

CO-OPERATIVE
PURCHASING OF
FARM SUPPLIES .

By

Joseph G. Knapp & John H. Lister

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and
John H. Lister

FARM CREDIT ADMINISTRATION
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The research, service, and educational staff conducts research studies and service activities relating to problems of management, organization, policies, merchandising, sales, costs, competition, and membership, arising in connection with the cooperative marketing of agricultural products and the cooperative purchase of farm supplies and services; publishes the results of such studies; confers and advises with officials of farmers' cooperative associations; and cooperates with educational agencies, cooperative associations and others in the dissemination of information relating to cooperative principles and practices.

Copies of this publication may be obtained upon request from the

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Farm Credit Administration,
Washington, D. C.

COOPERATIVE PURCHASING OF FARM SUPPLIES

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Cooperative Purchasing of Farm Supplies¹

COOPERATIVE purchasing by farmers is not a new development in the United States where farmers have traditionally aided each other in agricultural activities. The simple partnership of two neighbors to buy a bull or a seeder may serve as an illustration of the early aspects of cooperative purchasing. As agriculture has grown more complex and commercial, the manner in which farmers have joined together for their mutual interests in production has changed. Early informal partnerships have given way to incorporated associations. Instead of a few neighboring farmers joining together to buy a car of feed, seed, or fertilizer, there are now associations which bring thousands of farmers into one farmer-controlled buying unit, enabling them to obtain the supplies and services which they need with assurance of quality and saving in cost.

Cooperation in agriculture in the United States has two major aspects—(1) selling agricultural products, and (2) purchasing the supplies and services needed in agricultural production and marketing. While many Government bulletins have been devoted to cooperative marketing, there is no comprehensive publication of the Federal Government devoted to the cooperative purchasing of farm supplies² even though this form of cooperation is fully recognized in Federal and State laws. This bulletin is designed to provide information on this important phase of agricultural cooperation in the United States.

AIMS AND PRINCIPLES

FARMERS are essentially manufacturers, and, like other manufacturers, are concerned with keeping down costs of production. The major costs of farmers other than for land, buildings, and labor, are for such basic materials of production as seed, feed, fertilizer, insecticides, oil and gasoline, farm machinery, and package materials. The more value the farmer receives for each dollar invested in such supplies the lower is his cost of production. It is, therefore, the aim

¹ It is desired to acknowledge here the generous assistance of leaders and students of the cooperative purchasing movement in the preparation of this bulletin.

Members of the Legal Division, Farm Credit Administration, have provided material assistance, particularly in the preparation of the section on the legal basis of farmers' cooperative purchasing associations.

² A pioneer study of the subject was made, however, as early as 1916 by C. E. Bassett of the Office of Markets and Rural Organization, U. S. Dept. of Agriculture (3).

of farmers participating in cooperative purchasing associations to obtain their basic supplies economically through their own agencies designed for this purpose. This objective is well supported in the following statement by Russell (39, p. 52)³:

We must bear in mind, what is too often forgotten, that farmers are manufacturers, and as such are entitled to buy the raw materials for their industry at wholesale prices. Every other kind of manufacturer in the world gets trade terms when he buys. * * * The farmer, who is as much a manufacturer as the shipbuilder or the factory proprietor, is as much entitled to trade terms when he buys the raw materials for his industry. His seeds, fertilizers, ploughs, implements, cake, feeding stuffs are the raw materials of his industry, which he uses to produce wheat, beef, mutton, pork, or whatever else. * * * Is it any wonder that agriculture decays in countries where the farmers are expected to buy at retail prices and sell at wholesale prices?

COST OF SUPPLIES A FARM PROBLEM

The extent of farmers' expenditures in production is often overlooked. In 1933 the feed, seed, and fertilizer bill in the United States was estimated by the Bureau of Agricultural Economics of the United States Department of Agriculture at \$486,000,000. The cost of containers, spray material, and twine amounted to \$92,000,000, and the cost of operating tractors, farm automobiles, and trucks was \$380,000,000. Other nonclassified farm expenditures were estimated at \$196,000,000. In addition, farmers had in 1933 capital expenditures of \$309,000,000 represented by the cost of machinery, tractors, autos, trucks, repairs, etc. While this expenditure cannot be considered a direct operating expense for 1933, since such capital goods are consumed over a period of years, similar capital expenditures for essential farm supplies occur annually. Thus the combined outlay of farmers for productive purposes in 1933 amounted to \$1,463,000,000.

Table 1 shows principal items of farmers' operating expenditures for the 2 years, 1926 and 1933, and the average of such expenditures for the 8-year period, 1926-33. This average, amounting to \$2,474,000,000, no doubt, affords a more accurate indication of general agricultural expenditures than the expenditures for the depression year 1933.

³ Italicized numbers in parentheses refer to *Literature Cited*, p. 74.

TABLE 1.—ESTIMATES OF OPERATING EXPENDITURES FOR AGRICULTURAL PRODUCTION ¹

Item	1926	1933	8-year average 1926-1933
	<i>Million dollars</i>	<i>Million dollars</i>	<i>Million dollars</i>
Feed, seed, and fertilizer	1,068	483	913
Containers, spray materials, and twine	146	92	126
Cost of operating tractors, automobiles, and trucks	417	380	429
Unclassified	291	196	227
Total current expenditures	1,947	1,154	1,707
Machinery, tractors, and repairs	409	96	328
Automobiles and trucks	262	108	227
Repairs on farm	282	105	210
Total capital expenditures	953	309	767
Total operating expenditures	2,900	1,463	2,474

¹ Data from Bureau of Agricultural Economics, U. S. Department of Agriculture.

For the 8-year period 1926-33, the combined operating expenditures of farmers amounted to 31 percent of their total cash income. This indicates that the cost of farm supplies is of great significance to farmers. If the average income of the farmer were as great as the average income of individuals in other industrial groups, the cost of supplies would be relatively less important. Since the average farm income is very small, however, a modest saving in the cost of farm supplies may be of great importance to the farmer. In a study made recently by the Institute of Economics of the Brookings Institution, "the average income of the farm families [in 1929] was \$1,240, as compared with \$3,226 for town and urban families. These wide differences are, of course, explained in considerable part by the weighting effect of the numerous high incomes among the city groups; but the disparity appears great even when this factor is eliminated." The study also indicated that 50 percent of the farm families had incomes of \$910 or under. Since total agricultural cash income declined from \$10,417,000,000 in 1929 to \$5,262,000,000 in 1933, the average cash income of farmers in 1933 was much smaller than the figure given above for 1929 (*25, p. 59*).

EXTENT OF COOPERATIVE PURCHASING OF FARM SUPPLIES

According to the Fifteenth Census of the United States (43), farmers purchased cooperatively in 1929 supplies valued at \$125,048,597. Cooperative purchasing was used by 410,914 farms or 6.5 percent of all census-reported farms. The average amount purchased cooperatively was \$304. The expansion of cooperative purchasing in the 5-year period from 1924 to 1929 is readily seen, for in 1924 the

value of supplies purchased cooperatively amounted to \$75,971,165. At that time, according to the Census, 362,745 farms, or 5.7 percent of all farms, reported cooperative purchasing of supplies, and the average amount purchased cooperatively was \$209.

A wide variation in the extent of cooperative purchasing by States is indicated in table 2, based on census data. States having the larger amounts of cooperative purchasing were, in the order of their importance, California, New York, Washington, Iowa, Missouri, Minnesota, Ohio, Michigan, Wisconsin, and Kansas. In each of these States the value of supplies purchased cooperatively during 1929, exceeded \$5,000,000. The total value of supplies purchased cooperatively in these 10 States was \$77,314,105, or 61.8 percent of the value of supplies purchased cooperatively in the United States. The wider spread of cooperative purchasing within States, as indicated by the percentage of all farms reporting cooperative purchasing, occurred in Minnesota, Michigan, Washington, Iowa, North Dakota, Wisconsin, South Dakota, New York, Missouri, and Ohio. In all of these States more than 12 percent of the farms purchased cooperatively. The larger amounts purchased cooperatively per farm reporting, were found in Connecticut, South Carolina, Rhode Island, Florida, California, New Jersey, Massachusetts, Washington, Delaware, and New Hampshire. The table indicates much variation in the character of the cooperative purchasing movement in different States. This is, apparently, on account of the nature of farm operations, and differences in farmers' experience and aptitude in cooperative endeavor.

Reports from cooperative purchasing associations, in the files of the Cooperative Division, indicate that there has been a steady increase in the annual quantity of farm supplies purchased cooperatively since 1929. The value represented by such business has not shown a similar increase, because prices have declined greatly since 1929.⁴ The Cooperative Division has tentatively estimated that farmers' cooperative purchasing associations did a business of more than \$250,000,000 in 1934. This figure includes the amount of cooperative purchasing done as a joint activity by cooperative marketing associations (see p. 21). It is difficult to compare this estimate with the above census figure of \$125,048,597 for 1929, since the figures of the Cooperative Division represent some duplica-

⁴ According to the Bureau of Agricultural Economics, the index of prices paid by farmers for commodities bought in 1933 averaged 71 percent of the level of prices for similar commodities in 1929. The index for 1934 averaged approximately 80 percent of the 1929 level of prices.

COOPERATIVE PURCHASING OF FARM SUPPLIES

TABLE 2.—COOPERATIVE PURCHASING OF FARM SUPPLIES, BY STATES, 1929¹

State	Value of sup- plies pur- chased co- operatively	Percentage of farms report- ing coopera- tive pur- chases	Average value of sup- plies pur- chased coop- eratively per farm re- porting
	<i>Dollars</i>	<i>Percent</i>	<i>Dollars</i>
California	14, 812, 161	11. 0	962
New York	11, 407, 972	12. 5	872
Washington	9, 005, 416	16. 8	758
Iowa	7, 462, 349	18. 4	325
Missouri	6, 506, 159	12. 5	203
Minnesota	6, 414, 232	21. 4	163
Ohio	6, 167, 597	12. 2	231
Michigan	5, 797, 257	17. 0	202
Wisconsin	5, 184, 350	13. 4	314
Kansas	5, 046, 612	10. 8	282
Nebraska	4, 441, 475	11. 7	294
Illinois	3, 826, 054	7. 9	227
Pennsylvania	3, 677, 293	5. 2	408
Indiana	3, 463, 461	10. 3	185
Massachusetts	2, 544, 891	11. 3	880
Connecticut	2, 631, 429	11. 1	1, 329
South Dakota	2, 079, 436	13. 4	186
Florida	1, 628, 597	2. 8	1, 112
New Jersey	1, 785, 290	7. 5	940
North Dakota	1, 622, 265	14. 2	146
Vermont	1, 512, 633	10. 6	575
Virginia	1, 474, 475	2. 3	374
Oregon	1, 445, 269	8. 2	321
Louisiana	1, 825, 996	4. 3	197
Alabama	1, 360, 428	3. 0	177
Texas	1, 207, 582	. 7	326
Maryland	1, 178, 464	7. 8	348
New Hampshire	1, 113, 317	11. 0	676
Utah	979, 754	8. 4	429
Oklahoma	950, 004	2. 6	180
Maine	926, 176	4. 3	554
Montana	821, 793	6. 4	271
Colorado	804, 378	5. 6	241
South Carolina	718, 361	. 4	1, 204
Mississippi	607, 900	1. 3	123
North Carolina	483, 033	. 8	224
Idaho	447, 462	8. 2	306
Georgia	399, 968	. 7	282
West Virginia	389, 264	2. 7	172
Tennessee	382, 188	1. 2	133
Arkansas	358, 232	1. 0	142
Kentucky	375, 814	. 5	319
Wyoming	218, 113	3. 6	375
Rhode Island	171, 679	4. 5	1, 160
New Mexico	170, 487	1. 8	300
Delaware	138, 492	1. 9	745
Arizona	94, 937	1. 3	523
Nevada	86, 104	3. 9	267
Total	128, 048, 897	6. 3	304

¹ Adapted from the Fifteenth Census of the United States (43, pp. 686-687).

tion of wholesale and retail values. There has been a continuous increase in the number of purchasing associations reporting and a significant increase in the volume of business of associations which have reported for a number of years.

MAJOR OBJECTIVES—ECONOMY, SERVICE, AND QUALITY

The cooperative purchasing form of business organization provides a method by which farmers attempt through collective purchase to reduce costs of basic supplies. By setting up their own purchasing organizations, farmers are generally able to obtain trade discounts and other price considerations that are customarily granted only to retail agencies. Carrying the method still further and combining the purchases of local associations through the establishment of cooperative wholesale associations, it is possible for farmers to effect additional saving by obtaining basic supplies direct from manufacturers or primary producers for processing in cooperative plants. Some of the large-scale purchasing associations engage in extensive manufacturing operations.

Cooperative farm supply associations are interested in enabling farmers to purchase supplies at the lowest possible price. Prices paid by farmers too often must cover inefficiency in distribution. Many existing agencies handle an insufficient volume of business for efficient operation. Costs are often unnecessarily high because of competitive sales expense; carrying charges on unneeded, unstandardized, or slow-moving merchandise; excessive delivery service; poor credit and collection policies, and inadequate bookkeeping. A well-managed cooperative purchasing association may eliminate or reduce many of these costs and bring competitive pressure to bear on prices. A recent study made by the Pennsylvania State College (40, p. 9) of six cooperative purchasing associations in Pennsylvania indicates that 92 percent of the members and 50 percent of the nonmember patrons were of the opinion that the cooperative associations had lowered the prices generally paid for farm supplies in the counties served.

With respect to the efficiency of farmers' cooperative purchasing associations, a recent study of feed stores in New York State (34, p. 79) is of interest. In comparing cooperative associations with privately operated concerns it was stated that—

* * * the cooperatives had lower gross margins than did the privately owned stores and also a larger sales volume. * * *. The cooperatives had lower figures for every item of cost except for power in the case of the stores offering grinding service, and for bad debts in the case of the merchandising stores. * * *. This remarkable reduction of costs accomplished by the cooperatives was attained by means of efficiency in every direction.

Cooperative purchasing associations endeavor to provide a type of service especially adapted to farmers' needs. The customary retail and wholesale agency is concerned foremost with making a profit and any service which does not tend to develop a more or less immediate profit is likely to be neglected. On the other hand, the aim of the farmers' cooperative purchasing associations, while concerned with saving as much as possible for patrons, is to give detailed attention to the provision of supplies and services which will result in profitable farm operation.

As an example of the cooperative attitude, the case of a large wholesale and retail cooperative which handles feed, seed, and fertilizer may be cited. This association has been advocating use of a particular type of seed in order to produce a forage crop which will make possible an increase in livestock that will subsequently enable farmers to cut down their fertilizer bill. A noncooperative concern handling both of these commodities might well hesitate to do anything that would curtail a profitable line of business; while a cooperative, which exists only to serve its members, thinks first of the farmer's interests. Nourse (29, p. 579) has pointed out that—

insofar as the cooperative * * * represents the voluntary assembling of orders by the consuming group or the guidance of the process of market distribution and, back of that, of production itself according to the needs of the consumer, it proposes a quite distinctive and vigorous attack on the problem of economic efficiency and social economy.

Some of the service customarily provided farmers cannot be justified in the light of critical economic analysis. Credit, for illustration, is often so freely extended that many submarginal producers are kept afloat at the expense of other producers. In some cases the promiscuous extension of credit has resulted in serious overproduction of crops. While it is not contended that the use of credit is unwarranted in the production of a crop, it is clear that credit should not be uneconomically given as a competitive device to obtain sales. In the same way many of the advertising and selling services provided are unwarranted expense from the standpoint of the farmer. He should not be forced to pay an excessive amount for costs involved in making him buy. The following quotation from Perregeaux (33) indicates that such conditions were responsible for the development of cooperative farm supply buying in New York and New England shortly after the World War.

The dairy ration business was booming and the number of proprietary rations being compounded increased materially.

* * * Thus the farmer was faced with an increasingly complex problem of the choice and selection of the proper dairy feeds for greatest profit. * * * The highly competitive

situation engendered by this development led to an overextension of credit and other service facilities, thus increasing the cost of distribution. Furthermore, the farmer who was not using these facilities was forced to share in their cost.

Leading cooperative purchasing associations, notably the Eastern States Farmers Exchange and the Cooperative Grange League Federation Exchange, Inc. (the G. L. F.) have endeavored to provide farmers with the kind of supplies they require without excessive advertising, "high-pressure" selling methods, overextension of credit, unnecessary delivery, and similar practices which tend to increase farmers' costs unduly. In addition, these cooperatives have provided services which could not be obtained from established dealers. For example, farmers have desired to know the formulas of feed and fertilizer mixtures, which were long considered to be trade secrets. Farmers have also demanded more complete information on the source and viability of seeds. Cooperative purchasing associations, in meeting these demands, have pioneered in providing a service which may be called "dependability."

The viewpoint of one of the largest cooperative seed-purchasing services has been expressed as follows (6, p. 6):

Cooperative seed purchasing seeks the genetic history of seed for dependable inheritance and selects seed from desirable regions of seed production to assure its adaptation. Its seed refinement, vitality, and seed treatment must serve the best interest of the farmer. * * * [The association] has overcome the inertia and indifference of individuals concerning the use of inoculents with legume seeds by supplying suitable bacteria cultures with all legume seeds purchased. Likewise, all seeds which may carry disease or be handicapped by the attack of unfavorable soil-borne organisms are subjected to the necessary treatments for the control of seed or soil-borne diseases. * * * The cooperative challenge is to deliver, over a long period, consistently better and more dependable "consumer values" in seeds than are available through the ordinary channels of trade. In the purchase of questionable seed, the farmer risks all—his use of land and buildings, labor and time in season, machinery and horsepower, fertilizer, and spray material. He jeopardizes his future returns in feeding, marketing, and soil improvement.

So far this discussion has developed the fact that agricultural cooperative purchasing associations serve to reduce the farmers' essential costs of production and at the same time give him a type of service not generally obtainable from other agencies. It has been stated that cooperative farm-supply associations endeavor to provide supplies of a dependable high quality. To many leaders the achievement of this aim has been their outstanding accomplishment. For

illustration, the manager of a prominent purchasing cooperative has said (1):

I can say with no fear of contradiction that the Exchange has succeeded in its primary objective, that of making available the kind and quality of feed, seeds, and fertilizer that the farmers want and which are not available through established channels.

Without question, quality and economy cannot be disassociated as objectives in cooperative purchasing. A poor-quality product, no matter how cheap in price, is fundamentally expensive. A cooperative purchasing association, which attempted to make savings at the expense of quality, would soon find itself with few patrons. Quality and economy are simply two manifestations of the same purpose. It would be as absurd to measure the efficiency of the purchasing department of a great corporation solely by the price paid for supplies as to measure that of a cooperative purchasing association by prices paid without regard to values received for each dollar expended.

DEVELOPMENT OF COOPERATIVE PURCHASING BY FARMERS IN THE UNITED STATES

IT IS DIFFICULT to indicate a definite beginning for the agricultural cooperative purchasing movement in the United States. Since colonial times farmers have joined together to procure necessary supplies at reasonable cost. The great improvement in agricultural technique and the expanding market for agricultural products about the middle of the last century, resulting in a more commercialized agriculture and greater use of manufactured supplies, intensified this tendency. According to Nourse (30, pp. 30-32) about 1850, numerous farmers' clubs were organized in Illinois, and in 1858 a convention of Illinois farmers recommended "the formation of farmers' clubs wherever practicable, the object of which should be to produce concert of action on all matters connected with their interest", and "the formation of wholesale purchasing and selling agencies in the great centers of commerce, so that producers may in a great measure have it in their power to save the profits of retailers." The Civil War dissipated the momentum of this development, which merged into the Granger movement.

EARLY GRANGE EFFORTS

When the National Grange of the Patrons of Husbandry was established shortly after the Civil War, its first emphasis was upon social, fraternal, and intellectual benefits. After a few years, however, local granges became interested in plans for cooperative buying and selling. The first efforts in this direction were based on the idea

that farmers could club their buying power and get price concessions in return for their combined cash trade. This type of cooperative action resulted in the establishment of local, county, and to some extent, State agencies for pooling buying power. Buck has declared (4, p. 241) that "the aggregate business done by or through these local agencies throughout the country was certainly enormous during the years 1873, 1874, and 1875, and they no doubt effected very considerable savings for the members." The competitive pressure of the Grange agencies also tended to bring about a general reduction in prices paid by farmers.

By December 1874 there were 26 State Grange agency systems. However, the Grange agency plan was gradually replaced in popularity by the Rochdale principles of cooperative organization (14, p. 87) which have been stated as follows:

1. To sell goods at prevailing local prices.
2. Restriction to a fixed rate of the interest upon capital—this interest to have first claim upon the profits.
3. The distribution of profits (after meeting expenses and interest charges) in proportion to purchases.
4. No credit—all purchases and sales to be paid for in cash when the goods were handed over.
5. Both sexes to have equality in membership rights.
6. Each member to have one vote and no more.
7. Regular and frequent meetings to be held for the discussion of the society's business and for receiving suggestions for improving the society's welfare.
8. Accounts to be properly kept and audited; and balance sheets to be regularly presented to the members.

The executive committee of the National Grange recognized these principles in 1875 by establishing a system of rules for the regulation of cooperative associations within the order. The rules were prefaced by the following advice to members (27, pp. 94-100):

1. All cooperative associations should become incorporated.
2. Care should be taken that all records, accounts, and vouchers are properly kept.
3. Expose dishonesty and punish fraud.
4. Buy as far as practicable from the producer and manufacturer, and sell to the consumer, if possible.
5. Never depart from the principle of buying and selling for cash.
6. Take account of stock and make settlements quarterly.
7. Neither fear nor court competition.
8. Choose only men of undoubted integrity and ability for your officers, and then give them your confidence.

The rules provided that at least one share of stock of the value of \$5 should be held by each member and should not be transferable except to members. The amount of stock that could be held by one member was limited to 100 shares. Each member was to have one vote only. All business was to be on a cash basis. Interest on capital was limited to 8 percent. This was to be allowed provided that the member's purchases from the association reached a certain minimum during the year. The rules provided that net profits should be divided in proportion to the amount of purchases among those who purchased goods from the association.

