members at wholesale. National Cooperatives, Inc., in the United States also acts as central purchasing agent for a number of the cooperative wholesale companies in this country.

**Cooperation between Purchase and Sales Associations.** One might cite many examples of cooperation between similar types of associations, but one of the most singular instances of cooperation between two large associations representing diverse interests was the rescue of the Grain Growers Grain Company by the Scottish Cooperative Wholesale Society. The Canadian farmers' grain cooperative was expelled from the Winnipeg Grain and Produce Exchange while grain continued to be consigned to the company from many shipping points and the farmer shippers expected to receive an advance of 75 per cent of the current market price. The company could not dispose of its patrons' grain without paying the regular commission of 1 cent per bushel.

It was during this crisis that the struggling farmers' cooperative company obtained substantial relief through another much older and more powerful cooperative company. For the Winnipeg representative of the Scottish Cooperative Wholesale Society, on learning of the Grain Growers' predicament, decided to risk the disapproval of the Grain Exchange and support the newly formed producers' cooperative, not only by buying a large portion of its wheat, but also by allowing it the regular commission of 1 cent a bushel.<sup>9</sup>

The critics of the cooperative movement claim that clashes between various organized groups of producers are unavoidable,

<sup>9</sup> PATTON, HARALD S., "Grain Growers' Cooperation in Western Canada," p. 52, Harvard University Press, Cambridge, 1928.

and that purchasing associations will dissipate one another's good works with their rapacious greed for large volume, low prices, and great savings. If by some chance the organizations of producers on the one hand and the societies for purchasing on the other should escape destruction resulting from competition with one another, they maintain that a breakdown is inevitable when the cooperatively organized producers en masse meet the associated consumers in the market place. It is difficult to find support for this theory by citing actual experiences of large cooperative organizations. The hypothesis that competition tends to diminish as cooperative organizations grow in importance appears to be the most tenable in regard to the future outcome of the movement.

#### CROP CARRY-OVERS

The production of most agricultural products is seasonal, and the consumption of them is relatively uniform throughout the year. This phenomenon is the cause of great inconvenience in distributing agricultural commodities. The character and rate of consumption are relatively immutable. Seasonal supplies must be carried from one period to another.

The variations in production from one period to another create a surplus that must be carried over into the next cycle of production. This kind of surplus is so common to the grain crops that the problem arises of holding and storing supplies against the inevitable lean years. Hence, we have the "ever-normal granary" concept of 1937. With the possible exception of the tobacco associations, few cooperatives attempt to assume the risk of carrying over supplies from one period to another. In the case of major staple crops, such as cotton and wheat, the market organization provides adequate services for hedging against the uncertainties of the future.

In regard to specialized crops, however, the situation is different. The risks of carrying supplies from season to season and year to year cannot be easily shifted to professional "risk takers" without underwriting losses. In some instances, the cooperative associations have assumed unusual risks in the hope of making profits by holding the surplus off the market where associations do not control a large percentage of the total supply. The nonparticipators rush in and take more than their pro-

portionate share of the market opportunities and at the same time possibly spoil the market for those who assume the full burden of holding supplies in an effort to keep the price structure from collapsing. Such policy is suicidal for the cooperative and has led to a demand for clearinghouses and market prorate plans as have been described.

Cooperative institutions that are firmly established with adequate reserves, regular trade outlets, reputation for quality, excellent market services, and trade-branded products constitute an exception to the above situations. These organizations often find it necessary to assume the risks of carrying seasonal surpluses in order to be assured of a sufficient supply of a product of a certain quality to satisfy the requirements of their regular consumers. The flow of the products to market is regulated in such a way that the producers secure the most advantageous average price for the entire market period.

#### COOPERATIVE EXPORT SALES

If the supply exceeds the domestic market requirements, some associations handling specialty commodities organize an export department to sell a portion of the supply that might otherwise completely demoralize a domestic market if forced on the buyers. The Apple Growers Association of Hood River, Oregon, is a notable example of an association that has successfully merchandised a portion of its receipts abroad. The California Fruit Growers' Exchange has been making long strides in the exporting of citrus fruits owing to the recent disruption of trade in citrus crops resulting from the Italo-Ethiopian and Spanish Wars.

In domestic markets much has been done through advertising to make demand mutable. Some associations handling semi-luxury products, which possess a high degree of elasticity in demand, have been eminently successful in avoiding crop carry-overs and great seasonal surpluses by advertising.

#### ADVERTISING

Advertising serves two functions in making sales. One purpose may be to publicly apprise prospective customers of the wares on the market and their particular characteristics. Advertising

of this nature is called educational advertising and is of value from a social standpoint. The more recent and more popular purpose of advertising is to persuade the potential buyer that one particular brand of a product is to be preferred to all others. This type of advertising may have no social value and can not be justified as a means of increasing social capital.

Educational advertising may be made to play an important role in promoting the sales of agricultural products, but on the whole advertising is most profitable where capital is mobilized and large-scale production is carried on under the protection of patents, copyrights, and secret processes. It is more adapted to products with elastic demand, than to those not possessing it, and it is often used to stimulate the sale of products which enjoy some monopoly advantages.

The unbridled competition in agriculture, the number of competing sellers, and the nature of agricultural products have been factors which retarded the use of advertising as a medium for promoting agricultural sales. Since 1915, agricultural cooperative producers have advertised on a national basis in magazines and newspapers. Through the organization of large-scale cooperative sales associations, growers have been able to obtain direct advantages from advertising. In 1928 two associations, the California Fruit Growers' Exchange and the Sun-Maid Raisin Growers Association, were included in the Who's Who list of the first seventy-five companies expending the largest sums of money for advertising space. The number of farmers' sales associations, however, were still distinctly in the minority compared with other industries.

In general, not so much is spent for advertising staples as semiluxuries and luxuries. Advertising is playing an increasingly greater role in the sales made by cooperative associations. It will be noted from the table on p. 523 that several large sales associations spent from 1½ to 3 per cent of their gross sales receipts in 1935 for advertising.

It is logical that agricultural producers should take into consideration the choices and the habits of consumers and take advantage of any favorable trend toward a particular field of specialization in the industry. The change from heavy foods such as fat pork and bread to salads, fruits, and vegetables is quite evident.

Associations	Approximate Percentage of Gross Sales Spent for Advertising
California Fruit Growers' Exchange.....	2.0
California Walnut Growers Association.....	2.0 to 3.5
American Cranberry Exchange.....	4.0 to 4.5
California Prune and Apricot Growers Association	1.75
Pacific Egg Producers Cooperative, Inc.....	0.033 to 0.050
Tillamook County Creamery Association.....	1.5
Land O'Lakes Creameries, Inc.....	0.5
Sun-Maid Raisin Growers Association.....	9.5 to 10

Educational advertising may appear in a number of forms. The agricultural associations have used various distinctive styles of packaging as a means of extending the markets both intensively and extensively. The Colorado Potato Growers Exchange reports that the demand for Colorado potatoes can be readily stimulated by the use of packages with the label of their famous brand Colotato. More recently public announcements have been used to inform consumers concerning heavy frosts, floods, and quarantines which have interfered with the movement of products from one region to another. In many cases the activity of the labor unions in "sit down" strikes has caused a cessation of manufacturing and even business correspondence. Clear and concise statements from the business enterprises involved in such controversies have been deemed necessary to explain to the public the reasons for their omissions and commissions in rendering services during the period of interrupted transactions.

### CONCLUSIONS

Cooperative sales associations are largely incapable of controlling the quantity of production through their own efforts.<sup>10</sup> They are in a better position to influence the quality of production through their grading systems, paying on a graded basis, and through their educational campaigns. In Denmark where 84 per cent of the swine are slaughtered in cooperative abattoirs, it was necessary to institute a government hog-production-control

<sup>10</sup> They have effected some seasonal variation in production, as in the case of fluid milk, through the adoption of the "base-surplus" plans, but in these instances the aggregate production has not been controlled—rather it has gotten out of control.

plan in February, 1933, in order to adjust production and prevent prices from toppling to disastrously low levels. The cooperatives were not capable of restricting the production through their own efforts. In the United States the experiences of cooperatives during the administration of the Federal Farm Board indicated that the vital problem of adjusting production to market requirements was not yet solved. Some abortive attempts were made to keep production down through speeches and exhortations, but the volume of business of the cooperatives and the quantity of agricultural production during these years show that the preachments were in vain.