When the National Grange met in November 1876 the members had been generally converted to the Rochdale principles of cooperation. Unfortunately for the movement, however, the general lack of success of the exchange systems had tended to alienate members from further cooperative effort. Even though the Rochdale principles were accepted so late that they had little practical influence on the Grange movement, it is significant that many of the Rochdale type associations established by the Grange flourished and gave proof that cooperatives could succeed on a practical basis of operation. Although the Grange may be given credit for inculcating the cooperative principle as a means of agricultural relief, it is true that many of these early ventures were started without careful plans and in too large a way. Buck (4, pp. 241-242) has suggested that the Grange made a serious mistake in not working out a "comprehensive system of cooperation" before the various business agency systems became so well established. Undoubtedly, the proponents of the separate exchange type organizations did much to hamper the development of the more solid cooperative program embraced by the National Grange in 1875. The farmers of that period, however, were demanding quick relief and it is doubtful whether cooperative organizations alone could have quieted agricultural discontent. Furthermore, many of the State laws were unfavorable to the development of true cooperative organizations.

CURRENT GRANGE ACTIVITIES

The relationship of the Grange and the cooperative movement became less direct after 1880, although the Grange has continued to promote cooperative efforts down to the present day. The report of the Grange Committee on Cooperation at the 1933 convention (23, p. 155) stated that—

For 50 years the Grange has led the way in doing the educational work for cooperative organizations and we should at this time emphasize the importance of cooperation in buying and selling. The new credit bank for cooperatives offers a splendid inducement for farmers to cooperate together, thereby giving them advantage in financing. Cooperative associations have con-

tinually been fought by those who for selfish reasons seek their destruction. * * * We must rededicate ourselves to this cause and through cooperation in buying and selling give the farmer a better deal.

At the present time the Grange is actively supporting cooperative purchasing in a number of States. It is the general policy of the Grange, however, that cooperative buying and selling agencies need not be controlled entirely by it. The Grange has generally shown a willingness to work with other farm organizations in promoting cooperative developments. For illustration, the New York State Grange has always given its full support to the Cooperative Grange League Federation Exchange, Inc., which was set up in cooperation with other farm organizations. The North Carolina State Grange, in a similar manner, has recently assisted in the development of the Farmers' Cooperative Exchange, Inc., of North Carolina. In some States, however, the State Granges have engaged in actual cooperative buying operations. The outstanding development of this sort has been in the Northwest, notable in the State of Washington, where there is a heavy Grange membership. The Ohio and Pennsylvania Granges have also enabled their members to obtain special price concessions on various farm supplies.

THE FARMERS ALLIANCE

As the Grange waned in influence, about 1880, the Farmers Alliance movement developed aggressively, particularly in the Southern States (16). The Alliance, however, heedless of Grange experience, was anxious for quick relief through political pressure and was distrustful of conservative methods. Like the Grange, the Alliance promoted cooperative enterprise among farmers. It not only accepted but promoted the system of local and State business agencies and exchanges. In 1889 an association of State business agents was organized, and at the meeting of this association in 1890, 18 State agencies and exchanges were represented. It was reported at this meeting that these agencies did a total annual business of \$10,000,000. The success of the State agencies and exchanges did not meet expectations, however, and the Alliance turned its attention to political remedies for the wide-spread agricultural distress. When the Farmers Alliance became immersed in the Populist movement in 1890, it disintegrated rapidly.

The contribution of the Farmers Alliance to the development of agricultural cooperative purchasing was much less important than that of the Grange. A large number of cooperative ventures, however, obtained impetus from the strengthening effect of the Farmers Alliance movement. The Farmers Alliance, like the Grange,

pointed out some of the difficulties to be overcome in order to develop cooperative business organizations of a permanent type.

In studying the early history of the Grange and the Farmers Alliance movements with reference to cooperative purchasing, it is necessary to realize that the cooperatives sponsored by these farmers' organizations were established at a time of great economic distress. It was difficult for farmers to understand their problems clearly, and they were handicapped by overenthusiasm and lack of experience, leadership, and financial backing. It is not accurate to record these early efforts as cooperative failures, for they were simply experiments which demonstrated that successful cooperative undertakings must be grounded on something more substantial than economic need.

THE FARMERS UNION

The Farmers Educational and Cooperative Union of America, known popularly as the "Farmers Union", originated in 1902 as an outgrowth of the Old Farmers Alliance movement. It grew rapidly in the Southern States, but its strength shifted about 1915 to Kansas, Nebraska, and other Western States. From its inception the Farmers Union has advocated cooperative purchasing of agricultural supplies. In the words of Wiest (*46, p. 500*), "The Farmers Union took up cooperation where the Farmers Alliance dropped it." A leader of the Farmers Union movement stated in 1902 (*2, p. 100*) that the one great aim of the Farmers Union was "to aid each other in buying and selling." During the early years, the business agent system was generally employed, but gradually organizations accepted the Rochdale pattern of cooperation. In 1919 Rochdale principles were definitely recommended (*13, p. 35*) and Farmers Union business enterprises of the present day generally follow them.

The most significant cooperative purchasing developments under Farmers Union auspices have occurred in the States of Nebraska, Kansas, Oklahoma, Iowa, the Dakotas, and Minnesota. (See appendix A.)

In Nebraska there are approximately 100 Farmers Union cooperative stores, 100 Farmers Union cooperative oil associations, and 200 Farmers Union elevators and cream stations which engage in the cooperative purchasing of farm supplies. In addition, there are approximately 50 local farmers unions which handle supplies through secretaries or agents. The Farmers Union State Exchange at Omaha, Nebr., serves as a wholesale agency for the local cooperatives. Its wholesale business, which did not include the volume of retail business handled by its 14 branch stores, amounted to \$1,244,993 in 1933. This figure does not adequately reflect the wholesale value of purchasing business done by Farmers Union agencies in Nebraska,

since many of the local associations buy all or part of their supplies from other wholesale agencies.

The Farmers Union Central Exchange, Inc., of St. Paul, Minn., serves as a wholesale cooperative purchasing agency for 211 local Farmers Union purchasing associations in Minnesota, Wisconsin, the Dakotas, and Montana. The major supplies handled are gasoline, kerosene, distillate, oil, grease, farm machinery and equipment, tires and tubes, flour and feed, and twine. The progress of the Exchange in cooperative purchasing is indicated by the fact that 425 cars of gasoline, kerosene, distillate, and tractor fuel were handled in 1929, while in 1934 the number of cars handled had increased to 3,362. The value of sales in its wholesale department amounted to \$2,615,519 and the net income to \$55,468 for the year ending October 31, 1934. The Farmers Union Central Exchange, Inc., has also operated a number of branch retail stores, but these branch stores are gradually being turned over to the local communities to be operated as independent cooperative units. Within a year or so the Exchange will operate solely as a wholesale cooperative association, which will enable it to center attention on the performance of the wholesale function. It is of interest that the management of the Exchange has reached the conclusion that local cooperative ownership creates more interest on the part of members with consequent increase in volume and greater net savings.

AMERICAN SOCIETY OF EQUITY

The American Society of Equity was organized in 1902 as a general farm protest movement. The most significant development occurred in Wisconsin, where the Wisconsin Society of Equity, which was organized in 1907, sponsored cooperative elevators, creameries, and warehouses. The American Society of Equity has given way to the Farmers Equity Union, with national offices in Greenville, Ill., which was established in 1917 primarily as a business organization. The Farmers Equity Union has encouraged the cooperative purchase of farm supplies through Equity elevators and creameries which are largely situated in the Middle West.

THE FARM BUREAU

The American Farm Bureau Federation was established in 1919 by State Farm Bureau federations which had developed as agencies to promote agricultural extension work. Education in the matter of selling farm crops or purchasing supplies was considered to be a part of the county agent's regular duty and county agents assisted in the actual organization of cooperative associations. County agents could not participate in actual business transactions such as ordering

goods or handling funds. They could, however, aid farmers in their cooperative purchasing and marketing through organizations. This general situation gave real impetus to the organization of the Farm Bureau, which has from its beginning sponsored cooperative purchasing and marketing. One authority (24, p. 110) held that "Here was a definite job for the Farm Bureau separate and distinct from its duties arising out of its relationship to the county agent for demonstration and educational purposes."

Farm bureau developments in cooperative purchasing have been centered usually in those States having strong State Farm Bureau federations. Significant achievements in this direction have occurred in Illinois, Indiana, Ohio, Michigan, and other States in the Middle West and South, where strong State cooperative purchasing associations have been established with Farm Bureau support. (See appendix A.) The Illinois Farm Supply Co., which is illustrative of this development, is discussed on page 20. Moreover, in many other States, cooperative purchasing is carried on by county farm bureaus and affiliated organizations.

In certain instances, the State Farm Bureau purchasing associations have joined together to arrange favorable terms and prices. For illustration, the Farm Bureau Milling Company, Inc., with offices at Columbus, Ohio, serves as a bargaining association for the State Farm Bureau purchasing associations of Indiana, Ohio, Michigan, West Virginia, and Pennsylvania, in the purchase of feed, fertilizer, farm machinery, and twine. The Farm Bureau Milling Co., Inc., acting for the three associations, contracts with manufacturers on a yearly basis. Not only are the State associations able to obtain favorable prices but the contracts in some cases contain provisions whereby the associations participate in the profits of the manufacturer.

In a somewhat similar manner the petroleum products requirements of the above State associations are bargained for through the Farm Bureau Oil Co. which, in turn, is a member of National Cooperatives, Inc. (See p. 20.) Besides acting as a bargaining agent for gasoline and kerosene, and associated products, the Farm Bureau Oil Co. operates an oil-blending plant at Indianapolis, Ind. At this plant are manufactured oils and greases which are sold under Farm Bureau brands to the State purchasing associations.

INDEPENDENT COOPERATIVE PURCHASING ASSOCIATIONS

So far it has been shown how the general farm organizations have sponsored and developed cooperative purchasing. There has also been a continuous growth of cooperative purchasing by farmers independent of general farm organizations, a movement which has been greatly intensified by the depressed condition of agriculture

since the World War. Such cooperative purchasing is found in many forms.

Farmers may simply pool orders for certain items such as feed or fertilizer, and have them shipped to the community on a c. o. d. basis. Local cooperative purchasing associations may be set up which may or may not engage in cooperative marketing. Frequently cooperative

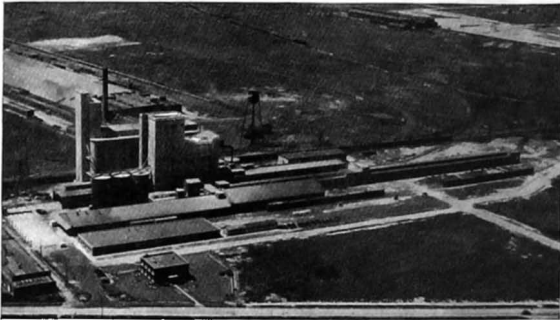


FIGURE 1.—PLANT OF THE EASTERN STATES FARMERS EXCHANGE AT BUFFALO, N. Y.

This mill manufactures approximately 1,200 tons of feed per day. Up to 36 cars can be loaded in a single operation and 3 complete loadings can be made in a 24-hour period. Seed and miscellaneous supplies also are distributed from these facilities.

elevators and creameries, cotton gin and livestock shipping associations carry on cooperative purchasing as a sideline activity. A significant recent development has been the establishment of large-scale cooperative purchasing associations which may serve directly the local purchasing associations or the farmers of one or more States. The Eastern States Farmers Exchange, the Cooperative Grange League Federation Exchange, Inc. (the G. L. F.), and the Southern States Cooperative, Inc. (the S. S. C.), are outstanding examples of this development, which has occurred within the last 15 years.

The Eastern States Farmers Exchange is an example of the centralized type of organization where farmers have direct membership. It was created in 1918 in response to a demand of New England farmers for an organization that would provide high-quality farm supplies at reasonable prices. This organization has had a steady growth, and at present has over 50,000 members (in New England, in Pennsylvania and other Middle Atlantic States) who buy annually through it more than 300,000 tons of feed, fertilizer, and miscellaneous supplies valued at more than \$12,000,000. Supplies are ordered by members through about 1,000 accredited representatives who are usually farmers. There are also numerous warehouses located at

strategic points in the territory where farmers may obtain supplies direct. The Eastern States Farmers Exchange operates a large feed mill in Buffalo, N. Y. (fig. 1), and fertilizer plants in Boston, Mass., and Wilmington, Del., so that the Exchange performs cooperatively all the distributing functions, including the processing of raw material. The Eastern States Farmers Exchange has an equity of more than \$1,500,000 in plants, inventory, and other assets. Patronage dividends amounted to about \$100,000 for the year 1934.

The Cooperative Grange League Federation Exchange, Inc., known as the "G. L. F.," the largest farmers' cooperative purchasing association in the United States, was organized in 1920 to combine the purchasing efforts of the New York State Grange, the New York State Farm Bureau Federation, and the Dairymen's League Cooperative Association, Inc. The first 2 years of operation proved almost disastrous. In 1922, after a deficit of approximately \$150,000 had been incurred, the G. L. F. was placed on a practical business operating basis. Since that time the progress of the organization has been phenomenal. In 1934 the G. L. F. served approximately 100,000 patrons located in New York, northern Pennsylvania, and



FIGURE 2.—MODERN MILL AND ELEVATOR OF THE GRANGE LEAGUE FEDERATION EXCHANGE, INC., AT BUFFALO, N. Y.

This plant has rail, water, and truck connections. The mill has a capacity of 75 cars of mixed feed per day, and the elevator has a grain storage capacity of 750,000 bushels. The largest grain boats on Lake Erie can load or unload here at the rate of 15,000 bushels per hour.

New Jersey, and distributed during the year ending June 30, 1935, feed, seed, fertilizer, and other farm supplies with a wholesale value of \$24,000,000. Its net worth as shown by its published balance sheet of June 30, 1934, amounted to \$4,195,032.

The G. L. F. has several hundred distributive outlets which may be divided into two main groups—(1) G. L. F. stores, and (2) G. L. F. local agents. The G. L. F. stores, of which there are approximately 135, are operated through a management corporation and local advisory boards on what may be described as a "centralized directed system." These stores form the backbone of the association's structure. There are also approximately 500 accredited G. L. F. local dealers, or agents, who handle supplies at agreed-upon resale prices. There are also a number of independent local cooperative associations which handle G. L. F. supplies on the same basis. The G. L. F. early found it necessary to develop its own manufacturing and processing plants for feed, seed, fertilizer, and paint, so that this organization, as the Eastern States Farmers Exchange, provides an integrated purchasing system from the farmer to the sources of raw material (fig. 2).

Another cooperative purchasing association of the regional type is the Southern States Cooperative, Inc. (the S. S. C.), which serves farmers in Virginia, North Carolina, Maryland, and adjoining States. The S. S. C. was started in 1922 as a seed purchasing association for Virginia farmers under the name Virginia Seed Service. It gradually expanded its operations to handle feed and fertilizer and extended its service into adjoining States. In order to better designate its scope as a general wholesale organization serving farmers in a group of southern States, its present name was adopted. The Southern States Cooperative, Inc., employs a system of local distribution very similar to that of the G. L. F. In North Carolina, S. S. C. supplies are handled through the Farmers Cooperative Exchange, Inc., which has its own system of stores, local cooperatives, and agents. The relationship of the S. S. C. and the Farmers Cooperative Exchange, Inc., of North Carolina, is of interest in that the arrangement affords the benefits of large-scale operation while retaining the advantages of State autonomy. The S. S. C. owns and operates cooperatively with the G. L. F. a large feed mill in Baltimore, Md., which is designed to serve the southern part of G. L. F. territory, as well as the territory of the S. S. C. The S. S. C. has a smaller feed plant and fertilizer manufacturing facilities at Norfolk, Va. The volume of business of the Southern States Cooperative, Inc., for the business year 1934-35, amounted to \$5,000,000. The net worth was \$402,782, as shown on its published balance sheet for the year ending November 30, 1934.

COOPERATIVE OIL ASSOCIATIONS

With the increased use of automobiles, trucks, tractors, and gas engines in farming operations, there has been a great expansion in the cooperative purchase of gasoline and oil by farmers (§5). There are now hundreds of associations which distribute oil and gasoline

cooperatively to farmers located throughout the United States, particularly in the Central States and the far West (fig. 3). No complete record of the total quantity purchased cooperatively is available, but a recent unpublished survey by the Cooperative Division, Farm Credit Administration disclosed 644 associations handling petroleum products in the United States, which did an aggregate retail business of \$31,900,000 in 1934. If information were available for all such associations, this figure would be considerably increased.

A number of wholesale purchasing cooperatives have undertaken to serve as a source of supply for the local and county associations which distribute petroleum products. The Illinois Farm Supply Co. supplies member purchasing associations which cover the State of Illinois, while the Farm Bureau Oil Co. serves the State Farm Bureau purchasing associations of Indiana, Ohio, Michigan, and Pennsylvania, which, in turn, supply county associations in these States. Approximately 130 associations in Minnesota and Wisconsin obtain their supplies through the Midland Cooperative Wholesale, Inc., of Minneapolis, Minn., which increased its volume of business approximately \$750,000 during 1934. The Midland Cooperative Wholesale, estab-

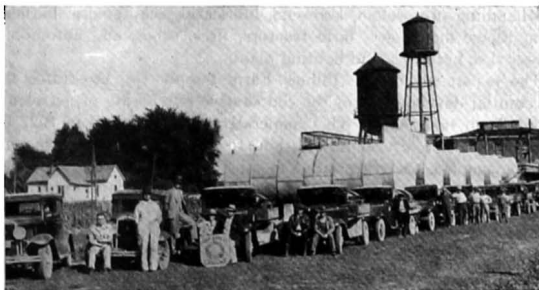


FIGURE 3.—A FARM BUREAU OIL-PURCHASING COOPERATIVE.

Farmers using tractors and other motor-driven equipment obtained in 1934 over \$30,000,000 worth of petroleum products from bulk tanks and trucks operated by cooperative purchasing associations.

lished in 1926 as the Minnesota Co-Op Oil Company, has the distinction of being the first wholesale oil association established in the United States. In North Dakota, Wisconsin, and Minnesota over 200 associations are joined to the Farmers Union Central Exchange, Inc., of St. Paul, Minn. Local associations in Nebraska generally obtain their supplies through the Farmers Union State Exchange. The Consumers Cooperative Association of North Kansas City, Mo. (formerly the Union Oil Co. Cooperative), serves over

250 oil and farm-supply associations operating in Kansas and other western States. In the Pacific Northwest, the Pacific Supply Cooperative serves about 60 local associations in Oregon, Washington, and Idaho, while the Washington State Grange acts as the wholesale agency for its member associations. (See also appendix A.)

A number of these regional wholesale cooperative purchasing associations, which serve approximately 800 local and county oil and gas associations in 20 States in the Middle West and West, formed in 1933 a joint bargaining agency, the National Cooperatives, Inc. At present there are seven affiliated organizations: Consumers Cooperative Association (North Kansas City, Mo.); Farmers Union Central Exchange, Inc. (St. Paul, Minn.); Midland Cooperative Wholesale, Inc. (Minneapolis, Minn.); Central Cooperative Wholesale Co. (Superior, Wis.); Consumers Cooperatives Associated, Inc. (Amarillo, Tex.); Pacific Supply Cooperative (Walla Walla, Wash.); Farm Bureau Oil Co. (Indianapolis, Ind.). Through this organization master contracts are negotiated for all the member regional associations. National Cooperatives, Inc., is authorized to deal in any commodity, but its major activities up to the present have been in the field of petroleum products. It has entered into contracts for the handling of gasoline, kerosene, lubricating oils, grease, harness, farm tillage machinery, farm tractors, tires, tubes, and automobile accessories, batteries, and lighting plants.

The experience of the Illinois Farm Supply Co. illustrates the substantial development of the cooperative purchasing of petroleum products in one State. This cooperative was organized in 1927 by the Illinois Agricultural Association, to act as its cooperative purchasing agency. Starting with 8 member companies, it has expanded until today it comprises a system of 58 member companies operating in 90 counties with approximately 75,000 farmer purchasers. The farmers' capital stock investment is almost \$1,000,000. The 58 companies were operating 427 tank trucks in rural territory on September 1, 1934, and were either operating or supplying 600 retail outlets from 156 bulk storage stations which had a combined storage capacity of more than 6,500,000 gallons. The volume of petroleum products handled for the year ending August 1, 1934, totaled 47,670,378 gallons, consisting of 31,043,729 gallons of gasoline, 10,312,027 gallons of kerosene, 5,006,868 gallons of distillate and other fuels, 1,198,993 gallons of lubricating oil, and 108,761 gallons of grease.

The Illinois Farm Supply Co. handles also a number of miscellaneous items such as tires and tubes, fly spray, paint, chinch bug oil, commercial fertilizer, alcohol, antifreeze radiator solutions, cod-liver oil, stock dips, and mange oil. These miscellaneous items represent but a small part of the total volume of business, which for the fiscal period ending August 31, 1934, totaled \$3,378,833 at wholesale

values. The value of retail sales of the 58 member service companies for this period amounted to over \$6,000,000.

COOPERATIVE PURCHASING BY MARKETING ORGANIZATIONS

In every section of the United States there are farmers' cooperative associations doing both marketing and purchasing. Approximately 6,000 associations which are primarily engaged in marketing, handle farm supplies as a side-line activity. In many instances, the cooperative purchase of farm supplies is of more significant value to the farmer than the cooperative marketing of his crop. The extent of such side-line business amounts to many millions of dollars annually.

Many cooperative marketing associations require supplies such as cans, labels, and package materials in marketing or processing operations. These supplies are here considered farm supplies since they are purchased for farmers through their cooperative agency, and may be as essential to the farmer as those used in primary production.

Cooperative purchasing has developed along with cooperative marketing for several reasons. For example, associations have found it possible to reduce their overhead costs by using the same facilities for assembling and selling crops, and for buying and distributing supplies to the farmer. Furthermore, a farmer delivering crops to be marketed by an association looks upon it as a convenience if he can buy his supplies from the same association. Also, he may not desire to belong to two organizations with the responsibilities of membership in both when one association can perform satisfactorily all the required services.

A number of large-scale cooperative associations of both the federated and centralized types, which were primarily established for marketing purposes, have developed purchasing departments or subsidiary purchasing corporations. For example, the Land O'Lakes Creameries, Inc., of Minneapolis, Minn., which serves a wide area in the Central West, through its feed and creamery machinery and supply departments, did a business of \$2,082,316 in 1934. During 11 years of operation these departments have paid patronage dividends of more than \$1,000,000, and have undoubtedly had an influence on the competitive price situation. In Los Angeles, Calif., the Fruit Growers Supply Co. was organized in 1907 to provide members of the California Fruit Growers Exchange with their own source of package and orchard supplies (fig. 4). In 1934 this company did a supply business of \$7,649,491 and paid patronage dividends amounting to \$546,914.

In the Pacific Northwest, the business of the feed department of the Washington Cooperative Egg and Poultry Association amounted to approximately \$5,000,000 in 1934. The feed department operates 9 mills which also serve as distributing plants, and 17 other distributing warehouses. A fleet of approximately 120 trucks is used to

collect products to be marketed and to make deliveries of feed for members. The net earnings of the feed department have averaged, recently, approximately \$500,000 per year. These illustrations indicate that cooperative purchasing and cooperative marketing are of mutual importance in developing a cooperative structure that will adequately serve farmers.

WORK OF THE NATIONAL COOPERATIVE COUNCIL

A large number of farmers' cooperative marketing and purchasing associations are joined together in the National Cooperative Council, a conference body through which agricultural cooperatives formulate



FIGURE 4.—LUMBER YARD OF THE FRUIT GROWERS SUPPLY CO., SUSANSVILLE, CALIF.

This 50,000,000 feet of lumber represents approximately one-third of the annual box shock requirements of members of this association.

their policies on national matters.⁵ The Council does not engage in any business operations, but provides a mechanism for determining general policies on matters affecting the agricultural cooperative movement. It maintains an office in Washington, D C., where it represents cooperatives in matters relating to business practices, taxation, transportation, and tariffs (26). It publishes bimonthly the *Cooperative Journal*, which reports current developments and carries articles on cooperative marketing and purchasing. The Council performs other educational services through radio, press releases, and memoranda.

The National Cooperative Council has a purchasing division which is made up of the following associations: Cooperative Grange League Federation Exchange, Inc., Ithaca, N. Y.; Eastern States Farmers Exchange, Springfield, Mass.; Farm Bureau Services, Inc., Lansing, Mich.; The Farmers Cooperative Exchange, Inc., Raleigh, N. C.; Fruit Growers Supply Co., Los Angeles, Calif.; Indiana Farm Bureau

⁵ A number of large-scale agricultural cooperative purchasing associations are also members of the Cooperative League of the U. S. A., New York City, which is a general educational and promotional organization for the consumers' cooperative movement.

Cooperative Association, Inc., Indianapolis, Ind.; Mississippi Federated Cooperatives (A. A. L.), Jackson, Miss.; Ohio Farm Bureau Service Co., Columbus, Ohio; Producers Cooperative Exchange, Inc., Atlanta, Ga.; Southern States Cooperative, Inc., Richmond, Va.; Consumers Cooperative Association, North Kansas City, Mo.; and Cooperative Farm Services, Inc., Clarksburg, W. Va. In addition, many of the cooperative marketing associations affiliated with the Council provide cooperative purchasing service.

There are a number of State cooperative councils or similar State conference bodies which perform activities similar to those described above, within State lines. These State councils are usually affiliated with the National Cooperative Council.

In the foregoing discussion an endeavor has been made to show the influence of the many agencies which have contributed over a period of 70 years to the development of cooperative purchasing in the United States. All of the national farm organizations have played an important role in sponsoring the cooperative purchase of farm supplies. Purchasing associations have also developed independently and in conjunction with cooperative marketing associations. Reference should be made also to the assistance given farmers in the formation and management of cooperative associations, by the research and extension staffs of the State agricultural colleges and the United States Department of Agriculture, the State departments of agriculture and markets, and the Cooperative Division of the Farm Credit Administration. The cooperative supply buying movement is now established on a firm footing as an integral part of agricultural cooperation.

LEGAL BASIS OF FARMERS' COOPERATIVE PURCHASING ASSOCIATIONS⁶

WHETHER farmers or any other group of persons may join together to form cooperative purchasing associations; how they may be organized and controlled; how they may conduct their business; what rights they may enjoy, are all questions determined either directly or indirectly by the law of the State in which the association is formed, and the law of the State in which the association operates, and, to a certain extent, by Federal statutes.

Thus, a State may, if it so desires, refuse to permit cooperative associations to be organized under conditions different from those permitted ordinary corporations. Or it may, on the other hand, within constitutional limits, permit cooperative associations to organize and carry on their business with greater latitude than is allowed ordinary corporations. In so far as cooperative associations conduct

⁶ More detailed information relating to the legal basis of farmers' cooperative purchasing associations has been given by Hulbert, in a bulletin of the U. S. Department of Agriculture (#1), and in his address before the American Institute of Cooperation, 1932, Ithaca, N. Y.

any part of their business, either in buying supplies or in selling them, within more than one State, they are engaging in interstate commerce and are, therefore, to that extent at least, subject to regulation by the Federal Government. The Federal Government, under its authority to impose income taxes, may determine whether or not and to what extent the income of such associations is subject to taxation (*Flint v. Stone Tracy Co.*, 220 U. S. 107, 173; *Brushaber v. Union P. R. R. Co.*, 240 U. S. 1, 21).

Practically all States have long had statutes permitting persons, subject to certain conditions, to form and operate business corporations. The purpose of such corporations generally has been the conducting of an enterprise for profit. As a rule, the kind of business done has had no relation to the private business of most of the members. The control by investors of the affairs of the corporation and the distribution of its profits have been determined on the basis of the relative units of capital invested.

Fundamentally, the purpose of farmers in forming cooperative associations has not been to realize a profit on money invested. It has been rather to achieve an efficient way of marketing their products or of obtaining supplies and services needed in their farming operations. In the latter case the objective is to enable each member to obtain supplies as nearly as practicable at cost plus handling charges. When initial capital is required, usually the rate of interest to be paid is restricted. In many instances the members of the association vote on the basis of one man, one vote, and generally a large percentage of the business must be with members. In most other respects, however, a cooperative purchasing association usually resembles an ordinary business corporation. It comes into existence upon obtaining a charter from the State. It adopts bylaws for the conduct of its affairs. Its members hold meetings and elect a board of directors to guide and direct its business. In noncooperative aspects, cooperative purchasing associations are subject to the same laws as other business corporations except as modified by statutory provisions.

Until the last quarter of the nineteenth century there were practically no special cooperative statutes. Farmers joined together for cooperative purposes either informally or under the existing corporation laws. Following the ninth annual meeting of the National Grange, in 1875, at which a committee report (27, p. 94) stressed the importance of cooperation, State legislatures began to enact special cooperative statutes. Today virtually every State in the Union has a statute authorizing the formation of agricultural purchasing as well as agricultural marketing associations. (Some of these acts authorize the incorporation of cooperatives which are not limited to agricultural producers.) Although the provisions of these statutes

may differ as to the extent of power conferred upon cooperative associations, they generally authorize or permit, either expressly or by implication, the Rochdale principles of cooperation. (See p. 10.)

The inherent right of States to enact statutes providing for the formation by farmers of cooperative associations in accordance with cooperative principles has been established by both the highest State courts and the United States Supreme Court. In a case involving the power of the States to enact such statutes, the United States Supreme Court stated that cooperative marketing statutes "promote the common interest" (*Liberty Warehouse Company v. Burley Tobacco Growers' Cooperative Marketing Association*, 276 U. S. 71.)

CHARACTERISTICS OF FARMERS' PURCHASING COOPERATIVES

Farmers' cooperative associations today have the following general characteristics of organization and operation. The statutes of a number of States prohibit the use of the word "cooperative" in the name of the corporation unless the corporation is in fact a cooperative one, or unless it is organized under a certain statute. The law of at least one State, Montana, prohibits the use of the word "farmer" unless one-half of its members are "farmers by occupation." In general these associations are incorporated, with or without stock. A number of States provide for the incorporation of cooperatives on a nonstock or membership basis. This type of incorporated association is very popular in California. A discussion of financing such associations through the revolving fund method will be found on page 52. The nonstock incorporated association should be carefully distinguished from the nonstock, unincorporated association, which also operates, as a rule, on Rochdale principles. Such organizations, which are common in all parts of the United States, may be looked upon as training schools for more permanent incorporated associations. Membership in an association formed with capital stock requires the purchase of a share or shares of stock which should be transferable only to those who meet specified conditions. Membership in a nonstock cooperative association is generally evidenced by so-called "certificates of membership", issuance of which should be restricted to those meeting the requirements for membership. Certificates of membership are generally not transferable except by approval of the association.

A cooperative association may select its members and thus determine for whom it will furnish supplies or market products (*W. G. Press & Co. v. Fahy, et al.*, 313 Ill. 262, 145 N. E. 103). In general a person continues to be a member of a cooperative association formed with capital stock until a valid transfer, redemption, or forfeiture of his stock is effected, although usually his rights as a member may be restricted if, for instance, he ceases to patronize the association. In

a nonstock cooperative association a person continues to be a member until he resigns or is expelled or has his membership terminated in accordance with law. As a member of either a stock or nonstock association, a person at common law has no right or interest in it after withdrawal, either voluntary or enforced. Likewise at common law upon dissolution of an association, only stockholders or members at the time of the dissolution are entitled to share in the net assets of the corporation.

Preferred stock should be limited as to dividends, may be given preference upon dissolution, and if nonvoting may be held by nonproducers and not be restricted as to transfer. In addition to the capital acquired through stock or membership subscriptions, associations frequently finance themselves by issuing so-called "certificates of equity", which represent deductions from operating revenue or savings. Such a certificate records the member's equity in the assets of the association. Other terms commonly used are "certificates of indebtedness", "certificates of interest", and "revolving fund certificates." These certificates are generally analogous to noncumulative, nonvoting preferred stock. (See p. 52.)

A cooperative purchasing association ordinarily is not required to sell exclusively to members. Sales are customarily made at the market price and, after all necessary expenses and reserves have been deducted from gross income, the savings that remain are distributed among patrons in proportion to the value of their purchases, as "patronage dividends." (See p. 43.)

Cooperative marketing associations frequently enter into contracts with their members by which the members bind themselves to market their products solely through the association and to pay liquidated damages in the event of a violation of such agreement, but purchasing associations do not as a rule enter into contracts requiring their members to purchase their supplies exclusively through the association. Generally an association empowers its board of directors to promulgate rules and regulations which set forth the relationship of the member to the association with reference to the purchase of supplies. The bylaws of some associations provide for the automatic forfeiture of membership upon failure to patronize the association for a given period of time. Cooperative purchasing associations generally operate on the principle that the advantages inherent in a well-managed cooperative purchasing association will assure steady patronage without resort to contracts.

LEGAL POSITION OF COOPERATIVE PURCHASING ORGANIZATIONS

Nearly all of the States have included provisions in their constitutions or statutes against monopolies, trusts, and restraint of trade. These statutes prohibit any contract or combination or association

which tends to injure the public by stifling competition and unduly enhancing prices. States which have enacted such antitrust laws without expressly excepting farmers' cooperatives have generally passed farmers' cooperative statutes of the nature already discussed. Since such statutes are subsequent in time to the antitrust laws of these States, it can reasonably be said that State legislation clearly intended that antitrust laws should not apply to farmers' cooperatives.

Congress has enacted antitrust and restraint-of-trade statutes applicable to business conducted in interstate commerce—the Sherman Antitrust Act (1890) (26 Stat. 209, title 15, U. S. C. A., sec. 1) and the Clayton Act (1914) (38 Stat. 730, title 15, U. S. C. A., sec. 12). Nonprofit agricultural or horticultural organizations not having capital stock were excepted from the prohibitions of the Clayton Act. In 1922, Congress passed the Capper-Volstead Act (42 Stat. 388, title 7, U. S. C. A., sec. 291), which expressly authorized farmers to act together in associations formed with or without capital stock. Such associations in their normal operations are regarded as exempt from the provisions of the antitrust laws. This act, however, does not apply to purchasing associations or to cooperative stores.

It has been held, however, by both Federal and State courts that individuals have a right to join together for the purpose of purchasing commodities which they require for use in the conduct of their separate enterprises. The courts have recognized that the motive for such organizations is the acquisition of necessary commodities on more advantageous terms than those available to individuals. Such motive, it has been stated, does not operate unduly to stifle competition and obstruct commerce, but rather to encourage competition and trade.

As early as 1909 an arrangement, whereby individual jobbers of window glass joined together as a jobbers' association for the purpose of purchasing glass jointly from manufacturers, was approved by the highest court of Massachusetts (*Wheeler-Stenzel Co. v. American Window Glass Co.*, 202 Mass. 471, 89 N. E. 28 (1909)). In the same year a similar arrangement was considered by one of the Federal courts not to be an unfair method of competition (*Arkansas Brokerage Co. et al. v. Dunn and Powell, Inc.*, 173 F. 899 (1909)). In this case five domestic corporations, constituting substantially all the jobbers in a city, had organized a corporation to do their own brokerage business, as well as any other such business which it might obtain. The court held that neither the jobbers' association nor its method of operation was prohibited by the antitrust statutes or by the common law, in existence prior to the enactment of such statutes. It stated that since the jobbers could have given their brokerage business to an enterprise already in existence, they had an undeniable right to associate together and to operate their own brokerage business in competition

with other brokers—particularly in view of the fact that their purpose was to promote economy.⁷

Generally speaking, purchasing associations of farmers may enter into agreements with their members requiring them to purchase specified supplies through the associations, and the associations likewise may lawfully enter into contracts with sellers for the furnishing of the supplies.

Cooperative associations are, as ordinary business corporations, subject to property taxes; and are required to pay such franchise or license taxes as are specified by the law for such corporations. On the theory that they are nonprofit organizations, Congress has exempted both cooperative marketing and cooperative purchasing associations from liability for the payment of Federal income taxes, provided they are in fact farmers' cooperative associations meeting the conditions specified by Congress for exemption (Revenue Act of 1934, 48 Stat. 683, title 26, U. S. C. A., sec. 5001). The fact that an association has capital stock does not affect its right to exemption from Federal income taxes if the dividend rate on the stock is fixed at not to exceed the legal rate of interest in the State of incorporation or 8 percent per annum, whichever is greater. An association formed with capital stock must have substantially all of it, other than non-voting preferred stock, held by producers who market their products or purchase supplies and equipment through the association. An association may not be denied exemption because it accumulates and maintains a reserve required by the State law or a reasonable reserve for any necessary purpose. A statement on exemption of farmers' cooperative associations from certain Federal taxes will be found in appendix B.

RECENT FEDERAL LEGISLATION AFFECTING FARMERS' PURCHASING COOPERATIVES

In 1926 Congress enacted the Cooperative Marketing Act (44 Stat. 802, title 7, U. S. C. A., sec. 451) which provided for the creation of the Division of Cooperative Marketing in the Department of Agriculture. This Division was directed to carry on research and provide other assistance to farmers' cooperative marketing and purchasing associations. The Division of Cooperative Marketing was transferred by Executive order under authority of the Agricultural Marketing Act of 1929 (46 Stat. 11, title 12, U. S. C. A., sec. 1141) to the Federal Farm Board, later the Farm Credit Administration. The Farm Credit Act of 1933 (48 Stat. 257, title 12, U. S. C. A., sec. 1131) authorized the establishment of 12 regional banks for

⁷ It is appreciated that there are court decisions that appear to be in conflict with those cited. See *Pulpwood Company v. Green Bay Paper & Fiber Company*, 188 F. 2d 400, (70 N. W. 230 (1919)).

cooperatives and a Central Bank for Cooperatives for the purpose of making loans, not only to farmers' marketing associations, but also to farmers' purchasing associations for their activities in the distribution of supplies. (See pp. 55-58.)

The Farm Credit Act of 1933 also enlarged the powers of the Federal intermediate credit banks, to enable such banks to make loans to and discount paper of farmers' cooperative purchasing associations. Up to this time Federal credit aid had been available only for marketing purposes.

The Farm Credit Act of 1935 (Public, No. 87, 74th Cong.) enlarged the lending authority of the banks for cooperatives to further aid cooperative purchasing associations. They may now make loans to eligible cooperative associations of farmers engaged in purchasing farm supplies, or in providing farm business services, to assist not only in financing the ordinary business operations of such associations, but in the construction and acquisition of physical facilities and the refinancing of previous indebtedness for such facilities.

In 1935 Congress passed the Motor Carrier Act, which provides for the regulation of the transportation of passengers and property by motor carriers operating in interstate or foreign commerce. The statute provides for its administration by the Interstate Commerce Commission. Among other things, the statute provides for the regulation of trucks and busses that operate as common carriers and also includes contract carriers by motor vehicles.

Section 203 (b) reads in part as follows:

"Nothing in this part, except the provisions of section 204 relative to qualifications and maximum hours of service of employees and safety of operation or standards of equipment shall be construed to include * * *

"(4a) motor vehicles controlled and operated by any farmer, and used in the transportation of his agricultural commodities and products thereof, or in the transportation of supplies to his farm; or (4b) motor vehicles controlled and operated by a cooperative association as defined in the Agricultural Marketing Act, approved June 15, 1929, as amended;"

From the foregoing it is apparent that the statute does not apply to cooperative associations of producers, as that term is defined in the Agricultural Marketing Act as amended, except with respect "to qualifications and maximum hours of service of employees and safety of operation or standards of equipment" as specified in Section 204 of the Statute.

STRUCTURE OF FARMERS' COOPERATIVE PURCHASING ASSOCIATIONS

COOPERATIVE associations for the purchase of farm supplies in the United States may be generally classified according to area served as local (county or community) or regional. Local associations in turn may be classified as (1) informal farmers' purchasing groups, (2) unincorporated local purchasing associations, (3) incorporated local purchasing associations. The regional purchasing cooperatives may be divided into three categories: Associations of the federated type, associations of the centralized type, and associations which are combinations of the federated and centralized types. Cooperative purchasing organizations may also be classified as membership or stock associations, and in other ways. The classification here used is employed for general convenience.

TYPES OF LOCAL ASSOCIATIONS

Informal Farmers' Purchasing Groups

Probably the simplest type of purchasing association is an informal group of farmers who, through a purchasing committee comprised of one or more local men, order supplies for the entire group. These purchasing committees obtain the best possible prices on supplies, assemble orders, collect from the farmers, place the orders with the dealer or manufacturer selected (with instructions as to method and time of shipment), and then notify the members when the supplies are received. Such groups operate no warehouses and own no facilities. The members are required to call at the railway or at some central location for their supplies. Most of these associations operate on a cost basis—that is, the member obtains supplies at cost plus a share of the transportation and miscellaneous charges. As a rule, the expenses of such associations are small, and the purchasing committee makes no charge for its services. The supplies handled are usually those which farmers require in large quantities, and which can be purchased in large lots, as fertilizer and feed. This method of purchasing is employed especially in the South, where expense for fertilizer represents frequently a large part of the cost of producing a crop, and in New England and other eastern States, where commercial dairying requires large expenditures for feed.

Unincorporated Local Purchasing Associations

The second type of cooperative purchasing association is that in which farmers are organized in unincorporated associations. These are usually an outgrowth of the informal purchasing groups. They are generally set up with definite rules for operation and usually have paid managers. As a rule, they own no warehouses but purchase

considerable quantities of supplies for car-door delivery. Sometimes, however, rented warehouse space is provided by the association in which to store supplies until called for by the members. Many of these organizations operate in conjunction with county or community farm organizations. Associations of this type often restrict their services to members of a particular farm organization. The small amount of operating capital required is usually obtained by charging a membership fee. A management fee or a commission may be charged to cover the cost of management.

Sometimes unincorporated associations are operated in connection with some other cooperative enterprise in the community. For example, in order that their members may buy supplies cooperatively and to the best advantage, certain cooperative creameries and poultry- and egg-marketing associations have fostered the organization of unincorporated purchasing associations. The manager of the marketing organization usually acts as the manager of the purchasing association as well, and the costs of management are apportioned between the two organizations. The supplies handled are usually those required by farmers in certain special lines of agriculture, such as dairying and poultry and egg production. Feed and seed are the principal supplies handled, although farm machinery, dairy equipment, petroleum products, dairy and poultry remedies, and other miscellaneous items are often purchased cooperatively in this way.

Incorporated Local Purchasing Associations

A third type of local cooperative purchasing organization is the incorporated association. Such associations obtain operating capital principally through the sale of common and, in some cases, preferred stock. Such incorporated associations may also get a considerable amount of capital from membership fees, or savings resulting from operations. (See p. 48.) Although most of these organizations are incorporated under the cooperative laws of the various States, some are incorporated under general corporation laws. Before cooperative laws existed the older associations were organized under the general corporation laws as nonprofit organizations. Some of these associations have been reorganized under the cooperative laws in order that their members might obtain the benefits accruing to farmer cooperatives under the different State and Federal cooperative acts.

Local incorporated associations may be of either the warehouse or the bargaining type. The warehouse type operates a warehouse or store and carries stocks of various commodities so that members may call at the distributing station at any time and make their purchases. Numerous cooperative feed stores and oil associations in the different States are examples of this type of cooperative enterprise (fig. 5). The management of incorporated associations rests in the board of

directors chosen from the membership. A manager is usually employed to have direct charge of the association's affairs under the board's direction. As a rule, managers are full-time employees but in some associations they work on a part-time basis. Their compensation is generally based on the amount of time required to handle the business or on the quantity of supplies handled. Usually they



FIGURE 5.—WAREHOUSE OF A LOCAL COOPERATIVE PURCHASING ASSOCIATION HANDLING FEED, SEED, AND FERTILIZER.

Farmers bought cooperatively \$175,000 worth of feed, seed, and fertilizer of high quality from this North Carolina association in 1934.

are paid a straight salary, but they may receive a commission. Payment of commissions has a tendency to encourage managers to be more interested in building up a large business than in providing service and quality to farmer members.

The incorporated associations which operate as buying agents usually own no facilities but have connections or contracts with dealers or manufacturers whereby trade or quantity discounts on various supplies are obtained. The members of such associations receive the benefits of these discounts and usually pay a certain fee or commission (which is added to the cost of the supplies) to cover the cost of rendering this type of purchasing service. These agent associations are employed for the cooperative purchasing of seed, fertilizer, petroleum products, and miscellaneous farm supplies.