In fact the successful cooperative is an important force in increasing production rather than in restricting it. If the cooperative is successful in getting good prices for the growers, the cooperative cannot prevent the farmers from reacting to good prices as they always have, namely, to increase their production. The experiences of the raisin growers, fluid milk producers, potato producers, and other agricultural producers need only to be recalled to see what responses are made to good prices. If new markets are not developed so rapidly as the production increases, it is inevitable that prices will drop.

Since the cooperative, as a marketing agency, is concerned chiefly with the distribution of products that agricultural producers as free agents have produced, it is indubitable that if prices obtained per unit of goods are low as a result of excessive production rather than as a result of inefficiency in distribution, the cooperative is not to be indicted for such low prices any more than a private agency should be. The establishment of clearinghouses, market proration plans, export departments, by-products plants, and advertising schemes at best are effective only in creating order in distribution of a product already produced. The producers themselves must do their part in keeping production within the bounds of market requirements.

#### Questions

1. Review some of the conditions following the World War which seriously affected agricultural prices.
2. What measures were taken by the government to improve agricultural prices?
3. Describe a clearinghouse association. Was this form of organization successfully applied in agriculture? Explain.



4. Enumerate some of the objectives of clearinghouse associations. Were any of their objectives attained? Do these associations tend to become permanent enterprises in areas of specialized agricultural production?

5. Contrast the efforts of the lemon growers with those of the orange growers in controlling the marketing of citrus crops during the period 1925-1937.

6. Can proration schemes be classified as one form of cooperative enterprise? Distinguish between compulsory and voluntary proration schemes.

7. Was the California Agricultural Prorate Act beneficial to agricultural producers? To the consumers? What attitude did the courts take in deciding its constitutionality?

8. What are the possibilities of diverting agricultural surpluses into new industrial products?

9. Critically appraise the statement, "a breakdown is inevitable when the cooperatively organized producers en masse meet the associated consumers in the market place?"

10. Under what circumstances may cooperative associations successfully carry over supplies from previous crops?

**PART V**  
**COOPERATION IN PERSPECTIVE**

*Limitations and Possibilities of Cooperation*

*Good and evil are seldom unalloyed in the associations of men whether their institutions are social, political, or economic. Variations in the degree of emphasis given particular factors in a complex organization lead to differences of opinion. What may appear as a possibility to one person may be regarded as a limitation by another. Likewise, a limitation may be considered a possibility. Through retrospection, limitations emerge from observations and past experiences bounding the activities of man. While possibilities may be grounded upon past attainments, they more commonly flow out of the hopes and aspirations of forward-looking individuals in society. Characteristic of the descriptions of all new movements of promise, much of the early literature on cooperation radiated hope and presaged great possibilities. The movement now has age and a status which permits a more critical analysis of its potentialities.*



## CHAPTER XX

### LIMITATIONS AND POSSIBILITIES OF COOPERATION

The cooperative system of buying and selling has its supporters as well as its critics. The enthusiasts see only those things that are promising and are blind to all defects. The antagonists magnify the weaknesses and fail to appreciate the elements of strength. Like all other commercial organizations, it is not immune to attacks. This chapter will present some possibilities and limitations which may enable the reader to gain a broader perspective than may have been obtained in the foregoing chapters.

#### LIMITATIONS

##### THE INERTIA OF THE MASSES

Cooperatives are characterized as group movements in business, and as such they have had to contend with irresolution and indifference since the time of their inception. Preliminary to organizing a cooperative enterprise, months and even years must be spent patiently educating groups of potential members. Often inertia cannot be overcome except through the impulse of outside stimuli. In such cases the masses may be deceived by the catch words of a demagogue. Likewise, well-intentioned but uninformed prophets, as well as opportunists, may present serious dangers to such an economic and social movement. Consequently, one of the major problems in the growth of the cooperative movement is how it may be controlled and directed toward its goal or objectives.

The selecting of the management of a newly formed cooperative frequently offers many problems. Capable leaders may avoid assuming official responsibilities, while those who possess little native ability are often elevated to positions of trust and authority. Such weaknesses are apt to exist in newly founded democratic administrations. After the group acquires experience in working together and in learning to detect business acumen and leadership, it may use more discrimination in the selection of officers and leaders. So much depends upon the choice of good

directors that some plan should be evolved for qualifying members as potential officers and directors in the association. If nominations could be restricted to include only those members who present certain qualifications, the risks of poor management would become minimized. Membership qualifications based, at least partially, upon interest in the enterprise should help to eliminate many inert members. The causes of inertia are inherent in men but may be modified to some extent by their environment. However, their susceptibility to new ideas is retarded by established institutions which tend to preserve the old traditions, habits of thought, customs, and folkways. Many people are still influenced by the words of Pope, in his "Essay on Criticism,"

Be not the first by whom the new is tried,  
Nor yet the last to lay the old aside.

**Provincialism.** The composition of a population has a decided effect upon the extension of cooperation. Modern improvements in communication and transportation have broken down the former barriers of isolation. Both telephone and radio provide excellent means for disseminating information, but there is need for government supervision as well as instruction in a wiser utilization of these facilities. The length of time necessary for the dissemination of new ideas through different segments of society is illustrated by the dates at which similar laws have been enacted in different states and countries. In England the federation of local cooperative societies into central exchanges was legalized in 1862. Twenty-five years later (1887) Wisconsin, the first of the United States, permitted by statute the federation of local associations. Various states enacted cooperative laws a quarter of a century before the federal government passed the Capper-Volstead Act of 1922 recognizing cooperative business associations. Such phlegmatism accounts for the slowness with which the ideas of cooperation permeate the masses. Some parts of America, as well as some areas of foreign countries, are still completely devoid of cooperative business enterprises. These areas have been called "cooperative deserts,"<sup>1</sup> and they are not necessarily the most sparsely settled sections.

<sup>1</sup> WEBB, SIDNEY and BEATRICE WEBB, "The Consumers' Cooperative Movement," pp. 311-321, Longmans, Green & Company, New York, 1930.

**Heterogeneity of Population.** The immigration from foreign countries has populated many sections of the United States with groups of people who differ greatly in their cultural background. The influence of their customs, habits, and mores persists for several generations. Some immigrants have introduced new ideals and methods of applying them that command general admiration. Frequently, their technique of organizing and managing cooperative enterprises is superior to the existing methods. This illustrates that homogeneity on a national basis is not essential to congenial relations in a community. The descendants of different nationalities often work together as harmoniously as if they had all descended from one nationality. It will in all probability be difficult for an agglomeration of persons of different races to cooperate. Also widely divergent cultures may hinder a cooperative undertaking. Their differences in standards of living, languages, and theories of organization may result in factional schisms and destroy the basis of organization. But more serious limitations to the development of cooperatives may be presented by differences in economic status or by educational training.

**Consanguinity.** Some communities become very closely knit through marriages and intermarriages. Family ties are taken into consideration in many business transactions, and the lineal relationships exert influence in every direction. It is difficult to create new institutions in such inbred neighborhoods because the established businesses are owned by cousins, uncles, nephews, and brothers. This type of community resembles a communal organization more than an economic society of free enterprises. The blood and marriage ties are important causes of inertia, as well as factors which make the group unwieldy in administrative functions. Thus, consanguinity may stubbornly resist cooperative organization even though sound economic reasons may make for its promotion.

#### TENDENCY TOWARD REVERSION

Many members of cooperatives tend to revert to their former methods of marketing instead of continuing their connections with the cooperative. Cooperatives should emerge from a recognition of needs, and the initiative should come from within

the group. Unfortunately, the impetus is sometimes furnished by someone from outside, and allurements may be proffered that are impossible of fulfillment by a missionary or professional type of promoter. Consequently, the association encounters ill will and widespread misunderstandings from the first, and some new organizations fail to regain the full confidence of their members. As soon as the flame of enthusiasm dies down, and the inspiring promoters have gracefully made their bow, the members begin asking "How can I get out of this association and cancel the obligations I have assumed?" This is illustrated by the experiences of the many large, centralized cooperative marketing associations now defunct that were formed in the postwar period 1921-1924 and fortified with a five-year ironclad contract and a monopolistic price concept.

Associations that are formed by the participants have a better chance to endure, but even then the movement is burdened with many individuals who fail to understand the main objectives. Much education is needed to sustain the morale of some organizations; failure in this may cause dissatisfied members to withdraw. The number withdrawing may be so great as to necessitate a reorganization of the association. It is not uncommon to find that existing successful associations had to be re-organized two or three times before they were loyally supported by their members. The teaching of cooperation in the public schools, the organization of cooperative councils, and the general dissemination of information about the aims and purposes of the movement may minimize the influx and outflow of members. The smaller turnover in members will stabilize the cooperative institutions and lessen the risks of financial losses to members. There is little tendency, however, to abandon *successful* cooperatives as the following statement made by the manager of the Wisconsin Cranberry Sales Company indicates:

Cranberry growers have a spirit of cooperation that perhaps has no equal in any other industry. The Wisconsin Cranberry Sales Company, for example, has no written yearly contract or pledge from its members—yet every member delivers all of his berries; there is no outside selling; there are no members dropping away from the organization.<sup>3</sup>

<sup>3</sup> GOLDSWORTHY, VERNON, Cooperation Plus Advertising, *Cooperative Journal*, vol. 11, no. 2, pp. 41-42, March-April, 1937.

**THE DIFFUSION OF BENEFITS**

Cooperative associations are occasionally alluded to as self-liquidating corporations. Their success may cause their destruction. For example, a cooperative association is organized to market a speciality crop such as blueberries. It introduces new methods in handling, grading, storing, packaging, and selling so successfully that the prices of this product are appreciably increased. New capital flows into the industry because it is profitable. Production is increased, and the association is forced to put forth additional efforts in making sales large enough in volume to satisfy the growers. This procedure is continued until the market is completely satiated. Additional sales cannot be made at prices that will return prime costs. Prices fall and a surplus of berries accumulates. The association thus becomes ineffective as a factor in determining market prices. Other marketing agencies imitate its methods in handling, packing, and shipping the berries. The buyers pour capital into the industries to offset losses, and the association attempts to support the price structure from complete demoralization by regulating the flow of products to market. During this time, however, the private agencies that are not under obligation to receive or buy berries, except as needed to supply a limited number of customers, may continue to ship berries into the market taking more than their proportionate share of sales. The cooperative under these circumstances may report lower returns than private agencies, and, if it does not have an enlightened membership to support its policies and program, it is destined to fail. Such instances are often cited by those who wish to discourage cooperative efforts.

From a social standpoint the diffusion of benefits may not be a weakness of the cooperative system but one of its strong points since all agricultural producers profit from the existence of the cooperative.

The sales associations that adhere to the principle of rendering services at cost not only induce severe competition but often precipitate price wars. Market prices are temporarily increased and the normal price over a long period is raised. All bases for comparison are erased in the competitive battle. A cooperative association may do only a small part of the total business, but its



existence during such a period is particularly beneficial to every producer in the community. Hence the expression, "It's not what prices are. It's what they would have been if there were no cooperative in this community." This characteristic of cooperative business limits its rapid development because many producers prefer to be on the outside where they may get all the benefits of the competition without assuming any of the possible costs. A few sales associations have been able to retain the gains from their services for their members by creating special market outlets for the products, which only their members produce, as well as through the use of patents, copyrights, secret processes in manufacturing, trade brands, skillful administration, and advertising. But a majority of the associations experience difficulties in attempting to prove the merits of their services as measured by improved financial returns to its own members.

#### EDUCATIONAL LIMITATIONS

The progress of cooperative sales associations may be impeded by a high percentage of members who have a limited education. This is true of certain geographical areas in both America and Europe.<sup>3</sup> It is difficult for uneducated people to understand marketing methods, to shoulder the responsibilities of membership, and to wisely direct marketing organizations. If the members of a cooperative are uneducated many internal operating problems occur that result in an expenditure of time and money which could have been used for productive enterprises. However, a cooperative that educates its members in marketing and production problems and develops latent rural leadership is an organization that may be looked upon as a social benefactor.

**Unreasonable Demands of Members.** Members with a limited education often make highly impractical demands upon their cooperative. A large portion of the members, and many nonmembers as well, consider cooperatives as reform agencies and may even expect accomplishments which are

<sup>3</sup> MANN, T. B., reports in *Farmers' Experiences and Opinions as Factors Influencing Their Cotton-Marketing Methods*, U. S. Dept. Agr. Circ. 144, 1931, that 63.4 per cent of the members and 75.9 per cent of ex-members had less than a high school education. Of these groups, 29.5 per cent of the members and 43.9 per cent of the ex-members had even less than common or country school education.

impossible of achievement. They are quick to criticize an association for not rendering certain services or obtaining certain prices even though the association, measured by ordinary business standards, is moderately successful. The impractical demands may vary considerably, but they usually center around the price which the cooperative is able to obtain for the producers. Producers and consumers frequently disagree as to what a *fair* price is. Consequently, it is apparent that it is an impossibility to please all members at all times. This condition is not an inherent weakness of the cooperative method of marketing but simply a situation which it must face.

#### INADEQUATE FINANCIAL RESOURCES

The majority of the members of a cooperative association have a low or moderate income. As a result many cooperatives suffer from inadequate financing and are forced to adopt a policy of delayed payments. Although the members may give their association wholehearted financial support, such support may be inadequate. Heavy lending follows, and the operating expenses of the organization are increased by interest payments. Members who regularly require outside financial assistance in producing a crop are often a burden to the organization and hinder its sales programs. For example, there is less expense entailed in paying creamery patrons once a month than semi-monthly or at time of delivery. Yet the financial situation of some producers is so stringent as to require cash on delivery. In order to make frequent payments the creamery is forced to make sales at inopportune times. Some of these difficulties have been mitigated by cooperative credit agencies, but for many associations, the financial handicaps are weaknesses which are difficult to overcome. Many of the problems that existing cooperatives face would be eliminated if the organization dealt exclusively with well-to-do persons who could provide adequate capital to start and promote the business, and who could permit the management to adopt a sales program which would not be pressed for early sales remittances.

The limited financial resources of the members make it necessary that a large portion of the net earnings be returned to the members as patronage dividends. Such demands are usually met, since the farmers who are on the boards of directors are

frequently in as great need for the patronage dividends as their neighbors. This results in failure to build up adequate reserves with which to weather a period of financial stringency.

This applies more to the local organizations than to the large-scale cooperatives. In a large-scale organization, special care must be exercised by the directors to prevent extravagance and careless spending which may easily occur once an organization becomes powerful and controls all or nearly all of a given crop. In such a situation there can be no standard of comparison with competing firms, and huge sums can be accumulated from small deductions on a large volume of produce. The failure of some large cooperative sales associations in the United States is attributable to such a policy of reckless expansion made comparatively easy by small deductions from the returns of the thousands of producer members.

#### FAILURE TO ESTABLISH MEMBERSHIP RESPONSIBILITY

Cooperative associations often fail to create a feeling of responsibility among their members. Many members regularly consign their products to their association but fail to attend annual and special meetings where policies and other matters of operation are discussed and voted upon. Hence, the members may participate blindly without fully understanding the principles of the cooperative philosophy. Cooperative leaders and enthusiasts have been prone to criticize the large corporations on the grounds that they are not democratic, that they are controlled by an esoteric group, and that ownership and control are divested from each other. True as this may be in many instances, cooperatives themselves are not entirely free from similar criticism, although in principle they stand for economic democracy. Cooperatives in America and in Europe often have less than 10 per cent of their members present at annual meetings. "While criticizing management control of private corporations, The London Cooperative Society, for one illustration, seldom has more than 1 per cent of its members voting in the annual meeting—and of less than 3,000 who voted in the last series of annual meetings more than 2,000 were employees."<sup>4</sup> The London Cooperative Society has a membership of over 300,000.

<sup>4</sup> HOOD, ROBIN, *Implications of European Consumer Cooperation*, *Cooperative Journal*, vol. 11, no. 2, p. 57, March-April, 1937.

The indifference on the part of members toward their organization results in a failure to make their cooperative "farmer controlled" as well as "farmer owned." The following quotations are illustrations of such situations:

Some of the associations which have directors elected by the members or by delegates selected by the members report that those who participate in the selection of directors or of delegates represent only a small percentage of the total membership. Approximately half of the associations reported that less than 25 per cent of the total membership participated directly or indirectly in the last election of directors. . . . Some associations can only estimate the number of members belonging to the association and the percentage participating in elections, because they have set up no system for regularly purging the membership roll.