FORMS OF REGIONAL ASSOCIATIONS

In an earlier section mention was made of cooperative purchasing associations which are organized to serve areas larger than rural communities. Such associations serve areas embracing several counties or parts of several counties, States or parts of States, or several States (fig. 6). These associations are often referred to as "large-scale" or "regional" associations. It is appreciated that the term "regional" is

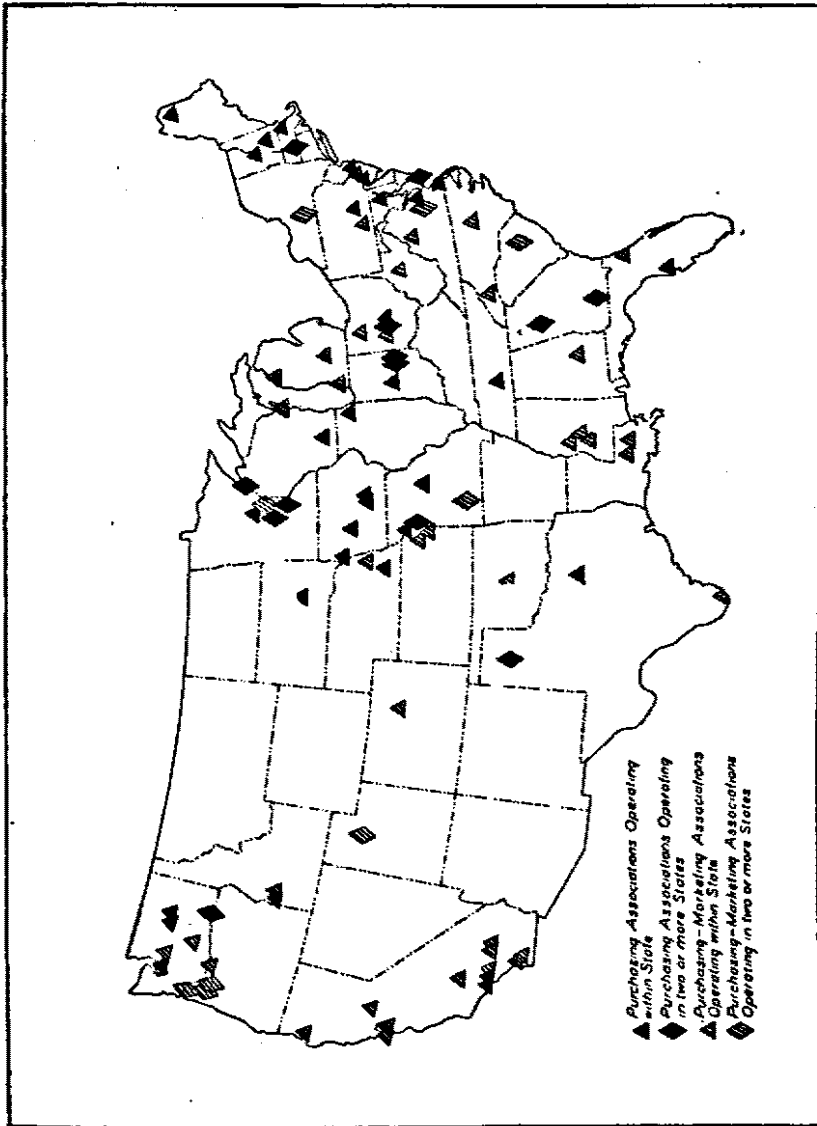


FIGURE 6.—REGIONAL FARM SUPPLY ASSOCIATIONS IN THE UNITED STATES.

often applied to associations operating over a wide territory, while the term is used here to define associations operating in an area larger than a county. Although the term "large-scale" is sometimes used for such organizations, it is not generally satisfactory, since many associations operating on a local or county basis have a large volume of business.

Regional purchasing associations are generally organized on either a federated or a centralized basis. It should be pointed out, however, that organization structures are highly variable. It is difficult to find associations which may be considered strictly federated or centralized.

Voting Control of a Typical Federated Purchasing Association

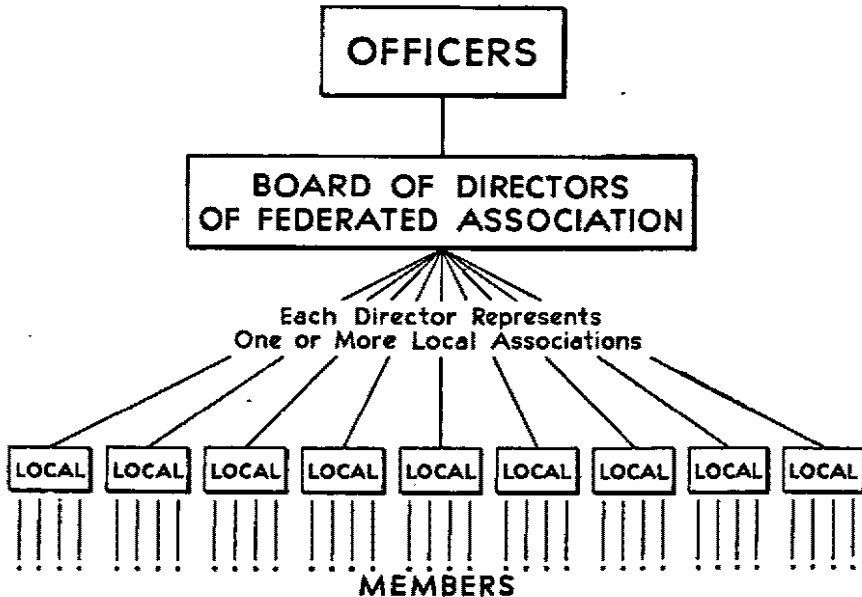


FIGURE 7.—VOTING CONTROL OF A TYPICAL FEDERATED PURCHASING ASSOCIATION.

Under the federated plan (fig. 7), associations combine to establish overhead wholesale purchasing organizations. The farmers are members of local associations and the local associations, in turn, are members of the overhead organization. Examples of the federated type of association are the Indiana Farm Bureau Cooperative Association, Inc., the Farm Bureau Cooperative Association (Ohio), the Farmers Union State Exchange (Nebraska), the Consumers Cooperative Association, and the Midland Cooperative Wholesale, Inc. Statistical information on the regional farm supply associations in the United States will be found in appendix A.

The centralized type of regional association (fig. 8), on the other hand, has individual farmers as members. While the federated type operates largely as a wholesale agency for local associations (fig. 9), the centralized type of association, to a large extent, combines the functions of wholesaler and retailer (fig. 10). Supplies are purchased on a wholesale basis by the centralized associations, and may be dis-

tributed over a wide area through branch offices or other local arrangements, directly to patrons. In other words, the centralized type association tends to integrate the wholesale and retail functions. A good example of the centralized type of association is the Eastern States Farmers Exchange. The Grange League Federation Exchange, Inc., may also be classified as a centralized association, since it serves members directly through local facilities and agencies, and since it is directly responsible to its individual farmer members through an annual membership meeting. (See also p. 37.)

The preceding discussion indicates that federated organizations differ from centralized organizations with respect to membership control and methods of operation. Figures 7 and 8 contrast the two methods of voting control. Figures 9 and 10 show the differences in operating methods. Comparison of these two figures indicates a more uniform type of local distribution by the typical federated association. The centralized association may distribute through one or all of the types of outlet shown in figure 10. The federated type,

Voting Control of a Typical Centralized Purchasing Association

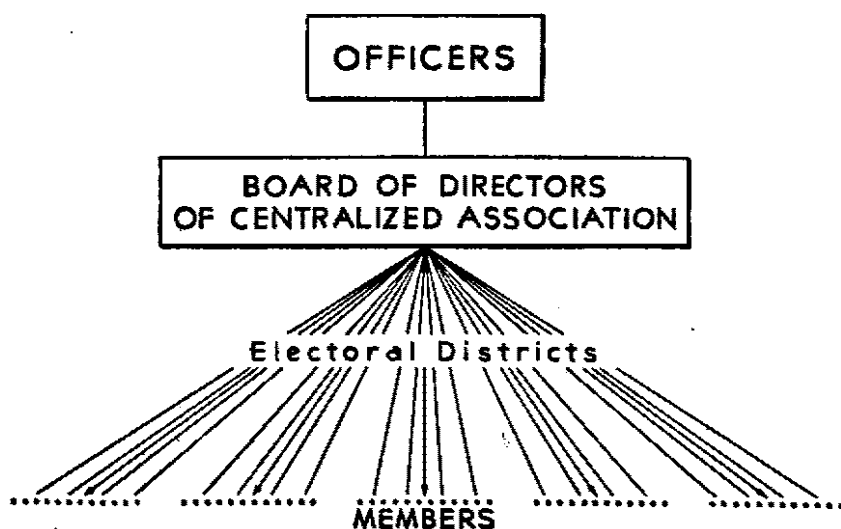


FIGURE 8.—VOTING CONTROL OF A TYPICAL CENTRALIZED PURCHASING ASSOCIATION.

as contrasted with the centralized type, brings the farmer member into less direct relationship with the main organization, both as to voting control and methods of operation.

A number of regional associations of the federated type operate on a brokerage or commission basis. These are sometimes termed

“brokerage associations.” They do not commonly have warehouses or other facilities for handling commodities. These associations usually order the supplies which are delivered directly to the local member

Distribution of Supplies by a Typical Federated Purchasing Association

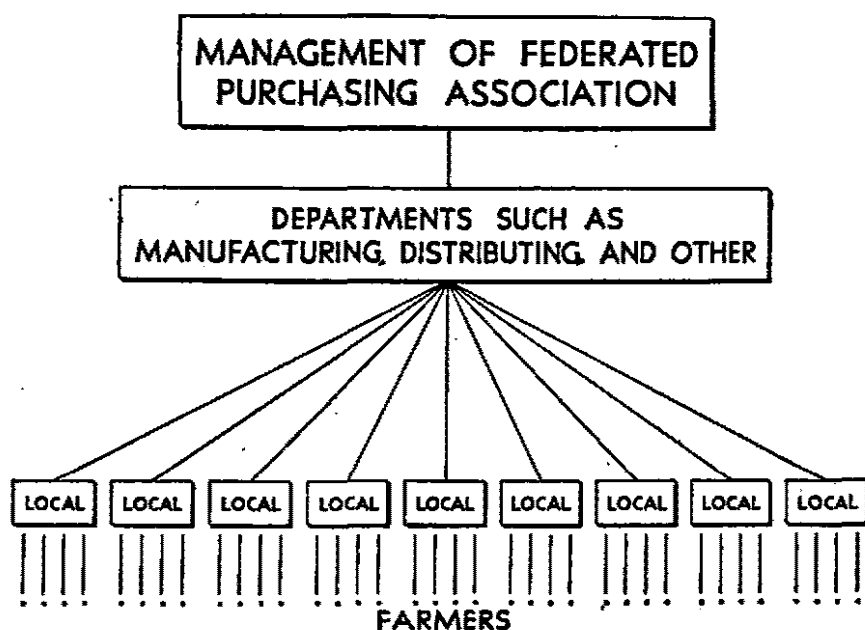


FIGURE 9.—DISTRIBUTION OF SUPPLIES BY A TYPICAL FEDERATED PURCHASING ASSOCIATION.

associations. Sometimes the supplies are invoiced to the overhead association and sometimes they are invoiced directly to the local association. In the first instance, the overhead association reinvoices them at a price sufficient to cover its expense of operation. When supplies are invoiced direct, the local association may remit a commission to the overhead agency or a commission may be included in the price charged to the local association and paid directly by the manufacturer or dealer to the overhead organization. In some cases an assessment is made on local units at the end of operating periods to cover their pro rata share of expenses for maintaining the overhead bargaining agency.

Organizations of the centralized type usually have local representatives, many of whom are farmers, who assemble orders in their respective areas and transmit them to the regional association. The shipments from the regional associations are made direct to individual members or groups of members. Organizations of the centralized type generally find it necessary to have a well developed system of field

representatives. Associations of the federated type have a greater degree of local control and usually find such extensive field services unnecessary.

In addition to the federated and centralized regional cooperative purchasing associations, there are regional cooperative associations which are neither strictly federated nor centralized. To a certain extent the Cooperative Grange League Federation Exchange, Inc., is an organization of this kind, since it both serves local associations as a wholesale source of supply and operates its own system of retail distributing facilities. The actual business operations of the G. L. F. are carried on through subsidiary corporations, the G. L. F. owning all of the common stock of the Cooperative Grange League Federation Holding Corporation, Inc., which in turn owns and controls the subsidiary operating corporations.

Distribution of Supplies by a Typical Centralized Purchasing Association

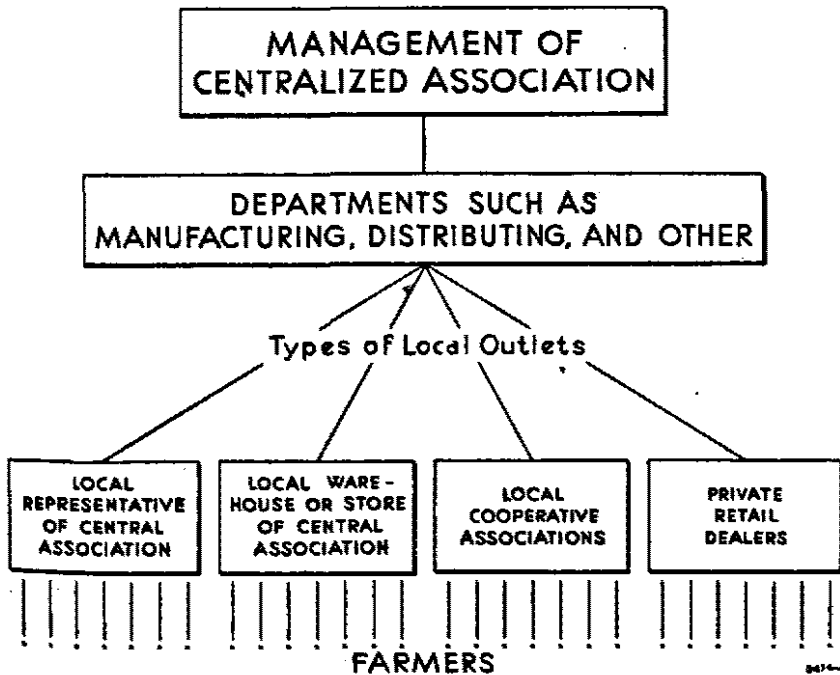


FIGURE 10.—DISTRIBUTION OF SUPPLIES BY A TYPICAL CENTRALIZED PURCHASING ASSOCIATION.

The patrons have a direct voice in the control of the management through a system of local advisory committees. These advisory committees are composed of farmers who have the respect and confidence

of their neighbors and the time and willingness to meet four or eight times a year to help direct the policies of their local store. Their representatives also attend the G. L. F. annual meeting and vote to the extent of G. L. F. stock owned by the store, local cooperative, or marketing agency which they represent.

The directors are elected by the stockholders at the annual stockholders' meeting, 5 of the 13 directors being elected each year. They are nominated in advance of the annual meeting to represent the New York State Grange, the New York State Farm Bureau Federation, the Dairymen's League Cooperative Association, Inc., G. L. F. service agencies and other like affiliated cooperatives. Other nominations are made at the annual meeting.

The Southern States Cooperative, Inc. (the S. S. C.), is organized on a basis which compares to a certain extent with that of the G. L. F., although the members elect directors by districts for the territory served. The S. S. C. does a combined wholesale and retail business by operating its own service stores and a wholesale business through local dealer agencies and cooperative associations. It also serves as a wholesale source of supplies for the Farmers Cooperative Exchange, Inc., of North Carolina, which has an arrangement for the exclusive distribution of supplies manufactured and handled by the S. S. C. in that State. The Farmers Cooperative Exchange, Inc., is largely an organization of the combination type, its bylaws providing that cooperative associations as well as individual farmers may hold membership.

PURCHASING DEPARTMENTS OR SUBSIDIARIES OF FARMERS' MARKETING ASSOCIATIONS

As noted in the section on development of cooperative purchasing a number of regional cooperative marketing associations of both the federated and centralized types have established departments or subsidiary associations to purchase supplies for members. These operate in much the same way as independent purchasing associations, except that joint use may be made of personnel, capital, services, and facilities. This method of cooperative purchasing has proven economical and particularly suited to the purchase of supplies used by patrons of the marketing association. For illustration, the members of a fruit marketing association require package materials, and the members of a poultry association require feed, both of which may be purchased advantageously through their respective marketing associations. A large overhead cooperative creamery association can purchase dairy equipment and supplies for its member creamery associations.

Marketing associations often find it possible to carry on a supply business which is essential to their operations with practically no addition to the personnel required ordinarily for marketing work.

This is largely because the supply purchasing season usually precedes the marketing season, making it possible to utilize more completely labor, facilities, and general overhead, and effect economies that would not be possible if only the marketing activity were carried on. Such economies may result in larger savings for farmers and more satisfactory service for patrons.

METHODS USED IN COOPERATIVE PURCHASING

COOPERATIVE purchasing associations operate in accordance with established business principles. The significant difference between cooperative purchasing and ordinary business operation lies in the fact that the cooperative is engaged in buying those commodities required by its members, while the ordinary business concern is engaged in selling products to all prospective customers. The cooperative purchasing association, although striving for efficiency, is not interested in obtaining a profit on operations for the benefit of those who subscribe capital. It aims rather to procure for members necessary supplies of high quality at the lowest possible cost.

The operating methods of cooperative purchasing associations may be discussed under the following headings: (1) Sources of supplies, (2) distribution facilities and services, (3) cash or credit sales, (4) price and patronage dividend policies, (5) accounting procedure, and (6) maintenance of quality.

SOURCES OF SUPPLIES

Cooperative purchasing associations obtain their supplies through wholesalers, jobbers, primary producers, and manufacturers, who may operate on either a commercial or a cooperative basis. As cooperative associations grow in size, they tend to undertake first cooperative wholesaling and then the direct manufacture of the required supplies. This tendency is illustrated by the history of such large-scale purchasing associations as the G. L. F., the Eastern States Farmers Exchange, and the Farmers Union Central Exchange, Inc., which now operate extensive manufacturing properties (fig. 11).

Other large cooperatives join together to make special contracts with manufacturers or wholesalers to obtain at a reduced cost supplies especially prepared for them. Certain cooperative purchasing associations have combined in this way to obtain benefits (through quantity buying and quality standards) from manufacturers and wholesalers in the purchase of such supplies as feed, fertilizer, and petroleum products. A striking example of this tendency was the establishment in 1932 of National Cooperatives, Inc., discussed above in the section on development of cooperative purchasing. National Cooperatives, Inc., reports that in 1934 it brought together for bargaining pur-

poses 500,000 farmers who together bought \$19,202,390 worth of oil, gasoline, and other farm supplies.* Commodities distributed through the regional members of National Cooperatives, Inc., are sold under a trade mark which is in the form of an outline map of the United States on which is inscribed the word "CO-OP."



FIGURE 11.—COOPERATIVE OIL BLENDING PLANT RECENTLY OPENED BY THE FARMERS UNION CENTRAL EXCHANGE, INC.

This building also houses the general offices of the association.

Farm-supply cooperatives purchase a considerable volume of their supplies from cooperative marketing associations. The cooperative associations which market feeds and seeds afford a natural source of supply to cooperative purchasing associations. In some cases where cooperative purchasing and cooperative marketing are carried on by one association, members may obtain supplies which have been produced by other members.

Many cooperatives have not established contact with satisfactory sources of supplies. This is particularly true of many small cooperatives who would benefit by joining with other cooperatives for this purpose. Perhaps the most striking recent development in cooperative purchasing has been the federation and unification of cooperatives which makes it possible for smaller associations to obtain more dependable supplies at lower cost because of large-scale bargaining power thus obtained.

DISTRIBUTION FACILITIES AND SERVICES

Cooperative purchasing associations are not selling organizations, but it is essential that such agencies have the equivalent of the distri-

* While National Cooperatives, Inc., is not exclusively a farmers' organization, the great bulk of supplies sold is purchased by farmers for use in their farming operations.

bution services of business concerns wherever this is to the producer's interest. Thus cooperative purchasing associations generally provide local facilities through which supplies may be obtained conveniently and economically at any time. Such facilities have proven most satisfactory when located on railroad sidings with adequate parking and loading arrangements, out of high-rent districts but not too far removed from other business establishments. Certain associations, however, do not find it necessary to employ handling facilities. Supplies may be shipped to local points in carload quantities and delivered directly from the car to the patrons. As stated above, this method of handling is common in many parts of the United States.

Many farmers' purchasing associations have found it desirable to operate delivery trucks as a convenience to members. The Washington Cooperative Egg and Poultry Association owns a fleet of approximately 120 trucks which operate from warehouse centers and cover the State, delivering supplies required and collecting produce to be marketed (fig. 12). Tank trucks also play a very important part in the operation of associations handling petroleum products. Association oil trucks generally cover definite routes to supply, at fixed intervals, the needs of farmer members. The significance of truck

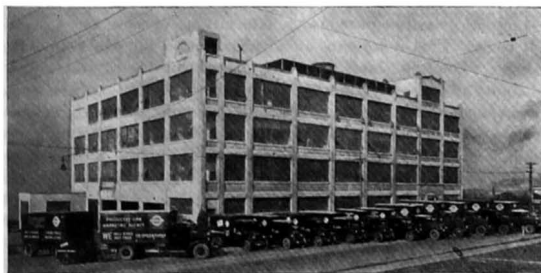


FIGURE 12.—GENERAL OFFICE AND PLANT OF THE WASHINGTON COOPERATIVE EGG AND POULTRY ASSOCIATION, SEATTLE, WASH.

Farmers bought over 160,000 tons of feed, worth more than \$5,000,000, through this cooperative in 1934. The trucks in the foreground are used jointly for marketing and purchasing work.

operation in this field is indicated by the fact that the affiliated service companies of the Illinois Farm Supply Co. operated 427 tank trucks in rural Illinois territory in the fall of 1934.

Cooperative purchasing associations which handle farm machinery, dairy equipment, and similar supplies have often found it desirable to provide repair and installation service, although an association must

handle a considerable volume of such supplies to justify the expense of such service. A large-scale organization such as the Land O'Lakes Creameries, Inc., however, which handles large quantities of dairy equipment, has been able to provide repair and installation service economically.

A certain amount of advertising and selling service must be provided by cooperative purchasing associations in order to acquaint member patrons with the advantages of buying through the association. Some associations advertise through newspapers and farm journals. Others do most of their advertising through their own house organs or by means of painted signs or printed or mimeographed statements. Every employee of a cooperative purchasing association is a salesman to the extent that he acquaints farmers with the advantages of patronizing their own association. There is one general difference between commercial advertising and selling and cooperative advertising and selling. Commercial salesmanship is designed primarily to bring about greater profits for the benefit of the operator. In the case of the cooperative association, advertising and selling may be looked upon as an information service designed to encourage member patrons to make full use of their own association for their own benefit.

CASH OR CREDIT SALES

Many cooperative purchasing associations operate on a strictly cash basis. This represents an ideal situation for any cooperative business. Doing business on credit ties up working capital, restricts the ability of an association to render other valuable services, causes management worries and dissatisfaction among members, increases expense for collection, necessitates more extensive bookkeeping, and entails losses from bad debts. Cash trading puts all members on a similar basis in dealing with the association and reduces selling prices or increases refunds by cutting down financial and operating expense. However, complete cash business is not always possible, for in many rural communities credit service is deeply rooted. Since competing agencies often allow very liberal credit privileges which induce farmers to buy on credit, many cooperatives must continue to sell goods on careful terms until farmers can become better situated financially, or can obtain credit from banks or from governmental or other sources, which will enable them to pay cash.

Cooperative purchasing associations offer an opportunity for farmers to appreciate the advantages of doing business on a cash basis. It may be said that one of the objectives of the cooperative purchasing movement is to assist farmers to operate on a cash basis by effecting savings and developing a better understanding of credit costs. Many purchasing associations have found it desirable to keep records which show how costs are increased by credit business (38). Some associ-

ations try to discourage credit buying by allowing a discount for cash. Associations that extend credit should proceed with caution and follow a vigorous collection policy.

The establishment of cooperative production credit associations by the Farm Credit Administration under authority of the Farm Credit Act of 1933 promises to play an important role in enabling farmers to operate on a cash basis. With a cooperative system of production credit, there is no reason why a purchasing association should grant credit to any farmer who can meet the loan requirements of a production credit association. Moreover, if a farmer cannot meet these requirements, it is clear that he should not be given credit freely by a cooperative purchasing association. While set up primarily to reduce the farmer's operating costs, the production credit associations should tend to remove one of the major obstacles to the efficient operation of cooperative purchasing associations.

PRICE AND PATRONAGE DIVIDEND POLICIES

Cooperative purchasing associations generally price goods to be sold on a cost-plus-handling-charge basis, on a prevailing-price basis, or on a part-cost part-prevailing-price basis. In 1934 an analysis by the Cooperative Division of 779 cooperative purchasing associations, disclosed that 131 used the cost-plus-handling-charge basis, 361 the prevailing-price basis, while 287 associations used combinations of these 2 methods.

Some associations consider it better practice to handle supplies on a small margin and distribute little or no patronage dividends than to sell at prevailing prices and return the savings to members on a patronage basis. The goal of both methods is the same; namely, to permit members to obtain supplies at cost plus operating expense. The cost-plus-handling-charge policy places an association on a direct price-competing basis. It may entail complicated bookkeeping procedure of doubtful value if applied on a strict cost-accounting basis. This system of pricing is favored by associations which desire to build up volume by selling at a low price.

Many farmers' buying associations favor selling at prevailing prices in order that competitive conditions may not be unduly disturbed. Under the prevailing price method, any net difference between cost-plus-expenses and selling price is not considered a profit, as in private business, but a saving returnable to the purchaser. This saving, known as a "patronage dividend", is prorated to the farmers in accordance with each member's share of the total business done. As indicated in the section on financial problems of farmers' cooperative purchasing associations, it is a common practice for cooperatives to pay patronage dividends in the form of stock as a means of building up the capital structure. In some cases where each member of a

cooperative is required to purchase at least one or more shares of stock, it is common for associations to credit amounts which would be earned on an individual's patronage toward the purchase of a share of stock. Thereafter, the patron would be a member and eligible for cash patronage refunds.

Patronage dividends are paid usually once a year, after the results of the year's operations are known, although some associations pay on a semiannual or other basis. It is not considered good policy to pay patronage dividends more often than twice a year since this increases the accounting costs in making the distribution and decreases the amount of the dividend. Furthermore, the results of seasonal business cannot usually be determined for periods of less than 6 months or a year.

One advantage of operating on the prevailing price method is that the extent of patronage dividends serves to show the common price margins. A good sized patronage dividend indicates clearly the advantage of cooperative organization. When a cooperative pays patronage dividends, other concerns are influenced to lower prices so as to hold business. In this way the payment of patronage dividends by a cooperative plays an important part in reducing the general level of prices to the benefit of the agricultural producers who are not members of the cooperative.⁹

While patronage dividends offer a measure of inducement for farmers to become members of a cooperative organization, some cooperatives have overemphasized their importance. The competition engendered by the cooperative may tend to reduce the cost of supplies to farmers even though patronage dividends are not paid. The cooperative may, in effect, enable all farmers of the community to obtain supplies at comparatively low cost. As a general rule a cooperative should not pay patronage dividends out of any year's operations before it has built up adequate operating capital and reserves. That is to say, an association should not impair its ability to render service because of its patronage dividend policy. (See p. 54.)

ACCOUNTING PROCEDURE

Cooperative purchasing associations in general employ standard business accounting technique. However, in many cases the accounting system can be simplified because of the small range in commodities handled. Many small groups employ little more than a record book.

In one way, accounting for cooperatives is more complex than for ordinary business establishments since savings are generally dis-

⁹ It is interesting to note that Executive Orders numbered 6355 and 6606-A, issued under the National Industrial Recovery Act, recognized that the payment of patronage dividends is not an unfair trade practice.

tributed according to patronage. When this is done a record must be kept of the business of each member so that he may be paid patronage refunds in accordance with the proportion of his business to the total business. Many associations use a card system to record transactions with members as they are made. These cards may be totaled conveniently for any fiscal period. Some associations keep patronage records by commodities so that patronage refunds may be made on a commodity basis rather than for the entire business. The disadvantage of paying patronage dividends on a commodity basis is that it requires for absolute accuracy a system of cost-account records to allocate overhead expense for each commodity. Certain associations have found it practical to distribute a general dividend and special commodity dividends on products handled in great quantities.

There has been a significant development of standardized bookkeeping procedure for cooperative purchasing associations in recent years. For illustration, a centralized accounting system, which is used in modified form by the G. L. F. and a number of large-scale organizations of the centralized type, simplifies accounting work so that an experienced bookkeeper is not required at local distributing points. The local manager simply sends in to the central office a daily report which includes duplicate slips for all transactions. All accounting analysis for the local is carried on at the central office. Many large-scale regional purchasing associations of the federated type have also standardized accounting and auditing services for member units. In such cases the actual accounting records are maintained by the local or county member associations, although supervised and audited by the overhead association. This system makes possible uniformity of bookkeeping practices over a wide area and comparison of the operating efficiency of the member associations.

MAINTENANCE OF QUALITY

Furnishing supplies of high quality is accepted by cooperative purchasing associations as a fundamental principle of operation. Since the purchasing associations exist to supply farmers with the raw materials of their industry, they would not be justified in handling merchandise which did not further maximum farm efficiency. In many cases cooperative purchasing associations have been established primarily as a means of guaranteeing dependable supplies of a high standard of quality, price being a secondary consideration.

Cooperative purchasing associations have pioneered in the development of open formula feeds and fertilizer and the use of viability and climatic adaptability records on seeds. In this work they have

cooperated wherever possible with agricultural colleges and governmental agencies. Cooperatives in many States follow the recommended formulas of college feed conference boards and print the formulas of the feeds which they handle on the bags.

One of the reasons why cooperatives have undertaken the manufacture of their own supplies is the desire of farmers to be sure of the quality of the raw materials used in the manufacture of the supplies.

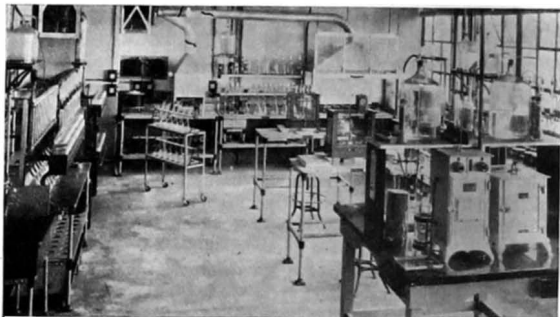


FIGURE 13.—UP-TO-DATE LABORATORY OF THE EASTERN STATES FARMERS EXCHANGE.

In this laboratory experimental and check tests are conducted in order to control the quality of materials used in cooperatively processing and distributing feeds, seeds, fertilizer, and other supplies for farmers.

While the use of the open formula may indicate in a general way the content of the feed or fertilizer, there may still be an opportunity for a manufacturer to use ingredients which legally meet the requirements of the formula but which are lacking in nutrient or plant food value. Several cooperative purchasing associations which operate manufacturing plants for feed or fertilizer have extensive laboratory facilities where raw materials are carefully analyzed and finished supplies tested before distribution to see that they come up to specifications. In a similar way cooperative petroleum associations employ laboratories to test oils and other supplies. These laboratories also carry on basic research in order to improve the manufactured product (fig. 13).

A striking example of cooperative effort to insure a high quality standard in supplies is found in the program of the Eastern States Farmers Exchange. This association has extensive trial grounds which are under the supervision of highly trained plant pathologists and technicians, who make tests of the seeds handled in order to determine their quality and to assist in the development of seeds of proven viability. Close cooperation in the seed program is also maintained with the agricultural experiment stations in the terri-

tories served. For illustration, this association recently maintained a fellowship in one of the New England agricultural colleges in order to have a test study made under careful scientific conditions. Reference should also be made in this connection to the fertilizer laboratory of this association which endeavors to analyze soil types and conditions in order to assist farmers to obtain the type of fertilizer which will give the most satisfactory results. Many further illustrations could be given of how cooperatives strive to raise the quality standards of farm supplies. In general, cooperative purchasing associations are alert to find evidence of adulteration or misstatement in the products which they buy for their members.

The development and maintenance of quality standards by cooperative purchasing associations has been greatly furthered by large-scale operations (fig. 14). Small associations cannot afford to render such comprehensive service in maintaining quality because of the cost of laboratory and field equipment and of employing highly trained technicians for this type of work. However, small associations can carefully select supplies for the benefit of their members.

FINANCING FARMERS' COOPERATIVE PURCHASING ASSOCIATIONS

BUSINESS undertakings, whether commercial or cooperative, require various amounts of capital depending upon the nature of the enterprise and the volume of business. Farmers' cooperative purchasing associations, especially those operating warehouses or other distributing units, require considerable capital to provide physical facilities, carry inventories, render services, and assume business



FIGURE 14.—A MODERN COOPERATIVE OIL BLENDING PLANT.

Each of the outlet valves to be seen along the rear wall leads from one of a number of tanks which contain finished oil. Three men are barreling with portable and automatic barreling meters that deliver a measured quantity of oil, corrected for temperature.

risks. Associations which handle primarily quick-moving supplies such as petroleum products do not require so much operating capital as those handling large quantities of slow-moving commodities such as farm machinery. While certain supplies must be carried over

from one season to another, it is the general policy of supply purchasing associations not to carry large inventories, and this in general has been found to be a wise policy. In most cases members' supply requirements may be gauged in advance so that the need for carrying large inventories for long periods is small. Local associations of the car-door type do not require much capital since they operate no facilities, carry no inventories, and, as a rule, assume no risks.

The chief problems involved in financing cooperative purchasing associations are first, obtaining adequate initial capital when the association is being organized, and second, developing a financial program which will enable the association to operate on a permanent basis (45). In reality, these problems interlock since a program to provide initial capital should provide also for carrying on the operations of the association after its initial stages. In this connection well organized associations usually operate on carefully prepared budget plans which involve a detailed analysis of the anticipated business. This practice promotes business and financial efficiency.

OBTAINING INITIAL CAPITAL

Cooperative purchasing associations obtain capital to start and carry on their business operations in three main ways: (1) By membership fees, (2) by capital stock, and (3) by loans or credit. All or any of these methods may be employed.

Membership Fees

Small organizations require but little operating capital, and may be financed by membership fees. Many associations of the car-door type are not large and a small fee from each member is sufficient to provide adequate working capital.

Some of the larger incorporated organizations which purchase farm supplies for their members are also of the membership or non-stock type. Many of these large membership organizations are marketing associations which handle supplies in connection with their marketing activities. The Poultry Producers of Central California, San Francisco, Calif., is an example of a membership association which deals in farm supplies. Such large-scale cooperatives look upon the membership fee as a supplementary source of operating capital, since they usually obtain larger amounts from loans or by means of a revolving fund built up from charges in connection with operations. (See p. 52.) The certificate evidencing payment of the membership fee may be of value in such associations as a means of showing "residual equities" (41, p. 165) in the assets of an association.

Capital Stock

Purchasing associations which operate warehouses or other facilities for distribution and which carry supplies in stock require considerable amounts of capital. As a rule these associations are incorporated under the cooperative laws of the various States. Incorporation has the advantage of giving the investors of an association liability limited to their capital contribution. It also gives associations a certain standing, in that incorporation, particularly under cooperative statutes, implies certain standards. (For further discussion see section on the legal basis of farmers' cooperative purchasing associations, pp. 23-29.)

Associations that depend upon the issuance of stock for capital require each member to purchase at least 1 share of stock, and in some cases more than 1 share, the number depending upon the size of the individual member's operations and the benefits which he may derive from purchasing through the association. For example, a member of a feed association may be required to purchase 1 share of stock for every 25 cows in his herd. Certain associations permit the purchase of share capital on the partial-payment plan. A common practice is payment of an initial amount and payment of the balance by the application of patronage dividends. (See p. 44.)

Some associations obtain part of their capital requirements through the sale of preferred stock. This type of stock generally carries a fixed rate of interest which is frequently cumulative. It is generally redeemable at some future date at the discretion of the board of directors. The redemption of preferred stock is permissible under cooperative statutes, but certain general incorporation statutes do not permit redemption. In most cases holders of preferred stock have no voice in the affairs of the association. Certain difficulties are involved in this method of financing. Investors, as a rule, are skeptical of new undertakings and they do not wish to take the risks of loss which accompany such investments when the dividend is limited to a fixed rate and where there is little possibility that the stock will increase in value. The investor may feel that he will lose part or all of his investment if the undertaking fails, while if it is successful the preferred stock may be called for redemption at par or at a small premium. Investors usually prefer more seasoned or more readily marketable securities than the preferred stock of a newly organized farmers' purchasing association. From the fiscal standpoint of an association, preferred stock may not be entirely satisfactory. Such stock usually carries a fixed and cumulative dividend rate which places a burden on the association as long as the stock is outstanding.

Because of these features, associations often find it more desirable to obtain capital through the issuance of common stock or some other nonfixed-interest-bearing instrument which usually entitles the holder

to utilize the services of the association and which places no fixed charge upon the business. Preferred stock is often sold to public-spirited individuals who are anxious to have the association succeed and who are not primarily interested in large earnings on the investment. Preferred stock so sold provides funds which do not have to be repaid immediately, a factor of much importance when an association is becoming established.

Loans or Credit

Many associations obtain part of their initial capital by means of loans or credit. Sometimes loans for long-term financing, especially those for the financing of real estate or equipment, are obtained from banks or other lending agencies. Sometimes manufacturers or dealers supply credit through the installation of necessary equipment (feed-grinding machinery, for example) on a partial-payment plan. Short-term loans, used ordinarily for operating purposes, are obtained mostly from banks for cooperatives or from other lending agencies. As a rule short-term borrowing is used for temporary financing during periods of peak business and is considered supplementary to normal working capital.

Sound business practices are opposed to the use of too much borrowed money or credit. An oversupply of either may lead to carelessness in purchasing or to unnecessary or improper expenditures. Furthermore, interest on borrowed money is a direct expense on the operations of an association. If interest expense becomes unduly large it may cause the failure of an enterprise and the complete or partial loss of money invested by the members. It is generally considered safe policy for cooperatives to arrange for sufficient capital at the outset, through the sale of stock or memberships, to cover practically the initial cost of facilities and provide working capital for a minimum stock of supplies. Funds from banks or other agencies may then be borrowed to provide additional capital. Borrowing on the security of notes of members or directors is an unsatisfactory practice, for adequate capital should be obtained through membership fees, sale of stock, or on the security of collateral without making members or directors personally liable.

ACCUMULATING CAPITAL THROUGH OPERATIONS

Up to this point particular attention has been directed to the problem of obtaining initial capital for efficient operation. It is equally important for an association to have a financial program which will provide adequate capital for continuing operations. Well-established associations usually obtain operating capital partly from loans or credit and partly from funds built up through operations. Attention will be given later in this section to lending facilities which

are available to cooperative purchasing associations. At this point the methods used by cooperatives to build up capital from operations will be considered.

A number of associations issue capital stock or certificates of equity in connection with a revolving fund. By this arrangement active members supply capital in proportion to the use made of the association. For example, charges of 1 or 2 percent of sales may be made from the proceeds of each member's purchases, to be applied against the cost of shares. At the end of each fiscal period members are issued capital stock for the amount of the accumulated deductions. Where the revolving fund method is used the oldest outstanding stock is redeemed after a sufficient amount of operating capital has been obtained. Thereafter, as new stock is issued, a similar amount of old stock is retired. Under this plan each member tends to contribute capital to the extent that he uses the association.

The Fruit Growers Supply Co. which operates as a supply purchasing organization for the California Fruit Growers Exchange, Los Angeles, Calif., employs the following revolving-fund arrangement. A deduction of 4 cents per packed box of fruit marketed is made by the Exchange. The member packing houses are issued common stock in the supply company by the California Fruit Growers Exchange in accordance with the quantity of fruit marketed for them by the Exchange. Since the authorized capital of \$6,000,000 has been reached, proceeds from the issuance of new stock are now used to retire the oldest outstanding stock, which is at the present time about 6½ years old. In other words, the \$6,000,000 capital of the Fruit Growers Supply Co. revolves in approximately 6 or 7 years.

The California Fruit Exchange, Sacramento, employs a somewhat similar procedure in accumulating operating capital. From the commissions charged member associations on fruit marketed and service charges on supplies purchased, the costs of operation are deducted and the remaining earnings are used to provide operating capital, permanent reserves, and to pay dividends on capital stock. After payment of 8-percent dividends on capital stock and deductions amounting to one-half of 1 percent on gross sales for a permanent reserve, the balance of earnings is placed in a revolving fund called "withholdings repayable", and used as operating capital for the entire association until retired. These withholdings which amounted to \$1,598,196 on December 31, 1933, are noninterest-bearing and usually remain in the hands of the association for a period of 5 years.

Some associations, instead of building up capital by making fixed deductions per unit of product marketed or similar devices which may be burdensome in a highly competitive situation, issue patronage dividends in stock. In this way the savings of the association are used to build up the capital structure while each individual's equity in

such savings is clearly established. The net earnings of the feed department of the Washington Cooperative Egg & Poultry Association, Seattle, Wash., are thus used to provide operating capital. Preferred stock paying 8 percent interest per annum is issued to each member for his proportionate share of the annual net earnings. The stock in reality is a deferred patronage dividend which may be redeemed by the association at its discretion. During recent years it has been the policy of the association to retain these accumulated funds for a period of about 4 years. Preferred stock outstanding amounted to \$1,428,215 on December 31, 1934.

Certain membership-type associations have followed similar procedures by issuing certificates of equity, to represent earnings in lieu of stock. (See p. 25.) It is considered the more sound policy to have interest rates for such certificates currently established by the board of directors, for fixed interest charges may embarrass an association in its operations. It is also considered sound policy to have the certificates of equity subject to retirement at the discretion of the board of directors although such certificates are often redeemable at fixed dates in the future. The responsibility for retiring certificates at a given time may penalize the association in a period of business depression when sales values are low and loans difficult to obtain. In general, certificates of equity may be looked upon either as membership loans or as patronage dividends which are used as a source of working capital until paid. The plan is, according to Hulbert (*21, p. 105*), one under which the capital needed by an association is equalized, and,

to a degree at least, is shifted from year to year so that all members who utilize the association help to furnish its capital in proportion to the use they make of the association. The certificates are written evidence of loans which the members of an association have made thereto.

The method of the Poultry Producers of Central California (at San Francisco) in procuring capital through the use of "feed finance" certificates illustrates the certificate-of-equity method. This association has created a "feed finance fund" out of earnings of the supply department entirely separate from a similar fund created for marketing purposes. Certificates representing ownership in the feed finance fund are issued to members in multiples of \$10 and draw interest at the rate of 6 percent per annum. Funds so obtained are retained by the association as operating capital for the supply department for a period of about three years and then paid through retirement of the certificates. The outstanding feed finance certificates on December 31, 1933, amounted to approximately \$940,000.

RESERVE POLICIES

It is necessary at this point to indicate that revolving fund devices which are used to build up capital for satisfactory operation should not be confused with reserves or surpluses which are commonly created out of current operations. Members cannot directly earmark their contributions to true reserves or surpluses which are the general property of the association. A revolving-fund method sets up a claim for each member in the assets of the association, while the respective equities of members represented by reserves are difficult to determine. According to Stokdyk (41, p. 178).

True reserves in nonprofit corporations (cooperatives) are undivided and unassigned equities which are held to withstand unexpected or unforeseen losses. The courts have sustained this view of the nature of reserves holding that the reserve fund is "a permanent continuing fund and corporate asset" not limited to the year's business in which it is collected, and furthermore, that reserves may be used for the purposes deemed advisable by the association including the purchase of physical facilities.

Adequate reserves are essential to the successful operation of a cooperative purchasing association. They give proof to lending agencies and members that business is being conducted on a conservative and planned basis.