The following quotation, taken from an unpublished report made to the Cooperative Division of the Farm Credit Administration, probably would apply equally as well to some other associations. "[Owing] to the lax system of keeping track of its membership in the association, the annual election of directors has developed into more or less of a cut-and-dried affair resulting in the election of the same men year after year."<sup>5</sup>

The above reports show that although a cooperative should be "member owned" and "member controlled," in many cases it is an ideal that is not realized. This is owing to the absence of a feeling of ownership, which is especially true of cooperatives organized on a nonstock membership basis in which much of the capital has been derived from member loans and earnings of operations.

#### QUASI-PUBLIC NATURE OF COOPERATIVES

Several states provide that a representative of the public may be permitted to sit with the directorate of large-scale associations whenever public interest may be affected by their decisions because cooperative organizations are of a quasi-public nature. One serious mistake or failure seems to make a more lasting impression on the public than many successful ventures and notable achievements. Enemies of the movement take advantage of the human propensity for remembering unfavorable events by pandering half truths which effectively hinder progress.

<sup>5</sup> JONES, J. W., *Membership Relation of Cooperative Associations*, Farm Credit Administration, *Bul.* 9, pp. 44-48, 1936.

Even though private corporations may have hundreds or thousands of stockholders they may not become semipublic institutions as do the cooperatives. It is essential for cooperative organizations to keep the members constantly informed about their operations. The books must be open at all times for inspection by the members for valid purposes, and the members must be educated in the principles and practices of their movement. The association must decide to keep its members informed even though such procedure also apprises its competitors of its activities or it may choose to withhold information and run the risk of generating acute membership problems because its members are uninformed about the affairs of their enterprise.

#### INABILITY TO PREVENT EXCESS PRODUCTION

Under the cooperative system, the benefits of all increased market prices and reductions in the cost of marketing are returned to the producers more quickly than under the private system of marketing in which such benefits are reflected for a time in increased profits to the middlemen. As a result members of cooperatives receive a quicker stimulation to increase their production than they would under the independent system of marketing. If farmers used their increased returns to buy greater quantities of consumption goods rather than diverting it to land, equipment, or other production goods, increased agricultural production might be prevented. But an analysis of the cyclical production of many agricultural products shows that farmers respond to increased net returns by increasing their production. This is particularly true for such products as fluid milk, hogs, cotton, potatoes, and tobacco.

Realizing this tendency of farmers to respond to higher net returns by an increased production, many of the cooperatives have attempted to discourage such reaction through exhortation and through devices such as the base-surplus plan of payment in the fluid milk markets. These attempts to adjust the volume of agricultural production have not always been effective.

#### INDIFFERENCE OF EMPLOYEES

It is assumed that most men will work more diligently and faithfully in a private business where there are prospects of

gains than they will for wages in a cooperative association. The problems that arise between members and employees in large-scale cooperative associations rest fundamentally upon the fact that their interests are not identical. The employee is interested in receiving good wages; the cooperative member's main interest is to receive better prices for his goods and better services at less cost. This difference in objectives may lead to an exploitation of the members by the employees or of the employees by the members, according to which group is in the more advantageous bargaining position. This difference in interest influences the attitude of the employees toward the members. The services tend to lose the personal touch that private businesses attempt to include with every transaction.

It is axiomatic that one spends other people's money more freely than his own. The funds are usually well controlled in an association, but this contention has an element of truth in it when applied to the use of machines, materials, and other properties. Another reason for the employees' dissatisfaction is that farmers will not pay large enough salaries to attract good management. The basis for this assertion is that producers are reluctant to pay their managers more than they themselves are able to earn. However, if low managerial wages are paid by an association, it is logical to conclude that internal control may be lax, that the employees may be indifferent to the best interests of the members, and that the whole enterprise may be affected by poor administration.

It has also been contended by critics of cooperative purchasing associations that if these associations succeed in lowering the costs of operating stores it will be at the expense of the employees, since wages constitute the largest item of expense in merchandising. Cooperatives, it is held, will lower the level of wages. If money wages were actually lowered and all possibilities of gain through the efficient operations of an integrated system of marketing discounted, even then real wages might be increased appreciably to offset decreases in money wages.

#### DEVIATION FROM PRINCIPLE

It is regrettable that the principles of a true type of cooperative enterprise have not been the subject of research investigation by some central authority.

In Chap. VI, nine principles are listed which are considered basic to cooperative sales associations. There are many existing associations, however, that could not apply these principles without making major changes in their plans of organization.

With the exception of the two or three principles which have usually been incorporated into laws for definitive purposes, there is no unanimity on this subject among American writers or experts. Neither has it received the attention it merits. Many failures in cooperative undertakings can be traced to the fact that the fundamental principles of cooperation were not clearly recognized. As a consequence, such undertakings became hybrid enterprises observing two or three cooperative principles along with a larger number of precepts or rules taken from private enterprises.

The accretions of experience which American cooperatives possess should be made available so that future organizations will be able to use them as a guide. The organized producers might undertake a study similar to that which has been made recently by the International Cooperative Alliance, an organization which represents the consumer cooperative movement of the world.

It is not to be presumed that this is a conclusive summary of the limitations of cooperative enterprises. These limitations will vary in their importance for diverse groups in different places attempting to apply the cooperative method to unlike types of organizations.

#### SUMMARY OF POSSIBILITIES

Many advantages have been enumerated throughout the preceding chapters, and it seems unnecessary to recapitulate them here. In place of a summary of these, the advantages given by other authors are stated. Their lists and summary statements include many of the main advantages found elsewhere in this book.

A cooperative marketing organization is a very useful instrument for farmers. It enables a group of producers to secure more practical information and to act more intelligently in its use than is possible for the unorganized. It is not, however, a means of guaranteeing profits to anyone, or of changing bankrupt agriculture suddenly into a profitable industry. Cooperation is a slow-working, evolutionary process of

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leading men to and through the doorway of organized endeavor as a means of solving difficult problems. For those who have stubbornly persisted in applying sound economic or business principles in their cooperative endeavor, there have been decidedly worth-while results.

According to the experience and judgment of the old and well-established cooperative companies, there are eight principal kinds of cooperative benefits. These in turn are characterized as tangible and intangible. Those benefits which are not subject to actual financial measurement are intangible, owing to the difficulty of measuring them definitely in dollars and cents. Briefly stated, according to the foregoing classification, these eight proved benefits of successful cooperative marketing are:

1. Tangible or Financial Benefits
  - a. Gives farmers the profits of marketing that ordinarily flow to middlemen
  - b. Reduces costs of marketing so far as practicable
  - c. Improves old and devises new standards of marketing service
2. Intangible or Nonfinancial Benefits
  - a. Readjusts standards of production
  - b. Establishes farmer confidence in the marketing mechanism
  - c. Gives farmers conviction that products are marketed in the most efficient way possible
  - d. Stimulates and develops an agricultural leadership
  - e. Helps to make marketing efficient, farming profitable, and living worth while

All of these beneficial results of marketing cooperatively obviously have not been obtained by every farmers' organization nor have they all been realized by any company. Yet this classification brings together the actual gains of one kind or another for which the cooperative movement is the chief sponsor. Every marketing organization has within it the possibility of bringing to its members most or even all of these advantages.<sup>6</sup>

Another authority on the subject of cooperation states that cooperatives are capable of:

- Standardizing and improving production
- Standardizing and improving grade and pack
- Stabilizing production
- Controlling flow to market
- Improving distribution between markets
- Advertising and the development of new markets
- Collective bargaining

<sup>6</sup> MACKLIN, T. M., *The Annals, American Academy of Political and Social Sciences*, vol. 117, no. 206, p. 208, Philadelphia, January, 1925.



Individually the farmer is a notoriously weak bargainer because

1. He does not know in what grade his product falls
2. He does not know the relative value of different grades
3. He does not know what his local price should be even when central market prices are known, and frequently he cannot even interpret wholesale market quotations
4. He cannot follow market conditions closely enough to know at any given time whether market tendencies are up or down
5. He is slow in judging a proposition put in a new way

Financing of marketing operations

Making marketing more efficient

Maintaining favorable public relations<sup>7</sup>

The Federal Trade Commission in a recent report on agricultural income came to the conclusion that cooperative organizations are an efficient means of alleviating unfavorable conditions in agriculture.