A reserve account provides for particular or unforeseen uses of assets. "Valuation reserves", such as reserves for bad debts and depreciation, are used to establish the proper value of asset accounts. "Liability reserves", such as reserves for taxes, if a definite liability is known to exist, should be provided for, even though it is necessary to estimate the amount of the liability. This reserve should not be confused with the item "accrued taxes", which represents a liability of known amount. Liability reserves may be set up for other debts where the amount of the liability is not definitely known, but must be estimated. Such reserves are somewhat similar to expense items since they recur in every operating period. Valuation and liability reserves should be set up in order to determine accurately the net worth and the profit and loss of an association.

Reserves for contingencies, on the other hand, represent assets which should be available to meet the uncertain needs of the business. Reserves for contingencies usually indicate a part of net worth which may be used as the management sees fit (subject to possible restrictions of the legal structure) in carrying on the business.

Some associations prefer to segregate definitely net-worth reserve accounts by such terminology as "reserve for contingencies", and "reserve for acquiring facilities." Other associations simply use a single net-worth account. The segregation of net-worth reserves by specific account names as to their purposes, however, is usually helpful. If all net-worth reserves are credited to a single net-worth account without proper classification, there may be a tendency for uninformed members or directors to distribute them in dividends. Numerous associations have paid out a large part of earnings in patronage dividends during times of prosperity only to find themselves cramped for working capital when business reaction sets in.

The determination of the nature of reserves to be set up and their adequacy are definite problems to be settled by the management on the basis of individual analyses. In general, reserves for contingencies must be sufficient to take care of unforeseen losses that might impair the ability of the association to render adequate service. It should be pointed out, however, that too large amounts may be set up in net-worth reserves as well as too little. Although an association may obtain for itself an impregnable position financially, it may destroy its support from the membership by retaining too great a part of its savings and failing to distribute a sufficient amount in the form of patronage dividends.

Furthermore, reserves must be more than bookkeeping entries. They must be available in the form of appropriate assets so that they can be used when the need arises. There should be cash or available assets sufficient to meet the needs for which the reserves were established. A reserve for contingencies does not serve its true purpose when it is necessary to borrow on fixed capital to make available the resources which it is supposed to represent.

Well-managed purchasing associations generally create adequate reserves for general and/or specific purposes and in addition may set aside a certain amount of savings in a surplus or reserve account. The extent of these withholdings for certain associations is indicated by the fact that the earned operating capital reserves of the Cooperative Grange League Federation Exchange, Inc. (the G. L. F.), amounted to \$2,362,872 on June 30, 1934. According to the G. L. F.'s balance sheet of that date, this represents an accumulation at an average rate of 1½ cents per dollar on \$195,714,159 of purchases at wholesale, made for patrons since the association began business. It is also of interest that the net worth of the Eastern States Farmers Exchange, which amounted to \$1,533,732 on December 31, 1934, has been built up by annual increments retained from operations.

SOURCES OF LOANS

Farmers' purchasing associations customarily obtain their capital for operations and facilities through loans from banks for cooperatives and other sources. Such loans are required for long-term financing of facilities or for emergency or short-term financing for operating purposes. To obtain loans, associations give their notes for the amounts required, secured by the pledge of facilities or other collateral. Some operating loans may be unsecured. Cooperatives that are financially sound are usually able to obtain short-term loans on unsecured notes but practically all long-term loans are obtained on the security of mortgages on real estate or other property. In most instances associations are required to furnish collateral on all loans whether for long or short periods.

The Farm Credit Act of 1933 enabled cooperative purchasing associations to obtain working capital loans from the banks for cooperatives which were established under the provisions of the Act. Under the Farm Credit Administration, which was established in 1933, there are 12 regional banks for cooperatives located in the 12 land bank districts (fig. 15), and a Central Bank for Cooperatives located in Washington, D. C. These banks are empowered to make loans to farm cooperatives. Loans amounting to less than \$500,000 are usually handled by the regional banks for cooperatives. The Central Bank for Cooperatives handles loans of \$500,000 or more and in some cases makes loans, regardless of amount, to associations which operate in more than one of the 12 districts.

The banks for cooperatives operate in close conjunction with other units of the Farm Credit Administration such as the production credit corporations, land banks, and intermediate credit banks. One board of directors controls the affairs of these credit agencies in a particular district. The Central Bank for Cooperatives, however, has a separate board of directors. The activities of these agencies are directed toward furnishing the maximum amount of financial service to agriculture.

The basic requirement of the banks for cooperatives in making loans to a cooperative purchasing association is that the association conform to the definition of a cooperative established by the Agricultural Marketing Act as amended by the Farm Credit Act of 1933 (sec. 55), and the Farm Credit Act of 1935 (sec. 12). The definition as amended reads as follows:

(a) As used in this act, the term "cooperative association" means any association in which farmers act together in processing, preparing for market, handling, and/or marketing the farm products of persons so engaged, and also means any association in which farmers act together in purchasing, testing, grading,

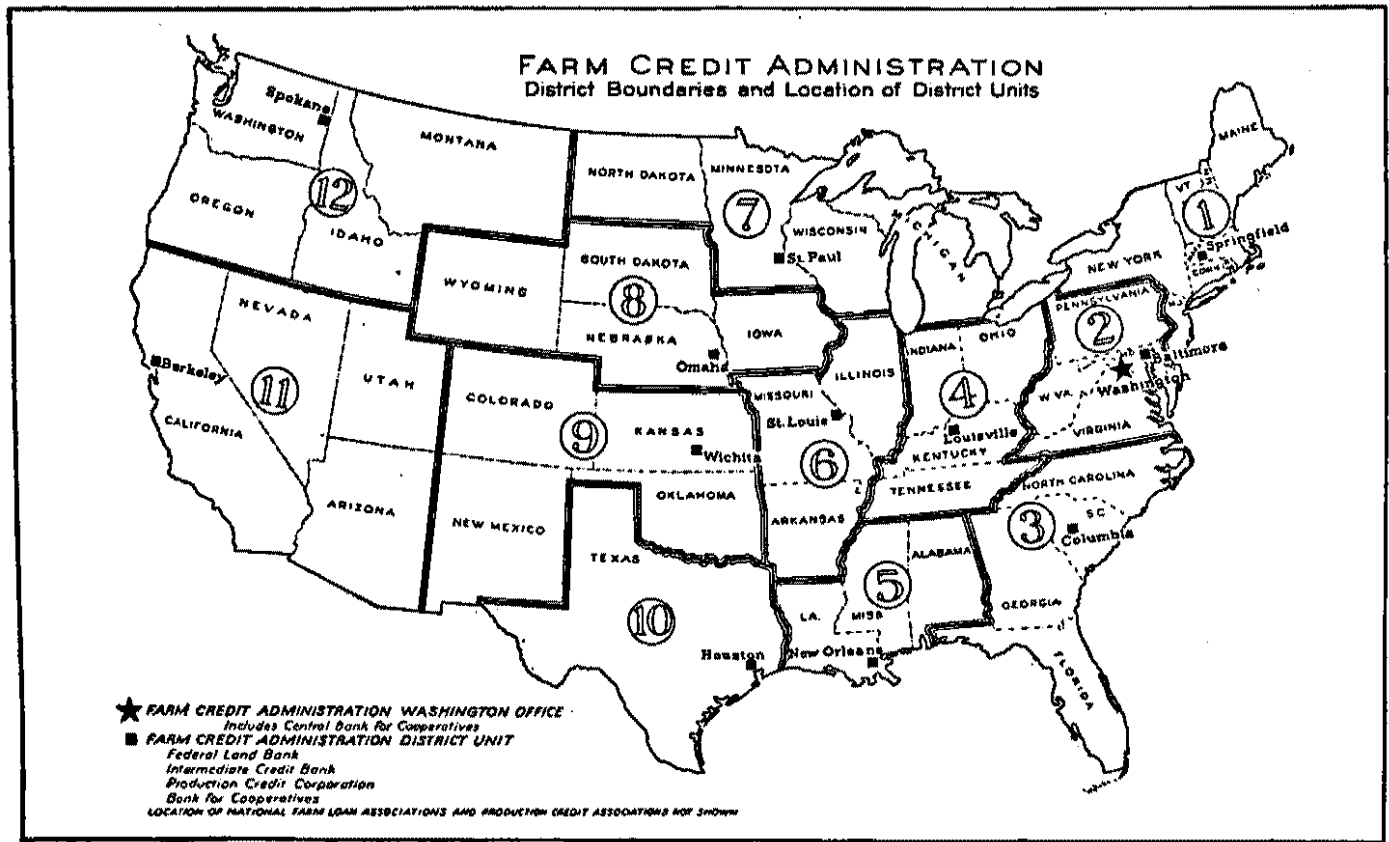


FIGURE 15.

processing, distributing, and/or furnishing farm supplies and/or farm business services: Provided, however, that such associations are operated for the mutual benefit of the members thereof as such producers or purchasers 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; and

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 farm products, farm supplies, and farm business services with or for nonmembers in an amount greater in value than the total amount of such business transacted by it with or for members. All business transacted by any cooperative association for or on behalf of the United States or any agency or instrumentality thereof shall be disregarded in determining the volume of member and non-member business transacted by such association.

Under the Farm Credit Act of 1933 loans from the banks for cooperatives to cooperative purchasing associations were restricted to loans for operating capital purposes; such as, for example, the financing of inventories of farm supplies. The Farm Credit Act of 1935 permits the banks for cooperatives to make physical facility loans up to 60 percent of the appraised value of all the collateral taken as security for such loans. A cooperative purchasing association may now borrow the full cost of the facility to be constructed or acquired provided it gives sufficient additional collateral.

The banks for cooperatives now offer practically the same financing services to cooperative purchasing associations as to cooperative marketing associations. Under the 1933 act, the interest rate on operating capital loans, except those secured by commodities, is fixed as nearly as practicable at 1 percent in excess of the prevailing interest rate paid by production credit associations to the Federal intermediate credit bank of the district. It is restricted, however, to a maximum of 6 percent a year. Interest is charged only on the unpaid principal and for the time that principal is actually outstanding. The rate as of July 1, 1935, was 3 percent a year. The interest rate on loans for physical facilities 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 members of national farm loan associations at the time the loan is made. The maximum, however, is 6 percent. The rate as of July 1, 1935, was 4 percent a year.

The Farm Credit Act of 1935 also enables the banks for cooperatives to make loans to associations of farmers furnishing farm business services in connection with insurance, power, transportation, and other farm needs. This provision affords further financial assistance to cooperative purchasing associations which may provide such services.

SOME FACTORS ESSENTIAL TO EFFICIENT OPERATION

COOPERATIVE purchasing associations for farmers cannot afford to disregard rules of good business procedure such as the following: (1) The association must meet a definite need; (2) the structure must be adequate and flexible; (3) the association must be supported and controlled by its membership; (4) the volume of business must be large enough for efficient operation; (5) the management must be capable and conscientious; (6) the business policies of the association must be sound.

NEED FOR AN ASSOCIATION

No cooperative purchasing association should be organized unless there is a definite need which justifies its existence. An association may be needed in a community where margins taken by dealers are greater than farmers can afford to pay for the essential services involved, or where a type of service better suited to the needs of the farmers can be furnished cooperatively. An association should not be organized simply to satisfy the vanity or enthusiasm of the organizers, or merely to cultivate a "get-together" spirit. It must contribute to the material well-being of the community. The social benefits which accompany cooperation are to be derived only when the association fills an economic need. It would be disastrous to establish a cooperative association if the economic factors were not suitable for its success.

In some communities the services which might be performed by a cooperative purchasing association are already being adequately supplied by commercial agencies. In such communities the possible value of cooperative effort cannot easily be determined. As one cooperative manager has said, "If facilities provided by commercial operators are already adequate, and if they serve the best interests of producers within that territory, then it is not only economic waste but an invitation to financial disaster to organize a cooperative that duplicates or overlaps the already adequate facilities."

Before organizing an association, therefore, definite attention should be given to the questions, "Is an association needed?" and "What will be the beneficial results if an association is established?"

To express this differently, "Will the benefits cooperators can reasonably anticipate show returns which will warrant the effort and risk involved?" Highly efficient commercial establishments of the chain-store type do not establish a local unit until they have given serious consideration to all factors that would bear on the prospective success of a new unit. Cooperatives must follow such well-established principles of good business procedure if they are to succeed. The kind of information which should be obtained as a basis for setting up an association is discussed more fully in the section on suggestions for organizing farmers' cooperative purchasing associations.

ADEQUATE AND FLEXIBLE STRUCTURE

It is impossible for an association to give full satisfaction unless its structure is adapted to meet the particular needs of the area and the social conditions under which it is to function; therefore, no simple pattern of structure can be followed by all purchasing associations. In certain areas there is a strong sentiment in favor of establishing local associations which can be member units of a federated wholesale purchasing association. In others, there is a preference for setting up directly a large-scale regional association which will, in turn, establish local facilities for distribution. In some sections it may be desirable to have the cooperative purchasing work carried on as a department or subsidiary of a marketing association; while in others, it may seem more desirable to have an independent cooperative purchasing organization. Where a separate department or subsidiary is set up, care should be taken to provide that it will carry its own cost of operation and administration. Furthermore, its earnings should be clearly segregated. In some regions it is preferable, because of the laws of the State and the extent of cooperative information, to set up associations on a nonstock membership basis, while in other sections, the stock type of association is more desirable.

A satisfactory structure will, first, meet the requirements of the situation; and, second, adapt itself to the changing needs of its membership. Its aim should be to insure control by the members through a well-chosen management which will have sufficient authority to operate efficiently. Any cooperative purchasing structure, in the words of a prominent cooperative executive (37, p. 153), must provide for orderly government and avoid mob rule.

[The structure] must provide ways of qualifying for membership and of enabling members to exercise their franchise so that they control the policies of their association through the election of directors in whom lies the responsibility for the conduct of the business.

SUPPORT AND CONTROL BY MEMBERS

The members of a cooperative purchasing association must feel that it is their own association and must take pride in its development. Their loyalty must not be blindly based on the idea that the association can do no wrong; it must be to the association and not to any group of officials, unless the officials put the interest of the association above personal advancement. It is the member's obligation to make the organization into one that justifies his full patronage. It must be an intelligent and vigilant loyalty which will see that the association functions in the member's behalf. Membership in a cooperative association places definite responsibilities on each member, especially in the important duty of electing directors, in order that the association may achieve the results expected from it by the members as a group.

In order to keep a membership loyal, it is necessary to keep it intelligently informed on the affairs of the association. While it is not necessary to consider every member as an employer, yet in a broad way, all the members through their elected representatives are the ultimate employers and have a right to full and continuous information on the affairs of their association. The entire structure of an association and its policies must be designed to promote the satisfaction of the membership. An executive of a large-scale cooperative purchasing association, in commenting upon the above discussion, has analyzed these several relationships as follows:

The duties of members, directors, and management are distinct. The directors elected by the member patrons are the policy-forming section of the structure. The management is responsible to the directors for the administration of the cooperative's affairs. As the business grows, it becomes necessary for boards large enough to be representative of the membership to delegate the more intimate contact with the management to an executive committee. Responsibility is not lost by such a device. Control is more secure. The management is responsible to the executive committee, the committee to the full board, and the board to the membership. Sound administration is difficult when the board and the management, or paid staff, are not distinct one from the other.

Although the above comment applies particularly to a large-scale purchasing association of the centralized type, it is generally applicable to any cooperative structure.

Further discussion of membership policy is unnecessary here other than to call attention to the fact that an association should provide means whereby the members are given an opportunity to indicate how the association can best serve their interests. It should be the

responsibility of the management to encourage members to feel that they have an interest in the success of the association. One important means of achieving this is to show the membership by actual performance that the association operates continuously in its interest.

VOLUME ENOUGH FOR EFFICIENCY

In these days of vigorous competition an organization must be large enough to afford capable administration. The advantage of having an adequate volume of business has been demonstrated in the experience of all successful cooperative associations. Very small organizations are sometimes handicapped in obtaining competent management, in arranging quantity discounts, in procuring high quality products, and in many other ways which tend to cut costs per unit of operation. A competent manager can handle a large business as easily as a small one, for with an ample volume of business the work can be departmentalized.

In a large-scale association members can employ a competent manager at a low cost per member, or per unit of volume, while in a small association the individual member's cost of hiring an equally competent manager would be excessive. A large-scale association is able to obtain more favorable price quotations from manufacturers or wholesale sources of supply, for its volume of business makes its orders attractive. Furthermore, a large-scale association with a stable body of buying members may be able to undertake manufacturing operations and thus obtain supplies at lower cost. A large-scale association can develop an advertising and publicity program, which could not be afforded by a small association at a cost as low per dollar of goods handled. Moreover, a large association at a small cost per dollar of supplies sold, can provide research facilities to improve business methods and to determine needs and best sources of supplies. The fact that costs per unit of operation tend to decrease with increases in volume of business explains the steady development of large-scale cooperative purchasing associations in the United States.

It is the view of some cooperative leaders that cooperatives in general have laid too much stress on building up volume. Obviously, the importance of volume can be overemphasized, for large organizations are not necessarily efficient. The proper size of a cooperative must be determined by economic and social conditions. With this qualification, the significance of adequate volume as a factor in successful operation cannot be denied.

CAPABLE AND CONSCIENTIOUS MANAGEMENT

The success of a cooperative purchasing association largely depends upon the manager, for management is not a routine job. The manager must have business knowledge and experience, resourcefulness, and

tact. He must constantly guard against unwise use of capital funds, unsatisfactory supplies, improper extension of credit, excessive inventories, and lack of merchandise turnover. The manager must be capable not only of dealing with business men and business problems, but also of working with the patrons and directors of the association. The manager must be more than a job holder; he must see that all of the elements in the organization give the best possible service, and set an example of the real spirit of cooperation. He must be willing to make as much sacrifice for the association as he demands on the part of members.

The manager of an association should look upon himself as only a part of the management. The board of directors must also share in the managerial function to the extent of its responsibility to the membership for the administration of affairs. The manager should feel that it is the rightful duty of the board of directors to adopt association policies and to assist him through advice and criticism in making them effective. Some cooperatives have been handicapped by having officious boards of directors who refuse to place sufficient authority in the hands of responsible employees; while in many other instances, boards of directors have become but rubber stamps for managers. Neither situation is healthful. A manager with tact and fairness ordinarily will not be handicapped by his board of directors; on the other hand, a live board of directors will do much to develop sound policies and a live membership, which are necessary for any association.

It is the duty of the board of directors to determine carefully whether the manager is carrying out the policies of the association. It is the duty of the manager to operate the association in an efficient manner to the general satisfaction of the directors and the membership. He should provide full and continuous information to the board of directors on the affairs of the association, and should provide to the members such information as will enable them to understand clearly how the association is operating.

SOUND BUSINESS POLICIES

The final and most important need of a cooperative purchasing association is wise direction. The business policies of an association must gain the respect and confidence of the members and the community. They should be looked upon only in a general way as rules of action. They should rather be considered as basic principles of operation which should determine a course of action. While an association should have clearly understood policies, these policies should permit the association to operate in a flexible manner. Any attempt to govern a manager by providing detailed regulations results in disaster.

The business policies of an association are molded by the directors, management, and membership, and relate to all problems which confront an association. In the beginning, the policies of an association are generally expressed in the documents of organization. Later, the policies are made more tangible as the association is confronted with definite problems. One authority has classified policies into three groups: General, major, and departmental (15). The general policies set forth the ideals which are the animating force of the association. For example, the general policies of one large-scale cooperative purchasing association are expressed as follows in its bylaws:

(1) To encourage, introduce and apply improved business methods in agriculture and to promote cooperation with national, sectional, State, county, and local organizations which are engaged in the work of developing agricultural interests concerned in cooperative buying and selling.

(2) To encourage, introduce, and apply better and more economical methods in the purchase of farmers' supplies and products.

(3) To secure efficient and economical methods in the grading, packing, transporting, marketing, and advertising of farm products.

(4) To effect economical methods of distribution.

(5) To develop business cooperation among agricultural interests and to encourage a cooperative spirit on the part of the public.

(6) To encourage and promote a closer mutual relationship between agricultural interests and industrial interests and the consuming public, and a better understanding of the problems pertaining thereto.

The major policies are developed for the purpose of directing the association toward the goal established by the general policy and may be divided into internal policies which deal with such matters as finances, organization, and personnel, and external policies which relate to quality, credit, price, public relations, and advertising. Many of these policies are stated in a general way in the documents of organization, but authority is customarily given to the boards of directors and the management to put them into practical effect. The major policies are determined, to a large extent, by the board of directors and management, and are subject to the general consent of the membership.

Departmental policies designate the way in which the association segregates and combines its functions and the methods and systems used in the exercise of these functions. Departmental policies are subordinate to major policies, of course, just as major policies are subordinate to general policies. It is necessary that the three kinds

of policies be coordinated. The departmental policies are largely determined by the manager and his staff, but they are also under the general jurisdiction of the membership through the board of directors.

By formulating policies so that they will be clear and understandable, an association may develop for itself a definite and permanent character which will assure efficient direction of its operations, and insure the good will of its members and the community.

SUGGESTIONS FOR ORGANIZING FARMERS' COOPERATIVE PURCHASING ASSOCIATIONS

THERE IS no stereotyped method of organizing cooperative purchasing associations, since every situation has its own peculiarities. Often cooperative purchasing can be most advantageously carried on in connection with cooperative marketing. Under some conditions it is desirable to organize a purchasing association for a local community; again it is preferable to set up an organization to serve an entire region. If the association is to engage in cooperative marketing, it will be necessary to study the marketing problems confronting the farmers of the area, so that the proposed organization may be adapted to render efficiently both purchasing and marketing service. Information on the organization of marketing associations may be obtained from the Cooperative Division of the Farm Credit Administration and from State agricultural colleges and departments of agriculture.

No cooperative association organizes itself. There must be leaders who have the initiative and ability to make plans and to put these plans into effect. Generally, associations for the purchase of farm supplies are formed by a number of farmers with a definite purchasing problem who have learned of the experiences of successful cooperatives.

ORGANIZATION OF SINGLE-UNIT PURCHASING ASSOCIATIONS

Assuming that there is such a group of interested farmers who believe that a cooperative purchasing association can be profitably established in their area, let us consider the general steps that should be followed. In the first place, it will be desirable to appraise carefully the factors that will determine the advisability of organizing an association, the nature of the association to be set up, and the probable degree of its success. Such study is necessary to provide a working basis for perfecting the association. Answers to such questions as the following are essential:

(1) Are the farmers of the area dissatisfied with the quality of available supplies or services?

(2) Are other agencies in the area operating inefficiently? Are such agencies making excessive profits?

(3) Do the farmers of the area believe in cooperative action? What lessons are to be drawn from past experience in cooperative action in the area?

(4) Can competent management be obtained at reasonable cost?

(5) Are there satisfactory wholesale sources of supplies? What supplies and services are available from wholesale cooperative associations? What commodities can be handled with the greatest opportunity for saving?

(6) Can sufficient volume of patronage be obtained to effect economical operation?

(7) Can adequate facilities be purchased or leased on satisfactory terms?

(8) How much operating capital will be needed? What financial services are available?

(9) How much capital can be raised by the use of common stock? Preferred stock? Membership fees?

Although all of these questions bear upon each other, each must be answered candidly in a manner that will indicate the advisability of establishing an association. There should be careful study of successful cooperative associations providing services similar to those which would be expected of the proposed organization. In this the group may find helpful bulletins from the Cooperative Division of the Farm Credit Administration or from the State colleges of agriculture. Assistance should also be requested from county agricultural extension agents, vocational agricultural teachers, extension marketing economists of State agricultural colleges, and others who may be in a position to help in organizing the association. Aid in forming a local purchasing association can usually be obtained from regional purchasing associations in the area.

Perhaps the most important question confronting the organizers of a cooperative purchasing association is whether or not sufficient patronage can be obtained to assure economical operation. This question can be answered only by ascertaining the buying needs of the farmers and their attitudes toward cooperation.

Assuming that the organizing group, after careful consideration of this and other questions, believes that it is desirable to set up a cooperative purchasing association, the next step is to call a meeting of all farmers who may be expected to make use of the proposed organization. A carefully prepared report, either oral or written, indicating the possibilities of an association if operated efficiently should be presented at this meeting. After the report has been given, the meeting should be opened for general discussion. If there is considerable sentiment favorable to the establishment of an association, an attempt should be made to determine the quantity and value of the various supplies which might be purchased annually from the

proposed association. It is desirable to have farmers indicate whether they would be interested in joining the association and whether they would be willing to subscribe to a share of stock at nominal cost or to pay a membership fee.

If there is a good representation of farmers and it is clear that the volume of business assured will be enough for efficient operation, the group should proceed immediately to the next step—the selection of an organization committee authorized to form and incorporate the association. This committee should be composed of men who are definitely interested in the success of the organization and who are capable and experienced in cooperative matters. If the attendance at the first general meeting does not adequately represent the area, it may be necessary to hold a second meeting to determine whether it would be possible to establish the association on a sound basis.

The primary duty of the organization or incorporating committee will be the preparation of the articles of incorporation and tentative bylaws (21). The committee should have available sample documents of organization used by successful associations. Most States have cooperative statutes and model bylaws which are helpful in the preparation of these documents. It is common for State agencies to supply legal advice in drawing up the articles of incorporation.

It is important that the greatest care be used in the preparation of the organization documents in order that they may be drawn so as not to hamper the association in subsequent expansion or possible combination with other associations or in meeting the requirements of legislation, both State and Federal.

After the committee has prepared the organization documents, a meeting of the membership should be called for the purpose of examining and approving the proposed articles of incorporation and bylaws. When these documents have been approved the organization committee can apply to the proper authorities for incorporation. The actual procedure in incorporation usually consists in having the incorporating directors sign the approved articles of incorporation before a notary public and send copies to the State corporation commissioner or other appropriate officer with the necessary filing and license fee payment. The cooperative law of the State will determine the exact procedure to be followed in incorporating the association. After incorporation a membership meeting should be called for the purpose of ratifying the bylaws and electing directors.

An effort should be made to select from the men available those whose business ability and experience best fit them to serve as directors, for the success or failure of an association will depend largely upon the capacity and energy of this group. Those responsible for the movement should also see that directors are chosen who will

work together successfully. It is not safe to assume that snap judgment nominations at the organization meeting will procure such a board. The first meeting of the board of directors usually occurs immediately after the first membership meeting. The directors may then proceed to organize as a board, electing from their number a president, vice president, secretary, and treasurer.

The most important immediate problem faced by the board is the selection of a manager. (Obviously, a paid manager, responsible to the directors, should not be a member of the board.) They should choose a man who is honest, capable, experienced, tactful, likeable, and interested in the success of the organization, for a competent manager is an indispensable factor in successful operation.

The association is now ready to commence business operations. Its success will depend for the most part upon the factors already discussed in the section on factors essential to efficient operation.

FORMATION OF REGIONAL COOPERATIVE PURCHASING ORGANIZATIONS

So far attention has been directed only to the formation of single-unit cooperative associations. A regional cooperative association of the centralized type is organized in much the same way as a local association, except that since the territory is much larger, the organization and incorporating committees should represent all the different sections, conditions, and interests. One of the chief problems here is the provision of adequate local operating facilities. It is generally desirable for a centralized purchasing association to plan a system of facilities for local distribution before business operations are started. Obviously, conditions should be studied carefully before local distributing facilities are set up. It may be that arrangements can be made for distribution of supplies at the car door combined with branch warehouses at points of heavy membership. As the organization gathers experience and builds up its operating capital, it can work out a comprehensive system of local distribution. For example, certain well-established associations make an intensive survey of local conditions before offering services at any point in the general territory served.

The formation of large-scale cooperative purchasing associations, however, is usually brought about by the desire of a number of local associations to set up an agency which will provide them with an adequate wholesale source of supply. Such agencies as the State agricultural colleges and State departments of agriculture and the Cooperative Division of the Farm Credit Administration can be called upon for assistance in determining the feasibility of such action.

In the formation of regional associations of the federated type, representatives of each of the local associations usually come together to appoint a committee to determine the type of wholesale organization that will best serve their needs. Such federations provide that locals organized subsequently in the area may become members.

The existence of a successful large-scale purchasing association greatly simplifies the organization of local cooperatives in its territory, for they are thus assured of a satisfactory source of supply. Such associations are also in position to assist in the selection of management, in the establishment of a bookkeeping system, and in many other ways during the difficult period when the local is becoming established.

Regardless of whether the regional association is set up on the centralized or federated basis, it should be organized in accordance with the general procedure described above except that the preliminary work in the case of a large-scale organization is necessarily more elaborate.

FIRST OPERATIONS

The crucial period of a new association occurs when it begins to operate. If it has been carefully set up, without extravagant promises of success, and if it is well managed, the way is clear for efficient operation. Caution should, however, be directed against too early and too rapid expansion. It is essential that the association develop on a conservative basis. For example, it may be advisable to handle only a few commodities until the cooperative can demonstrate its ability to give satisfactory service. Successful cooperative organizations have generally started with simple operations and limited personnel, and have expanded as their strength increased. The general difficulties faced by cooperative associations have been well summarized by Jones (23). The following causes for lack of success are given: (1) Inadequate or slovenly accounting practices; (2) obscure policies regarding budgets of income and expense; (3) inadequate reserves; (4) inexperienced or incompetent management; (5) too much concern for nonmembers; (6) faulty membership relations policy; (7) inadequate information to members for evaluation of achievements and problems.

AGRICULTURAL COOPERATIVE PURCHASING IN OTHER LANDS

THE EXTENT of cooperative purchasing by farmers in other lands is not generally realized in the United States. A brief description of the world-wide aspect of this movement will indicate the extent to which the cooperative method of purchasing agricultural supplies has developed in practically every country and under various types of government.

ENGLAND

Cooperative purchasing of agricultural supplies has long been customary in England (18, pp. 164-190). In 1929 agricultural "requirements" societies, as agricultural cooperative purchasing associations in England are called, did a total business of \$30,486,372. (In this section values expressed in foreign currencies have been changed to dollar valuations at going rates of exchange.)

The first English requirements society was organized in Manchester in 1867. The Aspatria Agricultural Cooperative Society, in Cumberland, has operated continuously since 1870. In 1930 there were 111 requirements societies classified as follows: County societies, 24; half-county societies, 19; local societies, 68. Of the county societies, three were operating on a relatively large scale with a combined volume of purchasing business amounting to \$2,491,202. The county and half-county requirements societies and their branches cover England "with reasonable completeness." The local societies operate only for single communities. There are approximately 40,000 members in these requirements societies and 25,000 nonmembers purchase more or less regularly from them.

* * * there are few farmers, even in remote districts, who cannot, if they choose, become members of a relatively large and well-established cooperative undertaking for this purpose and be sure of receiving satisfactory service (18, p. 172); * * *

While the requirements societies are primarily engaged in the purchase of agricultural supplies, many of them also perform marketing services. In a similar way, some associations which are primarily marketing organizations engage in the cooperative buying of farm supplies. A large number of these societies are affiliated with the National Farmers Union.

It is of interest that the agricultural requirements societies do not conflict with the well-established consumers' societies. The agricultural societies engage in furnishing supplies used directly in farm operations; such as feedstuffs, binder twine, seeds, fertilizer, coal, implements, hardware, and machinery. They do not, with a few exceptions, do a general retail business. Many of the requirements societies, however, are linked to the consumers' cooperative movement through a common wholesale source of supply—The Cooperative Wholesale Society (The C. W. S.)—which, in 1933, reported a total business of \$352,053,094. The C. W. S. manufactures feedstuffs, oil cake, and binder twine, and deals in coal, seeds, fertilizers, and a long list of other agricultural supplies (7) on a wholesale basis. The C. W. S. also assists some requirements societies through its auditing and general services. During the last year a committee representing the C. W. S. and the National Farmers Union has been

attempting to coordinate further the agricultural business of the C. W. S. with the interests of the requirements societies (17, 1935, p. 49). It is expected that a special department of the C. W. S. will be set up to serve this end.

IRELAND, SCOTLAND, AND WALES

The Irish Agricultural Wholesale Society, with headquarters in Dublin, was established in 1898 to serve as a general wholesale source of supply for Irish agricultural requirements societies and creameries. The Irish Agricultural Wholesale Society handles seeds, artificial manures, feedstuffs, agricultural implements, and such domestic supplies as groceries and clothing. The total value of business, in 1929 was \$4,974,322, of which \$666,792, or 13 percent, represented sales of domestic supplies. The retail sales of local requirements societies and creameries in the Irish Free State and northern Ireland amounted, in 1929, to \$8,221,366 (19).

Agricultural requirements societies in Scotland commonly handle household goods and engage in egg merchandising. In 1931 these organizations distributed agricultural supplies valued at \$1,769,459 and domestic supplies valued at \$122,595. Creameries and miscellaneous societies, in addition, handled farm supplies valued at \$74,899. The Scottish societies are generally smaller than those in England and it is common for them to handle supplies on an agency basis. These societies have not developed a wholesale source of farm supplies. The Scottish Cooperative Wholesale Society, Ltd., has not had as close connection with agricultural requirements societies in Scotland as exists between the Cooperative Wholesale Society in England and the requirements societies in that country (20).

Requirements societies have long been the backbone of agricultural cooperative effort in Wales. Many of these societies have operated for more than 20 years. They generally market farm produce and distribute limited quantities of household goods. Although there is no close connection between these societies and the consumers' cooperative movement, it is significant that 40 out of 61 requirements societies, in 1931, were members of the (English) Cooperative Wholesale Society, and purchased through it supplies valued at approximately \$906,000 (20). The total retail business of the requirements societies in Wales amounted to \$3,974,900 in 1932 (47). Household supplies represented about 17 percent of the total purchasing business.

DENMARK

The cooperative purchase of agricultural supplies in Denmark was started in the seventies (5, 12). It was encouraged in the eighties by the Cooperative Wholesale Society of Denmark which established a special department for seeds and fertilizer. In 1901 a separate

wholesale association took over the fertilizer business. Separate wholesale associations have also been developed for feed, cement, coal, machinery, and implements. According to the 1935 Year Book of Agricultural Cooperation (*11, p. 199*) in 1933, there were 2,837 agricultural purchasing societies (not including consumers' societies which also serve farmers) with a total business for the year of \$23,-380,000 and a total membership of 152,875 individuals.

The (Danish) Cooperative Wholesale Society distributes seeds through cooperative stores and agricultural societies. About one-fourth of the wholesale seed business was handled by the Cooperative Wholesale Society in 1923. The seed so distributed is obtained largely from the Danish Farmers Cooperative Association for Seed Growing. Christensen has maintained (*5, p. 64*) that:

Nowhere in European agriculture has the gulf between the producer and consumer been so successfully bridged as in the Danish seed industry. The producers of good seed are guaranteed a market and consumers are guaranteed well-grown and clean seed of superior strain.

Three central organizations engage in the cooperative distribution of feed. The Jutland Cooperative Association for the Purchase of Feeding Stuffs, the largest of these organizations, had a membership in 1922-23 of 818 local associations which had an annual business of over \$13,000,000. According to Christensen (*5, pp. 68-69*):

Membership in the central association is made up chiefly of local feed-purchasing associations; but in some cases cooperative creamery associations, consumers' stores, and other associations which supply their members with feeds, may be members. The local association is pledged to take its entire supply of feedstuffs from the central association for a period of 5 years. * * * The individual members under written agreement to the central association are pledged to take their consumption of feeds (excluding home-grown grains) from the local association.

These feedstuff societies handled 67.4 percent of the total net imports of feedstuffs in 1933 (*11, p. 198*).

The Danish Cooperative Fertilizer Supply Association was formed in 1901. This central association, in 1922, supplied fertilizer to 1,525 local fertilizer associations with a total membership of 74,000. The individual members sign contracts to buy all commercial fertilizer for a 10-year period through the central association. In 1933 this association handled 35.2 percent of the total consumption of fertilizers (*11, p. 199*).

The following paragraph taken from the 1933 People's Year Book (*3, 1933, p. 122*) shows clearly the cooperative relationships of the Danish farmers.

A typical Danish farm is now connected with the outside world through a network of cooperative agencies. The farmer buys

his necessities at his cooperative retail store: He borrows money and places his savings in a cooperative bank; his fertilizers, fodder, seeds, etc., are obtained from cooperative buying and import associations; his cement comes from the cooperative cement factory, and his electricity from a cooperative power plant. He delivers his milk to the cooperative dairy, his pigs to the cooperative slaughterhouse, his eggs to the Danish Cooperative Egg Export Co., and his cattle to the Danish Cattle Export Cooperative. It is usual for a farmer to be a member of at least half a dozen cooperative societies covering the entire range of his economic needs.

NORWAY, SWEDEN, AND FINLAND

In Norway nearly one half of the agricultural producers are members of agricultural requirements societies and nearly 40 percent are members of consumers' cooperative societies. The requirements societies distribute approximately three fourths of the Norwegian consumption of fertilizer and feed (17, 1933, pp. 92-93).

Agricultural requirements societies have existed in Sweden since about 1900. The Swedish Farmers National Federation, formed in 1905, initiated a movement in 1930 to reorganize the cooperative supply of agricultural requirements on the basis of 19 central unions with warehouses. The unions bind themselves to purchase from the National Federation all of their requirements in certain types of fertilizer, imported feeding stuffs, Swedish oil cake, and certain other feeding stuffs. The national and regional organizations handle about one fourth of the Nation's agricultural requirements business and sell to about one fourth of the farmers. While the Wholesale Society Kooperativa Forbundet sells certain agricultural requirements through cooperative stores, it works with the National Federation and encourages the formation of separate requirements societies with membership in the National Federation (10).

In Finland, which is predominantly a rural country of small landholders, the supply of agricultural requirements is to a large extent a function of the well-developed consumers' cooperative societies (31, pp. 89-103). The cooperatives are served by two large-scale wholesale agricultural supply societies, "Hankkija" and "Labor", which, in 1928, had combined sales of approximately \$12,636,000. Hankkija transacts 40 percent of the trade in manures, 30 percent of the trade in feeding stuffs, and 60 to 70 percent of the trade in seeds. Ninety percent of the country's wholesale trade in creamery machinery and 45 percent of the wholesale trade in agricultural machinery is handled by this wholesale farm supply association.

GERMANY, FRANCE, AND ITALY

The cooperative purchase of farm supplies is well established in Germany, where there are 3,443 sale-and-purchase societies affiliated with the National Union of German Agricultural Cooperative Societies Raiffeisen which embraces 80 percent of all agricultural cooperatives in Germany. These purchase-and-sale societies buy cooperatively manures, feedstuffs, seeds, coal, and agricultural machinery (17, 1934, pp. 237-240).

According to Tardy (42), in France,

agricultural cooperation for joint purchase and sale is represented by syndicates which are really groups for the study and defense of professional interests, and cooperative societies, properly so-called, which have been formed more recently than the syndicates.

There are approximately 15,000 agricultural syndicates. A large proportion of them engage in the joint purchase of farm requirements. There are also several hundred cooperative societies for collective purchase formed by unions of syndicates.

Cooperation plays a very important part in the life of the Italian farmer as described by Walter (44, pp. 20-27) and Cotta (9, pp. 44-53). Consumers' cooperative societies flourish in the agricultural provinces. While farmers give general support to the consumers' societies, they have separate societies, "Consorzi Agrari" for the purchase of farm requirements and the sale of farm products. There were, in 1932, about 540 agricultural societies with a membership of approximately 500,000 handling an aggregate business of around \$61,500,000. The requirements societies have established about 18 cooperative fertilizer factories which have a capacity of one third of the national consumption. These societies developed their own agricultural wholesale society as early as 1892.

OTHER COUNTRIES

The cooperative purchasing of agricultural supplies is a movement which may be considered world-wide in extent. Practically every country yields illustrations of joint effort in this regard. The following countries, among others, have healthy agricultural cooperative purchasing developments: Bulgaria, Canada, Czechoslovakia, Egypt, Holland, Hungary, India, Japan, Jugoslavia, Latvia, Lithuania, Poland, Rumania, and Russia (17, 22, 32, 36). The ability of agricultural producers to join together for their mutual interest in acquiring supplies and services is proven by the universal character of the movement.

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APPENDIX A

FARM SUPPLY BUSINESS REPORTED BY REGIONAL PURCHASING AND MARKETING ASSOCIATIONS¹

Association and Farm Credit Administration district ²	Address	Value of farm supplies sold ³		Value of farm products marketed	Period covered ⁴	Comments
		Wholesale	Retail			
District No. 1:						
Aroostook Federation of Farmers.	Caribou, Maine.....		\$343, 438		1934-35	
Burlington County Supply and Produce Company.	Mount Holly, N. J.....		377, 184	\$63, 308	1934	
Central Jersey Farmers Cooperative Association, Inc.	Hightstown, N. J.....		102, 474		1934	
Cooperative Grange League Federation Exchange, Inc.	Ithaca, N. Y.....	\$24, 258, 347	16, 011, 107	2, 500, 000	1934-35	Operates in New York, New Jersey and northern Pennsylvania. "Sales at retail" represent sales of 139 G. L. F. service stores. The wholesale sales include wholesale value of retail sales. For further information see pp. 8, 16, 17, 35-38.
Eastern States Farmers Exchange.	Springfield, Mass.....		12, 386, 498		1934	Operates in New England, Delaware, parts of Pennsylvania and Maryland. For further information see pp. 8, 16, 17, 35, 46.
Gloucester County Agricultural Cooperative Association, Inc.	Woodbury, N. J.....		144, 219	241, 357	1934	
Merrimack Farmers Exchange, Inc.	Concord, N. H.....	100, 000	1, 308, 607		1934-35	Data for period June 1, 1934 to May 31, 1935.

¹ The term "regional" is here used to define an area larger than a county.

² Several associations which were organized to serve 1 county have extended their operations to adjoining counties. Not all associations of this type could be included in this table.

³ The principal farm supplies handled are feed, seed, fertilizer, petroleum products, and package supplies. Sales at wholesale represent purchases from associations by associations or cooperating dealers. Sales at retail represent amounts paid directly by farmers for supplies purchased through these associations.

⁴ The operating years usually ended on or near June 30 or Dec. 31.

FARM SUPPLY BUSINESS REPORTED BY REGIONAL PURCHASING AND MARKETING ASSOCIATIONS—Continued

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Association and Farm Credit Administration district	Address	Value of farm supplies sold		Value of farm products marketed	Period covered	Comments
		Wholesale	Retail			
District No. 1—Continued.						
Middlesex County Farm Bureau.	Waltham, Mass.....		\$885, 880		1934	Data for period Nov. 1, 1933 to Oct. 31, 1934.
Windsor County Farmers Exchange, Inc.	White River Junction, Vt.	\$5, 600	274, 400	\$38, 000	1934	
District No. 2: 5						
The Agricultural Corporation of Maryland.	Baltimore, Md.....	325, 000			1934	
Cooperative Farm Services, Inc.	Clarksburg, W. Va....	449, 693	525, 028	60, 000	1934	In addition, sales of household supplies amounted to \$18,000.
Cumberland Valley Cooperative Association.	Shippensburg, Pa....	23, 311	442, 899	202, 025	1934	
Eastern Shore Farmers Supply Co., Inc.	Onley, Va.....	796, 134			1934	Operates as subsidiary of Eastern Shore of Virginia Produce Exchange, Inc., on Eastern Shore of Virginia and Maryland. Data for period Dec. 1, 1933 to Nov. 30, 1934.
Producers Cooperative Exchange, Inc.	Richmond, Va.....	* 346, 643			1934-35	Data for period Aug. 1, 1934 to July 31, 1935.
Rockingham Cooperative Farm Bureau, Inc.	Harrisonburg, Va....		455, 395	50, 769	1934-35	In addition, sales of household supplies amounted to \$227,698. Data for period Aug. 1, 1934 to July 31, 1935.
Southern States Cooperative, Inc.	Richmond, Va.....	4, 000, 000	1, 000, 000	180, 000	1934-35	Operates in Virginia, parts of Delaware and Maryland, and in North Carolina in cooperation with the Farmers' Cooperative Exchange. Retail sales represent sales through S. S. C. service stores. For further information see pp. 16, 18 and 38.