Although a measure of proof in the terms of dollars and cents of the value of cooperative associations is difficult to obtain, the commission desires to add its opinion to the vast body of opinion to the effect, namely, that true cooperative associations have been of great value to the producers of farm products. These cooperatives have significantly increased the bargaining strength of producers and have reduced the spread between producers' and consumers' prices . . . <sup>8</sup>

#### Questions

1. Prepare a list of the limitations which most commonly obstruct collective action in your community.
2. Give your interpretation of the word "provincialism." Cite some instance of provincialism which you have observed in your travels.
3. Is homogeneity of race and cultural background an essential to successful cooperation?
4. Explain the term "consanguinity." Do you know of any consanguineous communities or neighborhoods?
5. Are the diffused benefits of cooperation to be regarded as a limitation or an advantage to:
  - a. The members of the cooperative
  - b. All producers of the particular commodity handled in the region in which the association operates
  - c. Everyone within the market area

<sup>7</sup> ERDMAN, H. E., Possibilities and Limitations of Cooperative Marketing, *Univ. Calif. Agr. Exp. Sta. Circ.* 298, pp. 1-13, 1925.

<sup>8</sup> Report on Agricultural Income Investigations, mimeograph release, The Federal Trade Commission, Mar. 2, 1937.

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- 6. When are members most likely to revert to former methods of doing business? Why? How can the tendency to reversion be overcome?**
- 7. Have cooperatives had difficulties in getting members to assume positions of responsibilities in governing the affairs of the association?**
- 8. Make a list of disadvantages which you believe apply particularly to your home community.**
- 9. Why should a distinction be made between tangible and intangible benefits?**
- 10. Review the various advantages of cooperation that have been mentioned by the authors in the previous chapters.**

*The Future of Cooperation*

*A reappraisal of the present status of cooperative marketing is essential to anticipate the forces which will mold the movement in the future. One outstanding feature of the present-day status of cooperative marketing is its youthfulness. Few local organizations were in operation before 1880, and most central marketing associations appeared after 1921. Since these dates, however, the individual associations have had a wide range of experience in the use of membership contracts, sales operations, plans of organization, membership relations, and other problems peculiar to cooperatives. Out of this welter of experience many strong organizations have emerged that give promise of greater service to their members in the future. Cooperative marketing, cooperative purchasing, consumers' cooperation, as well as cooperation in the fields of credit, insurance, and other "service" fields have been preparing the ground up to now and may be expected to blossom forth and bear larger fruit in the years ahead than has been yielded to date.*

*Developments in agricultural production, governmental intervention in agricultural marketing, increasing efficiency of private competitors, and changes in transportation and communication will affect the organization and operating practices of marketing associations. It is almost a certainty that at no time will all farmers belong to marketing or purchasing associations or all consumers to cooperative retail and service organizations. Hence, two systems of distribution, the private and cooperative, will continue to compete with one another, each acting as a check and balance upon the other, and both striving for greater efficiency in the battle of competition.*



## CHAPTER XXI

### THE FUTURE OF COOPERATION

The authors do not wish to appear oracular in writing about the future of cooperative marketing in America. The manifold economic forces that will mold the cooperative movement in the future are largely a matter of conjecture. Before enumerating the forces which will affect the growth of the movement and the developments that may transpire, it is well to consider some of the outstanding features of its present-day status.

The cooperative marketing movement is still in its infancy compared with the private commercial organizations and the movement includes only a small percentage of the total number of producers of the country. Only a very small percentage of all farm products is sent all the way through the trade channels from producer to retailer or from producer to final processor, although practically every type of commodity is handled or processed by a cooperative during some stage of its distribution.

The movement has been given legal sanction through widespread enabling legislation and decisions of the highest courts of the country. It has received positive endorsement, promotion from state and federal authorities, and encouragement everywhere by leading citizens and civic institutions. Cooperative organizations have been freely given financial assistance, legal advice, and economic counsel from public supported commissions, educational institutions, and agricultural departments.

Associations within the movement readily pass on to other associations information relating to their operation and management. National and international institutes and conferences are arranged for this purpose. Such contacts tend to create an *esprit de corps* that leads to a certain solidarity within the movement. Education has been adopted as the surest means of perpetuating the cooperative principles. Repeated attacks by private dealers have often helped to unify what might have

been discordant elements in an effort to meet their mutual opponents.

There is a considerable amount of competition and rivalry among cooperatives which is particularly true of local associations. The trend toward federation lessens the severity of local competition because it calls for unified effort with a common program. There are many benefits of a central organization such as the elimination of duplication and waste in the assembling and processing of farm products near the point of production. The Federal Farm Board was influential in organizing national cooperative companies whose purpose it is to unify the cooperative sales companies and coordinate their efforts in the interest of a particular commodity group. The Farm Credit Administration affects the control of agricultural credit, and, consequently, its influence helps to avoid cross purposes and conflicts within the movement although no managerial responsibilities are assumed.

#### CHANGING CONDITIONS NECESSITATE FUTURE REORGANIZATION

Changes in the organization of cooperative associations may be expected. Improvements in transportation and communication will most likely cause local associations to expand so as to include members within a larger area of production. Local associations, instead of identifying themselves with individual shipping points, will widen to include several shipping points. Small regional associations embracing part or entire counties will undoubtedly be more common in the future. This change is definitely under way in the dairy regions where consolidations of several creameries and cheese factories are being effected. County-wide associations of livestock producers also illustrate the modern trend in the cooperative movement.

As cooperative associations become older, the number of stockholders that have moved away from the community, retired from farming, or deserted the cooperative increases. This results in a smaller percentage of stockholder members controlling the affairs of the cooperative. As the percentage of patron-members decreases, the democratic aspects of the association tend to disappear. Consequently, a reorganization of cooperatives will be necessary, especially if loans are requested from federal agencies, because such loans today require that 50 per

cent of the cooperative's business must come from patron-members. In all likelihood the revolving plan of stock ownership will be used by more associations in the future than today in order to vest the control in the hands of those who use the association.

#### AGRICULTURAL PRODUCTION AND COOPERATION

Future reorganization in industrial and agricultural production will probably be a major factor changing the character of the cooperative movement. The cooperative business institution of today is fundamentally an outgrowth of the small-scale unit farming system. It enables small producers to apply mass distribution methods to their widely separated and individually operated farming units. Will the American farms of the future be the small-scale, family-sized producing units as of the past, or will they be large-scale corporate or chain farms? If the former persist, as many believe they will, then the need for collective marketing will continue. If "capitalistic" farming organizations predominate, we can expect less need for the local associations, although central marketing associations will not be affected. Under the latter system, centralized sales associations instead of federated sales organizations will be formed. The associations of the large livestock ranchers in the West and Southwest, of the citrus producers of the West, and the fox and fur ranchers of the North serve as examples. The large producers, however, are generally less disposed to cooperate for marketing purposes.

The extent and nature of governmental programs relating to agricultural production, marketing practices, and price fixing will, no doubt, have some effect upon cooperatives. In all probability the expressed purpose of the government is to increase the net agricultural income. If this materializes, many farmers who are members of cooperatives may in the future find less necessity for such relations. Today, either the state or federal government agencies fix the prices paid in many milk markets.<sup>1</sup> Extra persuasion is necessary under such conditions

<sup>1</sup> In late 1936, twenty-one states had laws on their statute books regulating milk marketing, many of which included provisions for fixing prices to producers and to consumers. The twenty-two states were: Alabama, California, Connecticut, Delaware, Florida, Indiana, Maine, Maryland,

to convince farmers that as strong a farmers' cooperative is needed now as before to adequately represent the producers' interests in making price agreements. The effect which government price fixing may have upon the associations that rely upon bargaining power solely is problematical. Some associations will most likely shift their emphasis from considerations of price to that of other marketing problems, such as hauling, credit, procurement of quality products,<sup>2</sup> and internal operating economies.