FARM CREDIT ADMINISTRATION

Virginia Truck Growers Manufacturing Corporation.	Norfolk, Va.		100, 400		1934	
District No. 3: Carolina Cooperatives Consolidated.	Florence, S. C.		* 67, 000	490, 000	1934	
Exchange Supply Co.	Tampa, Fla.	329, 044			1934	Operates as purchasing agency for member associations of Florida Citrus Exchange.
Farmers Cooperative Exchange, Inc.	Raleigh, N. C.	990, 669		112, 490	1934-35	First year of operation. For further information see pp. 18 and 38.
Farmers Federation, Inc.	Asheville, N. C.		387, 495	273, 004	1934	Operates in 6 counties in western North Carolina.
Hastings Potato Growers Association.	Hastings, Fla.		230, 497	306, 993	1934-35	
Producers Cooperative Exchange, Inc.	Atlanta, Ga.		287, 703		1934	Operates in Georgia and part of South Carolina and Florida.
Sowega Fertilizer Corporation.	Adel, Ga.		98, 000		1934-35	Operates in southern Georgia and northern Florida. Started manufacturing operations in 1934.
District No. 4: [†] Farm Bureau Cooperative Association, Inc.	Columbus, Ohio	1, 488, 332	1, 997, 026	1, 169, 914	1934	Includes business of Ohio Farm Bureau Service Company which is being merged into the Farm Bureau Cooperative Association, Inc.
Indiana Farm Bureau Cooperative Association, Inc.	Indianapolis, Ind.	3, 130, 900	94, 928		1934	Does not include retail value of sales of 87 member county associations, which amounted to approximately \$7,000,000. For further information see pp. 15, 19, and 34.
National Cooperatives, Inc.	do	19, 202, 390			1934	Serves as bargaining agency for 7 regional associations operating in 20 midwestern and western States. For further information see pp. 15 and 20.

Data are not available for the Pennsylvania Farm Bureau Cooperative Association, Inc., Harrisburg, Pa., which has not yet operated for a full year.

* Unclassified.

[†] There are also in this district the Farm Bureau Milling Co., Inc., of Columbus, Ohio, and the Farm Bureau Oil Co., Inc., of Indianapolis, Ind., which serve State Farm Bureau purchasing associations as described on p. 15.

FARM SUPPLY BUSINESS REPORTED BY REGIONAL PURCHASING AND MARKETING ASSOCIATIONS—Continued

Association and Farm Credit Administration district	Address	Value of farm supplies sold		Value of farm products marketed	Period covered	Comments
		Wholesale	Retail			
District No. 4—Continued.						
Ohio Farmers Grain & Supply Association.	Fostoria, Ohio-----	\$1, 000, 000	-----	\$2, 250, 000	1934	
Ohio State Grange-----	Zanesville, Ohio-----	100, 000	-----		1934	
Tennessee Cooperative Supplies Association.	Columbia, Tenn-----	113, 947	-----		1934	
District No. 5:						
Central Strawberry Cooperative Association.	Hammond, La-----	170, 737	-----	416, 395	1934-35	
Farmers Marketing & Exchange Association.	Montgomery, Ala----	625, 402	-----	61, 571	1934-35	Retail supply business is done through local units.
Louisiana Farm Bureau Federation, Inc.	Baton Rouge, La----	295, 035	-----	104, 281	1934-35	
Mississippi Federated Cooperatives.	Jackson, Miss-----	409, 593	-----	85, 796	1934-35	
Mississippi Vegetable Exchange, Inc.	Crystal Springs, Miss.	* 45, 259	-----	115, 457	1934-35	Data for period Sept. 1, 1934 to Aug. 31, 1935.
Truck Growers Association, Inc.	do-----		* \$127, 467		1933-34	
District No. 6:						
Consumers Cooperative Association.	North Kansas City, Mo.	1, 776, 839	241, 872	-----	1934	Operates in Kansas and parts of Missouri, Nebraska, South Dakota, North Dakota, Colorado, and Utah. See pp. 19-20.
Equity Union Grain Co-----	Kansas City, Mo-----	27, 020	-----	882, 400	1934-35	Data for period May 1, 1934 to Apr. 30, 1935. Operates in Kansas.
Farmers Union Jobbing Association.	do-----	750, 000	-----	-----	1934	Operates in Kansas.

Illinois Farm Supply Co.	Chicago, Ill.	3, 378, 833			1934	Data for period Sept. 1, 1933 to Aug. 31, 1934. Does not include retail value of sales of 58 member companies, which amounted to \$6,729,834. For further information see pp. 20-21.
Missouri Farmers Association, Inc.	Kansas City, Mo.	2, 856, 179			1934	
M. F. A. Milling Co.	Springfield, Mo.	1, 861, 601			1934	Operates in Missouri, Arkansas, Oklahoma, Tennessee.
M. F. A. Oil Co., Inc.	Columbia, Mo.		546, 000			Data for period Nov. 1, 1933 to Dec. 1, 1934.
District No. 7: Central Cooperative Wholesale.	Superior, Wis.	301, 746			1934	Operates in parts of Michigan, Wisconsin, and Minnesota. In addition, sales of household supplies amounted to \$1,485,-810.
Cherry Growers Packing Co.	Traverse City, Mich.	158, 073		510, 023	1934-35	
Farm Bureau Services, Inc.	Lansing, Mich.	1, 670, 000	630, 000	100, 000	1934-35	
Farmers Union Central Exchange, Inc.	St. Paul, Minn.	2, 615, 519			1934	Data for period Nov. 1, 1933 to Oct. 31, 1934. Operates in North Dakota, Montana, parts of Wisconsin and Minnesota. For further information see pp. 14 and 40.
Fruit Growers Cooperative.	Sturgeon Bay, Wis.	160, 600		390, 000	1934	This association serves the sour cherry area of Wisconsin.
Great Lakes Fruit Industries.	Benton Harbor, Mich.		*185, 860		1934	
Land O'Lakes Creameries, Inc.	Minneapolis, Minn.	2, 082, 316		33, 000, 000	1934	Operates in Minnesota, North Dakota, South Dakota, Iowa, and nearby States. Includes feed sales amounting to \$652,-316. For further information see p. 21.

* Unclassified.

FARM SUPPLY BUSINESS REPORTED BY REGIONAL PURCHASING AND MARKETING ASSOCIATIONS—Continued

Association and Farm Credit Administration district	Address	Value of farm supplies sold		Value of farm products marketed	Period covered	Comments
		Wholesale	Retail			
District No. 7—Continued. Midland Cooperative Wholesale, Inc.	Minneapolis, Minn.	\$1, 751, 007	-----	-----	1934	Operates in Minnesota and Wisconsin. For further information see pp. 19, 20, and 34.
Minnesota Farm Bureau Service Co.	St. Paul, Minn.	235, 000	-----	-----	1934	
Wisconsin Farm Bureau Federation.	Madison, Wis.	177, 334	-----	-----	1934	
District No. 8: Farm Bureau Service Co.	Des Moines, Iowa	1, 500, 000	-----	-----	1934	Data for period, Nov. 1, 1933 to Oct. 31, 1934.
Farmers Elevator Service Co.	Ralston, Iowa	400, 000	-----	-----	1934	
Farmers Union Brokerage Co.	Sioux City, Iowa	351, 452	-----	-----	1934	Value of supplies handled on brokerage basis. Data for period, Jan. 1, 1934 to Nov. 30, 1934.
Farmers Union Cooperative Oil Association.	Des Moines, Iowa	219, 000	-----	-----	1934	
Farmers Union State Exchange.	Omaha, Nebr.	1, 115, 009	\$779, 926	\$150, 000	1934	In addition, sales of household supplies amounted to \$241,788. See also p. 13.
Nebraska Farm Bureau Service Co.	Lincoln, Nebr.	60, 409	-----	-----	1934	
South Dakota Farm Bureau Service Co.	Huron, S. Dak.	58, 324	144, 869	-----	1934	Data for period Nov. 1, 1933 to Sept. 30, 1934.
District No. 9: Colorado Potato Growers Exchange.	Denver, Colo.	100, 000	-----	750, 000	1934	
Oklahoma Farmers Union.	Oklahoma City, Okla.	111, 528	80, 426	82, 017	1934	In addition, sales of household supplies amounted to \$4,072.

District No. 10: Consumers Cooperatives Associated, Inc.	Amarillo, Tex.....	251, 993			1934	Operates in Texas Panhandle and parts of New Mexico and Oklahoma. Includes business done on brokerage basis of approximately \$125,000.
Rio Grande Valley Citrus Exchange.	Wealaco, Tex.....	89, 000		570, 000	1934-35	Data for period July 1, 1934, to April 30, 1935.
Texas Cooperatives, Inc.....	Dallas, Tex.....	126, 373			1934-35	In addition, sales of household supplies amounted to \$750.
District No. 11: California Fruit Exchange..	Sacramento, Calif.....	919, 364		15, 050, 121	1934	For further information see pp. 21 and 51.
Dairymen's Feed & Supply Co.	Los Angeles, Calif.....		* 500, 416		1934-35	Data for period May 31, 1934, to May 31, 1935.
Escondido Valley Poultry Association.	Escondido, Calif.....		140, 000	1, 200	1934	
Fontana Producers Egg & Supply Co.	Fontana, Calif.....		275, 804	405, 990	1934	
Fruit Growers Supply Co..	Los Angeles, Calif.....	7, 649, 491			1934	Operates in connection with California Fruit Growers Exchange. Farm supply business includes 1 percent household supplies. For further information see pp. 21, 22, and 51.
Hayward Poultry Produc- ers Association.	Hayward, Calif.....		25, 000	700, 000	1934	In addition, sales of household supplies amounted to \$25,000.
Mutual Orange Distribu- tors.	Redlands, Calif.....		711, 703	5, 680, 706	1934	Data for period Nov. 1, 1933, to Oct. 31, 1934.
Poultry Producers of Cen- tral California.	San Francisco, Calif..	697, 387	3, 549, 717	8, 618, 528	1934	For further information see p. 52.
Poultry Producers of North- ern California.	Eureka, Calif.....	86, 199		119, 413	1934	
Poultrymen's Cooperative Association of Southern California.	Los Angeles, Calif....	58, 918	1, 119, 449	998, 581	1934	

* Unclassified

FARM SUPPLY BUSINESS REPORTED BY REGIONAL PURCHASING AND MARKETING ASSOCIATIONS—Continued

Association and Farm Credit Administration district	Address	Value of farm supplies sold		Value of farm products marketed	Period covered	Comments
		Wholesale	Retail			
District No. 11—Continued.						
San Diego Cooperative Poultry Association.	San Diego, Calif.....	\$613, 073	\$25, 522	\$172, 071	1934	
San Joaquin Valley Poultry Producers Association.	Porterville, Calif.....	-----	° 887, 126	324, 254	1934	
Utah Poultry Producers Cooperative Association.	Salt Lake City, Utah..	° 2, 007, 106	-----	4, 529, 243	1934	Operates in Utah and part of Idaho.
District No. 12:						
Apple Growers Association.	Hood River, Oreg.....	-----	° 707, 385	2, 833, 000	1934	
Cooperative Union Oil Co.	Caldwell, Idaho.....	° 250, 179	-----	-----	1934	
Dairy Cooperative Association.	Portland, Oreg.....	-----	105, 685	1, 343, 064	1934	Operates in parts of Washington and Oregon.
Grange Cooperative Wholesale.	Seattle, Wash.....	950, 812	26, 314	-----	1934	Sales of household supplies amounted to \$167,171.
Idaho Egg Producers.....	Caldwell, Idaho.....	-----	180, 000	500, 000	1934	
Lower Columbia Cooperative Dairy Association.	Astoria, Oreg.....	77, 000	-----	520, 953	1934	Operates in Lower Columbia River Valley of Oregon and Washington.
Pacific Cooperative Poultry Producers.	Portland, Oreg.....	-----	285, 041	1, 368, 423	1934	Operates in Oregon and part of Washington.
Pacific Supply Cooperative.	Walla Walla, Wash..	311, 584	436, 218	-----	1934	Operates in Oregon, Washington, and Idaho. Began operations June 1, 1934, with 12 local units. Number of local units approximately 60.
Washington Cooperative Egg & Poultry Association.	Seattle, Wash.....	-----	5, 033, 699	9, 268, 265	1934	For further information see pp. 41 and 52.

Wenatchee Farmers Exchange.	Wenatchee, Wash.		196,984		1934	Products marketed through Wenatchee-Okanogan Cooperative Federation.
Wenoka Supply Company	do.	138,239			1934	
Yakima Fruit Growers Association.	Yakima, Wash.		* 500,298	1,913,811	1934-35	

*Unclassified.

APPENDIX B

EXEMPTION OF FARMERS' COOPERATIVE ASSOCIATIONS FROM CERTAIN FEDERAL TAXES¹

FEDERAL statutes have for years provided for exemption of farmers' cooperative associations, if properly organized and operated, from income and certain other Federal taxes (Internal Revenue Act of 1934, sec. 101, clauses 12, 13, and 14.) There is still, however, considerable uncertainty among cooperative associations as to the necessary conditions for exemption, and the proper procedure for obtaining it. A comprehensive outline of these subjects was prepared by L. S. Hulbert (21) in 1929, and few changes in the income-tax laws have occurred since that time. Most of the problems of income-tax exemption are dealt with also in a ruling (IT:E:R.R. Min. 3886) made by the United States Bureau of Internal Revenue on July 9, 1931, which may be obtained from that Bureau upon request.

The Internal Revenue Act of 1934 provides for exemption of such cooperatives from capital-stock and excess-profits taxes if exempt from Federal income taxes (secs. 701 and 702). Exemption from these taxes, like exemption from the income taxes, is not automatic but is obtained only by making claim for it. That is, in order to obtain exemption from these taxes, application must be made to the collector of internal revenue for the district where the principal business of the association is located. This is the initial step in proper procedure for exemption. The collector will supply forms outlining information which must be submitted to show that the association qualifies for the exemption.

In order to obtain the exemption, an association or a subsidiary of an association, must satisfy the Bureau of Internal Revenue that it complies with the requirements stated in the Revenue Acts. The burden of proof is upon the applicant.

As to taxes payable for any year, the claims for exemption and refunds must be filed within two years of the time when the association filed its tax returns for such year.

By making minor changes in corporate organization or in business practices, associations are frequently able to qualify for exemption. It may be true that some associations which have been granted exemption for previous years are no longer entitled to exemption because they have not maintained the required conditions, although they might easily have done so.

SUBSIDIARIES ALSO EXEMPT

Corporations organized by exempt cooperatives, or their members, to finance the ordinary crop operations of such members, or other producers, and operated in conjunction with the exempt associations,

¹ Prepared by J. M. Wright, of the Legal Division, Farm Credit Administration.

will likewise be exempt from the payment of these taxes. Restrictions on stock ownership and dividends, and on reserves of these corporations are the same as for the cooperative marketing or purchasing associations.

Cooperatives organized by exempt cooperatives to hold title to property and pay over the income derived from it, less expenses, to the exempt cooperatives are similarly exempt from the payment of these taxes.

Exemption of subsidiaries, like that of ordinary cooperatives, is not automatic, but is obtained by the procedure outlined above.

A subsidiary corporation, therefore, is not exempt unless it meets the stated requirements as to its operations, and unless the cooperative association with which it operates is exempt.

CONDITIONS FOR EXEMPTION OF COOPERATIVES

In substance, the conditions required for exemption as a farmers' cooperative association from the payment of Federal income taxes are described below.

1. The association must be both organized and operated on a cooperative basis for the purpose of marketing products and returning the proceeds, less necessary expenses, to the producers on the basis of either quantity or value of the products marketed; or for the purpose of distributing supplies to farmers at cost plus necessary expenses. Of course, one association may engage in both activities.

2. Substantially all of the stock (except nonvoting preferred stock, entitled only to fixed dividends and to redemption at the price for which issued) or of the voting memberships in nonstock corporations, must be owned by producers who patronize the association.

3. In regard to an association's marketing business, producers who are members and producers who are nonmembers must be "treated alike" with reference to patronage dividends. In regard to purchasing activities, all persons who buy supplies from or through the association, whether members or nonmembers, must be treated alike as to patronage dividends.

4. Associations organized with capital stock must not pay dividends on such stock, directly or indirectly, in excess of the legal rate of interest in the State of incorporation, or in excess of 8 percent per year, whichever is greater, on the amount paid for the stock when it was issued.

5. At least 50 percent in value of both the marketing and the purchasing business of the association must be done with members, and not more than 15 percent of the purchasing business may be done with persons who are neither producers nor members.

6. Any reserves or surpluses set up by the association must be required by State law, or must be reasonable reserves for necessary purposes of the cooperative business.

Associations Must Be Cooperative

Although the Bureau of Internal Revenue does not require that an association keep ledger accounts with its patrons, it must have records showing, among other things, the amounts of its receipts, expenses, and earnings, and the funds carried to reserves or distributed as dividends, patronage, or otherwise. This is necessary because the exemption provisions require that the association be both organized and operated on a cooperative basis. Therefore, in order to show that it has complied with the statute, the association must prove that it has turned back to the producers (if it is a marketing association) and to the purchasers (if it is a supply-distributing organization) all of its earnings other than amounts required for expenses. Subsidiary corporations must show that the associations in connection with which they operate are exempt, and also that such corporations meet the requirements specified for them.

Purchasing associations may treat as supplies and equipment anything that is used in the operation or maintenance of the farm or farm household, and for the purposes of the income tax its distributing business is not limited to articles and supplies used directly in farm operations, such as farm implements, stock feed, and fuel for farm motors.

Voting Control in Producers

In order to obtain exemption, an association is not required to show that farmers hold direct ownership of substantially all its stock or memberships. It is sufficient if such stock or memberships are owned by exempt cooperative associations, engaged in similar activities, whose members, in turn, are farmers. Similarly, it is sufficient if voting stock is held in trust for farmer-members by a State educational and cooperative nonprofit association, conducted for the benefit of such members. The ownership of small amounts of stock by, or for the benefit of, persons who presently cease farming operations will not necessarily exclude an association from exemption. The association will be required to explain such ownership of such stock or memberships. Generally it is necessary to show that the association is doing all that reasonably can be done to see that such stock or memberships are transferred to or owned only by farmers or their cooperatives.

Equal Treatment of Members and Nonmembers

The requirement of equal treatment of members and nonmembers will be complied with: (1) If the cooperative shows that, although its charter and bylaws are silent on the subject, it has consistently paid patronage dividends to members and nonmembers equally, in cash or its equivalent, within a reasonable period after the close of the

fiscal year involved; or (2) if the bylaws provide for payment equally to members and nonmembers and a general reserve has been set up for the payment of patronage dividends; or (3) if the bylaws are silent as to the payment of patronage dividends to nonmembers, and a specific credit to the account of each nonmember is set up on the association's books in the same manner as for members.

The requirement of equal treatment is not violated by applying patronage dividends, distributable to a nonmember who is eligible for membership, to the payment of the price of a share of stock or of the membership fees in the association.

It has been held that a marketing association may make certain limited emergency purchases from persons who are not producers, and does not lose the exemption by failing to distribute patronage dividends to such persons; but fundamentally all producers who market their products through the association, whether they are members or nonmembers, must be treated alike. Purchases of products from nonproducers who are not granted patronage dividends, if made for other than emergency purposes, may cause the association to lose exemption. With reference to the distribution of farm supplies, it has been held that sales to nonmembers, although constituting only a small proportion of the total business, and purely incidental to business done with members, would subject the association to the payment of taxes if such nonmembers were not allowed patronage dividends.

Capital Dividends Must Be Limited

In order to comply with the limitations on stock dividends, and to show that returns to producers, or purchasers of supplies, are properly made, the corporate papers of the association should show that no gains will accrue to members or stockholders in amounts exceeding the permitted dividends, unless such gains are in proportion to their business done with the association. To do this, the association's articles of incorporation or bylaws should provide that whenever assets of the association, including reserves deducted by it, are distributed to members or stockholders, any of such assets resulting from the proceeds of products marketed or of supplies sold shall be credited to the producers or purchasers in proportion to their business with the association.

Business With Nonmembers Limited

The Bureau of Internal Revenue has ruled that an association may treat as a member anyone who shares in the profits of a cooperative association and who is entitled to participate in its management. Thus patrons who are entitled to vote as stockholders, or in nonstock associations as members, may be considered to be members for the

purpose of determining amounts of member and nonmember business. But persons may not be considered members because they hold nonvoting stock, or certificates of interest or indebtedness.

Reserves Must Be Reasonable and for Necessary Purposes

Funds accumulated or maintained by an association to meet capital expenditures of the association in connection with its cooperative business may be included in reserves, and are permissible if reasonable in amount. The applicant for exemption must show that the amount is not larger than is reasonably necessary to its business and that the funds are not used for purposes unrelated to the cooperative business.

PATRONAGE DIVIDENDS DISTRIBUTED NOT TAXABLE

If a farmers' association does not meet the requirements for exemption from income taxes, it still is not required to pay taxes on savings or earnings which it has returned, or has obligated itself to return, to its members or others in the form of patronage dividends. The theory upon which this rule is based is that the dividends when distributed, or the liabilities for them, constitute an expense which must be deducted from receipts in order to determine the net income. In order to meet this requirement, the patronage dividends must be paid during the tax year, or the obligations to pay them must have become binding on the association during the tax year by contract, bylaw, or provision in its articles of incorporation, which requires the distribution, on a patronage basis, of net earnings above the stock dividends and reserves allowed. Where patronage dividends have not been paid, or the amount due to each patron declared by resolution of the board of directors, it is desirable that the corporate papers or a resolution of the board make the obligation as easy to determine and as definite as possible, both as to the basis of the dividend and as to the amount.

Where patronage dividends are distributed, or the association has become obligated to pay them, during the tax year, they may be deducted from the receipts for the purposes of the excess profits tax which is provided by the Internal Revenue Act of 1934. However, such payments or obligations would not affect the amount of the capital stock tax, provided by that Act. Under the Revenue Act of 1934 the excess profits tax is equivalent to 5 percent of all net income for the year in excess of 12½ percent of the adjusted declared value of the association's capital stock at the close of the preceding tax year. Under the same Act the capital stock tax is \$1 for each \$1,000 of the adjusted declared value of the capital stock.