Many cooperatives have exerted considerable influence over the production policies of their members, especially as they relate to the quality and kind of products to be delivered to the cooperative. This influence is illustrated in fluid milk markets by associations that inaugurated the base-surplus plan as a method of paying for milk and reducing the great unevenness of production during the year. Other dairy associations have reduced the bacterial count in the milk through proper education of their members and through a scheme of differential payments. Many fruit and vegetable associations have been able to get their members to concentrate upon the production of selected varieties. Such direct and indirect influence upon production will characterize the future.

#### PROBABLE CHANGES IN COOPERATIVE PRINCIPLES

Since customs and practices of cooperative methods vary from period to period, laws pertaining to cooperatives may likewise change to meet the newer problems. In 1936 thirteen states permitted voting on a participation basis. The other thirty-five states still limit all voting in cooperatives to a one-man, one-vote basis. It is anticipated that amendments will be made to

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Massachusetts, Montana, New Hampshire, New Jersey, Oregon, Pennsylvania, Rhode Island, Utah, Vermont, Virginia, West Virginia, Wisconsin, Wyoming.

<sup>2</sup> Some states, Mississippi, for example, have passed laws requiring the grading of cream and payment for same on a differential basis. Such legislation attempts to secure equitable treatment of producers by law and promotes improvement in the quality of farm products through governmental edict. Cooperatives have made such objectives a major part of their programs for years. If the government undertakes to do this in many states, what effect will it have upon cooperatives?

many state laws in the future modifying the plan of member representation.

#### EFFICIENCY VS. NARROWER MARKETING MARGINS

The cooperatives of the future may center more attention upon efficiency in marketing services than upon patronage dividends and price comparisons, although today many members judge the success of their associations by the amount of the patronage dividend declared. As cooperatives become more numerous and successful, the margin upon which private competitive dealers operate tends to narrow thus making it more difficult for cooperatives to show the comparatively greater financial results that they have in the past. It is reported in the south that the spread between prices paid at interior markets and at central markets for cotton has been greatly narrowed since the cotton cooperatives started in 1921. Comparable reports emerge from dairy, livestock, and grain producing regions. In early years emphasis was placed upon the spread in price between local and central markets. Often these spreads were so great and the results of cooperatively selling so impressive that it provided a strong incentive for collective action. In more recent years, the spectacularly wide spreads are exceptional. Greater interest on the part of unaffiliated locals in central marketing associations, in expanding the uses of their products, in widening market outlets, in integrating marketing operations, and in accomplishing internal operating efficiencies may be developed as a result of more severe competition.

The efficiency of established cooperatives has tended to cause buyers of farm produce to pay prices comparable to the net returns obtained by members of cooperatives and has caused sellers of farm supplies to reduce their prices to the level of the prices charged by farm purchasing associations. Competitors of cooperatives have found it necessary to become more efficient or to operate on smaller margins. Thus, the cooperative has extended the benefits of cooperation to nonmembers as well as members. Agriculture in general is benefited. As a result many producers have felt no need for joining a cooperative. The future extension of the selective membership principle may result in fewer individuals belonging to cooperative enterprises, but the quality of the membership will be improved to such an extent



that the disadvantage in the reduction in numbers will be compensated.

It is not anticipated that all farmers will belong to cooperative marketing or purchasing associations. From a purely practical point of view, it is better to have the extreme individualists on the outside rather than on the inside where they may be ever-disturbing elements. As long as the institutions of free enterprise and individual liberty continue in this country, some producers will prefer to remain outside the cooperative movement. Their wishes should, of course, be respected. In countries where the cooperative is further developed than in the United States, many farmers are found who do not belong to a cooperative.

#### COOPERATION BETWEEN PURCHASING AND SALES ASSOCIATIONS

The cooperative purchasing movement has made considerable progress during the recent years of depression, although the amount of business at wholesale and retail is a very small portion of the total. Much of this movement is confined to retailing. In all likelihood the future may witness a closer working relationship between the producers' sales associations and the purchasers' cooperatives. That such a working relationship may be for the mutual advantage of both groups is entirely possible. The experience of the British cooperative consumer movement leads one to conclude that greater economies and larger social values are achieved when strong consumer cooperatives and strong producer marketing cooperatives operate than if the consumer cooperatives themselves operate agricultural enterprises. Organizations of producers for marketing and of consumers for purchasing recognize fundamental interests of members and will in all probability characterize the development in the future. Today the cooperative marketing associations are handling considerably more products than the existing consumer organizations require, but in years to come, larger sales to the consumers' groups will very likely be made.

#### THE EFFECT OF RURAL EDUCATION

The number of farm boys and girls that complete primary schools, go to high schools, and attend colleges is increasing every year. Such general increase in the education of the rural youth augurs well for the cooperative movement. The large number

of young men from the farms that attend the short courses of agriculture in agricultural schools may provide many of the future leaders for the movement. General education of both the prospective members and potential leaders in the cooperative movement should insure better members, objectives, and more permanent institutions. A number of studies on membership relations indicate that educated farmers are generally better members than farmers who have not had the advantages of a formal education. Intelligent leaders supported by intelligent followers strengthen any movement.

#### EXPERIENCE AND THE FUTURE

Any new undertaking has its "growing pains," its mistakes, its failures, and its successes. The cooperatives have had their share of these experiences. One can legitimately claim larger future possibilities for the movement in general than have already been experienced by many individual associations in the past. The productivity of a mature institution is obviously increased with its age. Fewer failures should be experienced if the lessons of experience are heeded.

No doubt, some fraudulent cooperatives will appear to capitalize upon the good name of the movement. The movement will always appear attractive to ulterior-minded individuals in society, and its leaders will have to be alert at all times in guarding against the selfish motives of unscrupulous individuals. Such, however, can be reduced to a minimum if the individual states will set up functioning "councils of cooperatives" from which endorsements in the nature of "certificates of necessity" must be procured before any new associations are launched.

New types of cooperative associations will continue to make their appearance. Such will be true especially in the fields of "service" cooperatives. Cooperative insurance companies—life, accident, automobile, fire, theft, and hail—burial associations, housing associations, laundries, restaurants, savings banks, credit unions, medical and hospital associations, legal associations, electric and gas associations, transportation, communication, and irrigation organizations will be found in all probability in increasing numbers in the future. Many of these have been started since 1930 and, based on their experiences within the past several years, promise to expand considerably in the years ahead.

Among the "service" associations which may become important to agricultural producers in the future are the credit unions. These unions are patterned after the Raiffeisen associations of Germany where they serve principally the rural population. The credit unions in the United States have made their greatest advance in urban centers, but expansion in rural areas is also predicted. The credit unions may, likewise, organize their own banks to hold and utilize the surplus funds of the individual unions. The development in credit union banking foreshadows a cooperative banking system which may ultimately serve all types of cooperative associations. Such a system would be the counterpart of the private banking system which has developed in this country to serve primarily private commercial and industrial concerns.

#### THE FUTURE OF FARM PURCHASING ASSOCIATIONS

In the next two paragraphs Dr. Knapp states what he believes to be the chief considerations influencing the future of farm supply associations.

Leaders in the cooperative farm-supply movement do not believe that the time will soon come when farmers will buy all supplies cooperatively. Rather it is their view that cooperative purchasing associations will continue to develop only to the extent that the benefits of cooperative purchasing can be clearly demonstrated. In a number of areas there has been a noticeable increase in the efficiency of commercial competitors owing to the presence of efficient cooperative purchasing associations, which may be likened to the improvement of operating practices of local merchants which has been due to the competition of chain stores and mail-order houses. These cooperative purchasing associations, by injecting more competition into farm-supply distribution, have thus performed a general service for the agricultural industry in that they have reduced the general cost of farm supplies and brought about a general improvement in quality and service. With the improvement in competitive agencies, it becomes increasingly difficult for cooperative purchasing associations to expand their direct field of service. At the present time, however, there is a broad field in which properly organized and well-operated cooperative purchasing associations can expand since such associations have demonstrated that they can operate as efficiently as commercial concerns. Any appraisal of the future place of cooperative purchasing associations in the distribution of farm supplies must furthermore take into consideration the fact that

there are certain noncommercial satisfactions that farmers derive from belonging to their own organization.

The future of cooperative purchasing of farm supplies in the United States will no doubt be closely related to the future of cooperative marketing since cooperative purchasing and cooperative marketing are both designed to make the farming enterprise more successful. While cooperative purchasing endeavors to provide a more economic source of farm supplies, cooperative marketing endeavors to secure a more efficient system for selling farm products. In many cases cooperative purchasing and cooperative marketing have been carried on jointly by the same agency in a very satisfactory manner. An expansion of such joint operation is to be expected, although there will no doubt continue to be many strictly purchasing and strictly marketing associations.<sup>3</sup>

This treatise on "The Economics of Cooperative Marketing" is an attempt to appraise the cooperative movement as a means to attaining a more abundant material wealth and a richer spiritual life. Those who aspire to greater perfection in the organized relationships of man in his struggle against economic scarcity and social insecurity may find some encouragement in these pages. The foresight and indefatigable efforts of large groups of socially minded people who have worked and learned and profited from collective action have made this publication possible.

We hope this book will inspire others to press on in their investigations of the less well-known phases of this subject in order that its fullest potentialities may be discovered.

#### Questions

1. Why is "dualism" (two cooperatives in rivalry for the same membership) a destructive influence within the cooperative movement? Why not a constructive one?
2. What serious consequences follow from having a diminishing number of stockholder-patrons taking an active part in the affairs of the cooperative? How may this situation be corrected?
3. Is it as essential for large-scale, "capitalistic," producers to cooperate for marketing and purchasing purposes as it is for the small producers?
4. Does successful cooperation spell the doom of the movement?
5. Do you concur in the following statement "Efficient cooperatives succeed in getting larger net returns for the members; larger net returns

<sup>3</sup> KNAPP, JOSEPH G., Improving Farm Efficiency through Cooperative Purchasing, the *Journal of Business* of the University of Chicago, vol. 9, no. 4, pp. 311-312, October, 1936.

cause members to increase their production; increased production begets lower prices and lower net returns; therefore, successful cooperatives tend to perpetuate and cause low prices to re-occur in agriculture. Nothing is gained, therefore, from cooperating." Critically appraise this viewpoint.

6. Is this statement tenable, "Cooperatives succeed best when the members have only a small amount of education, *i.e.*, the equivalent of a sixth grade education, but are almost certain to fail if the membership is highly educated (college graduates)? Education develops individualism and self-reliance while a lack of education engenders dependence upon others and collective action."

7. What do various writers mean when they speak of a cooperative commonwealth? Do you anticipate such a development in the United States?

8. Some writers on "consumer cooperation" believe that the agencies of distribution starting from the local plant handling farm products in the country market to the retail store in urban centers should be owned and operated by "consumers," while other writers believe that agricultural producers should own and operate the distribution machinery for their products, meeting the consumers' associations in the wholesale or retail markets. With which of these views do you agree? If not with either, what is your opinion of the scope of organization by consumers and producers?

9. Is the future of cooperation more secure with governmental paternalism or without it?

10. What do you think will influence the future of cooperative marketing in America and in what way will the movement develop?

## APPENDIX A

### CAPPER-VOLSTEAD ACT

#### AN ACT TO AUTHORIZE ASSOCIATION OF PRODUCERS OF AGRICULTURAL PRODUCTS

*Be it enacted by the Senate and House of Representatives of the United States of America in Congress assembled,* That persons engaged in the production of agricultural products as farmers, planters, ranchmen, dairymen, nut or fruit growers may act together in associations, corporate or otherwise, with or without capital stock, in collectively processing, preparing for market, handling, and marketing in interstate and foreign commerce, such products of persons so engaged. Such associations may have marketing agencies in common; and such associations and their members may make the necessary contracts and agreements to effect such purposes: *Provided, however,* That such associations are operated for the mutual benefit of the members thereof, as such producers, and conform to one or both of the following requirements:

First. That no member of the association is allowed more than one vote because of the amount of stock or membership capital he may own therein, or,

Second. That the association does not pay dividends on stock or membership capital in excess of 8 per centum per annum.

And in any case to the following:

Third. That the association shall not deal in the products of nonmembers to an amount greater in value than such as are handled by it for members.

Sec. 2. That if the Secretary of Agriculture shall have reason to believe that any such association monopolizes or restrains trade in interstate or foreign commerce to such an extent that the price of any agricultural product is unduly enhanced by reason thereof, he shall serve upon such association a complaint stating his charge in that respect, to which complaint shall be attached, or contained therein, a notice of hearing, specifying a day and place not less than thirty days after the service thereof, requiring the association to show cause why an order should not be made directing it to cease and desist from monopolization or restraint of trade. An association so complained of may at the time and place so fixed show cause why such order should not be entered. The evidence given on such a hearing shall be taken under such rules and regulations as the Secretary of Agriculture may prescribe, reduced to writing, and made a part of the record therein. If upon such hearing the Secretary of Agriculture shall be of the opinion that such association monopolizes or restrains trade in interstate or foreign commerce to such an extent that the price of any agricultural product is unduly enhanced thereby, he shall issue and cause to be served upon the

association an order reciting the facts found by him, directing such association to cease and desist from monopolization or restraint of trade. On the request of such association or if such association fails or neglects for thirty days to obey such order, the Secretary of Agriculture shall file in the district court in the judicial district in which such association has its principal place of business a certified copy of the order and of all the records in the proceeding, together with a petition asking that the order be enforced, and shall give notice to the Attorney General and to said association of such filing. Such district court shall thereupon have jurisdiction to enter a decree affirming, modifying, or setting aside said order, or enter such other decree as the court may deem equitable, and may make rules as to pleadings and proceedings to be had in considering such order. The place of trial may, for cause or by consent of parties, be changed as in other causes.

The facts found by the Secretary of Agriculture and recited or set forth in said order shall be prima facie evidence of such facts, but either party may adduce additional evidence. The Department of Justice shall have charge of the enforcement of such order. After the order is so filed in such district court and while pending for review therein the court may issue a temporary writ of injunction forbidding such association from violating such order or any part thereof. The court may, upon conclusion of its hearing, enforce its decree by a permanent injunction or other appropriate remedy. Service of such complaint and of all notices may be made upon such association by service upon any officer or agent thereof engaged in carrying on its business, or on any attorney authorized to appear in such proceeding for such association, and such service shall be binding upon such association, the officers, and members thereof.

Approved, February 18, 1922.

## APPENDIX B

### POTATO CO-OPERATIVE GROWER'S CONTRACT

#### PARTIES TO CONTRACT

This Memorandum of a stock subscription and agreement to buy or agency contract made in duplicate and entered into on the date of this instrument by and between the POTATO CO-OPERATIVE, a co-operative association of \_\_\_\_\_, Wisconsin, organized and existing under Chapter 185 of the Wisconsin Statutes of 1933 and the acts amendatory thereof and supplementary thereto, which co-operative shall hereinafter be referred to as the "Association" and \_\_\_\_\_, a resident of the (Town) (City) of \_\_\_\_\_ in the County of \_\_\_\_\_, and State of Wisconsin, who shall hereinafter be referred to as the "Grower"; Witnesseth That:

#### CONSIDERATION

(1) For and in consideration of the mutual benefits to both parties, the promises of each being the consideration of the promises of the other, hereby agree as follows, to-wit:

#### SUBSCRIPTION AGREEMENT

The grower hereby subscribes at par for and agrees to take \_\_\_\_\_ shares of stock of the Association, which Association is organized with capital stock of fifteen thousand and no/100 (\$15,000.00) dollars, which is divided into one thousand five hundred (1,500) shares of the par value of ten and no/100 (\$10.00) dollars per share. The grower agrees to accept said stock upon tender of delivery and to pay therefore either in cash or in the following manner; twenty-five (25%) per cent of the par value of said stock in cash upon the signing of this instrument and to make, execute and deliver to the Association his promissory note for the balance of the purchase price of said stock, which promissory note shall be due ninety (90) days from date of this instrument, shall bear interest at the rate of seven (7%) per cent per annum, and shall be payable at the office of the Association. The grower further agrees that upon default occurring in the terms of said promissory note the Association shall have the right to deduct the full amount due and owing under the terms of said promissory note from any and all moneys due, or to become due, from the association to the grower, whether said Association owes money to the grower as principal debtor or agent, until said promissory note, interest and all legitimate charges are paid in full.



### OWNERSHIP OF STOCK CONTROLLED

The Board of Directors of the Association shall have the prior option to buy for the Association the stock of the grower and the right to recall for value the stock of any stockholder subject to the limitations now or hereafter provided by law and subject to the further limitation that the Association upon exercising said option to buy or right to recall shall pay for said stock at its book value or at its par value when the book value is less than the par value. However, said option or right to buy shall be exercised by said Board of Directors within thirty days after it receives written notice from the grower that he is offering his stock for sale, and said option to purchase shall continue in said Association for said thirty-day period of time unless otherwise required by law. No transfer of stock shall be made by the grower contrary to the provisions of this instrument and any attempt to do so shall be void.

### ELIGIBILITY OF MEMBERS

Only people engaged in raising and producing potatoes shall be eligible to hold stock in the Association and any grower who fails to comply with the charter rules, regulations and by-laws of the Association shall in the discretion of the Board of Directors lose his power to vote at meetings of the stockholders and his stock may be recalled as hereinbefore provided. The Board of Directors shall be the sole judges as to whether or not any member has or has not complied with the Articles of Organization, rules and by-laws of the Association with respect to said stockholder's right to vote.

### AGREEMENT TO BUY AND AGENCY CONTRACT

1. The grower agrees that he will sell to or through the Association all marketable potatoes, except those which the grower reserves for seed and his own personal use, but not for sale, produced by or for him throughout the term of this agreement, and all potatoes grown, either by the grower or by any member of his immediate family, on land either owned by or leased to the grower, are intended to be included in this agreement. This contract is intended by the parties to pass an absolute title to all such potatoes, as soon as the same are delivered to the Association's warehouse or loading platform.

2. The grower hereby represents to the Association that he has not heretofore entered into any contract to sell or market any potatoes to be produced by him subsequent to the effective date of this agreement.

### DELIVERY NOTIFICATION

3. The grower agrees that he will notify the Association as soon as the potatoes are harvested of the approximate number of bushels he will have for sale. He further agrees that he will give at least three days' notice in advance of the time when he wishes to market the potatoes and the amount he wishes to sell at that time. He further agrees that after said notice is given he will deliver said potatoes at the time and place and in the manner

directed by the Association and that in the production and handling of said potatoes he will comply with all rules, regulations, requirements and by-laws of the Association, and with all laws applicable thereto. He further agrees that the Association may sort and grade said potatoes as delivered and that the Association's grading and classification shall be conclusive. He further agrees that the Association may pool or mingle potatoes which are of a like grade, kind, type or quality delivered to it under substantially similar conditions.

#### COMMODITY COLLATERAL FOR ASSOCIATION LOANS

4. The grower agrees that the Association is expressly authorized and shall have power to borrow money in its name and on its own account on the potatoes delivered to it, or on any accounts of the sale thereof or any drafts, bills of lading, bills of exchange, notes, acceptances, or any commercial paper held by it, and to pledge in its own name and on its own account drafts, bills of lading, bills of exchange, notes, acceptances or any commercial paper as collateral.

#### CONTRACT ONE OF AGENCY OR PURCHASE AND SALE

5. The Association agrees that it will either buy all the potatoes, on the basis of grade and quality, produced by or for the Grower or will act as the collective marketing agent of the Grower. It is expressly and mutually agreed that the Association may, in its discretion, as from time to time exercised, either purchase the said potatoes from said Grower or may act as his collective marketing agent.

#### METHODS OF MAKING PAYMENTS

6. The parties agree that in the event the Association acts as the marketing agent the price which shall be paid for said potatoes shall be the average price which the Association receives minus a uniform charge on all the potatoes of the same grade, kind, type or quality to substantially cover the expense of operating the Association. Average prices shall be based upon the Association's total receipts from the sale of potatoes of the same grade, kind, type or quality sold in the same period and under substantially similar conditions. The amount of the uniform charge and the elements to be included therein shall be determined by the Board of Directors of the Association and may include a sufficient amount to create such reserves and produce a working capital as the Board of Directors may deem necessary to accord with sound business principles and if working capital is so provided the interest of the grower therein must be accounted for on the books of the Association.

7. It is mutually agreed that in the discretion of the Board of Directors of the Association, the method of paying the purchase price of the potatoes delivered to the Association may be, to advance within a reasonable time after delivery to the Association, an amount to be determined by such Board of Directors, and to pay the remainder, if any, of the purchase price when the potatoes, which are of the same grade, kind, type, or quality of

any one period, to be fixed from time to time by the Board of Directors, are entirely sold; that in its discretion the Board of Directors may order and cause to be made partial payments prior to the final distribution and may defer the final distribution until all the potatoes of the same grade, kind, type or quality of any one period are sold, and until the uniform fixed charges have been fixed and determined for any reasonable period, which the said Board of Directors may designate. The parties hereto agree that the advance payments shall be in as large amounts as are possible in accordance with sound business practices; the parties further expressly agree that any and all payments made by the Association shall be considered as advances until the Board of Directors of the Association, by action duly taken, determines finally the amount to be paid and the amount of uniform charge for such period, as they may determine.

#### REMEDIES FOR BREACH OF CONTRACT

8. The Grower further agrees that in the event he breaches this agreement he will pay to the Association as liquidated damages thirty (30) per cent of the value of the potatoes not delivered by him under the provisions hereof, the value to be determined as of the day the breach occurred, at the place of contemplated original delivery to the Association and the said damages may be deducted from any money due to the Grower from the Association. The value shall be determined by the Association and shall be final and conclusive. The Grower agrees that in the event of a breach or threatened breach by the Grower of any of the provisions of this contract, the Association shall be entitled to an injunction to prevent breach or further breach thereof and shall also be entitled to a decree of specific performance hereof. It is further understood and agreed that a breach or threatened breach of this contract shall be cause for ejection of the Grower from the Association.

#### DURATION OF CONTRACT

9. This agreement is to be binding for a period of five years and shall be considered to be renewed at the expiration thereof for a like period of time unless either party hereto does, within thirty days before the expiration of this agreement, serve on the other party his notice of election to terminate this agreement. The effective date of this contract is the date upon which it is approved and signed by the officers of this Association.

#### MINIMUM VOLUME TO MAKE CONTRACT EFFECTIVE

10. And it is further mutually agreed between the parties hereto that the agreement to buy and agency contract herein contained shall be null and void, as conclusively determined by the Board of Directors of the Association, unless on or before the 15th day of July, 1937, sufficient contracts similar to this agreement have been entered into between the Association and other growers so that said contracts, according to the estimates recorded thereon, shall cover a production of at least three thousand five hundred (3,500) acres of potatoes.

11. It is mutually understood and agreed between the parties hereto that any and all encumbrances placed upon potatoes grown by the grower herein during the tenure of this agreement shall be subordinate to and subject to the terms of this agreement.

FEDERATION OF LOCAL ASSOCIATIONS MADE POSSIBLE

12. It is mutually understood and agreed between the parties hereto that the Association may make agreements with other growers not identical with this agreement but in conformity with Chapter 185 of the Wisconsin Statutes for 1935, and all acts amendatory thereof and supplementary thereto which may be hereafter enacted, but that the grower named herein may in his discretion have this contract amended so as to conform with the provisions of any other contract entered into by the Association with any other grower.

AGREEMENTS ARE SEVERABLE

13. It is further agreed between the parties hereto that the stock subscription agreement and agreement to buy and agency contract are severable and that if either is in any way invalid such invalidity shall not affect the other agreement.

Also it is further agreed that each of the several provisions of each of said agreements is hereby understood and declared to be severable and that if any one or more of such provisions shall be adjudged to be invalid such invalidity shall not effect the validity of the other provisions or either of them.

14. The parties agree that there are no oral or other conditions, promises, covenants, representations or inducements in addition to or at variance with any of the terms hereof; and that this agreement represents the voluntary and clear understanding of both parties fully and completely.

SIGNATURES

Read and considered, and signed at \_\_\_\_\_ this \_\_\_\_\_ day of \_\_\_\_\_ 193\_\_\_\_\_

Grower

Accepted this \_\_\_\_\_ day of \_\_\_\_\_ 193\_\_\_\_\_

POTATO CO-OPERATIVE.

Solicited by

By \_\_\_\_\_ President

Secretary

I planted \_\_\_\_\_ acres of potatoes in 1936 and I expect to plant \_\_\_\_\_ acres of potatoes in 1937.

Grower

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