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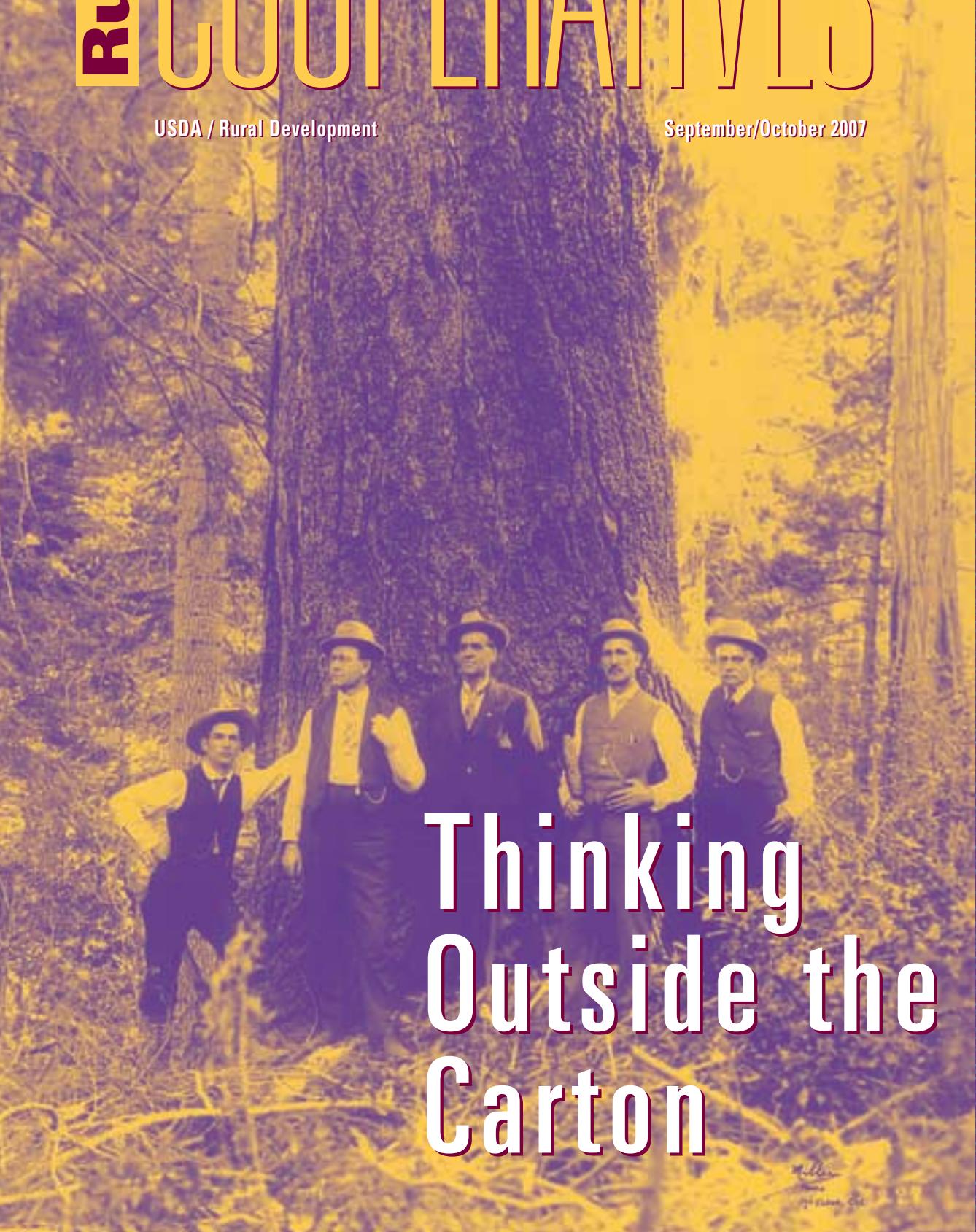
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Rural

# COOPERATIVES

USDA / Rural Development

September/October 2007



Thinking  
Outside the  
Carton

## Co-op structure aids longevity

The two feature articles about farm supply cooperatives that lead off this issue of *Rural Cooperatives* both tell remarkable stories. One is an account of how Southern States Cooperative in Richmond, Va., has come back from the brink of bankruptcy five years ago. The turnaround involved painful staff reductions, the selling of assets and out-sourcing of some functions (including retail credit operations and the co-op's transportation fleet).

But even with all those moves, the turnaround would have failed without the support of the co-op's loyal members, employees and suppliers. They stuck by the co-op because they know how much this cooperative has meant to producers and others throughout its broad service area.

CEO Tom Scribner is candid in saying that the co-op's policy of "laying all of its cards on the table" when dealing with suppliers and others was the only way it was able to overcome the rumor mill and continue to carry out the business moves it had to make. The article concludes with Scribner's checklist of "lessons learned" — something all co-op directors and managers should review carefully.

The cover story salutes California's Fruit Growers Supply Co. on its 100th anniversary. Even though it is the nation's oldest regional farm supply co-op, it has always existed somewhat in the shadow of its internationally famous sister co-op, Sunkist Growers. But the success of Fruit Growers also holds valuable lessons for all co-ops.

The fact that it was organized as, and has remained, a grower- and packer-owned cooperative has been key to enjoying a century of success, its managers and directors say. When dealing with a perishable product like citrus, and different production regions, the co-op business structure is "the best that you could adopt," says Fruit Growers President Nazir Khan.

While some bemoan slow decision making as a drawback of co-ops in a fast-moving business world, Khan sees advantages to the collaborative decision-making process that is a hallmark of cooperatives. "You may not be able to make decisions as rapidly, but you also avoid rash or impulsive decisions."

As a co-op, Fruit Growers looks at the interests of all its different districts and growing regions. "Chances are, we will have considered every nook and cranny of the important decisions we make," says Khan. "I believe it forces a better

*"Trust (between directors and management) can carry you a long way once established, but you can never compromise that trust."*

decision in the end, even though the process might not be a simple one."

Sunkist President Tim Lindgren (and former Fruit Growers Supply president) agrees

that the co-op business structure is ideal for ensuring that the 6,000 grower-members and 40 packer-shippers supported by the sister co-ops have their voices heard and their needs met.

"Fruit Growers has prospered because it stayed focused on supplying member needs. It hasn't branched out into a lot of areas that aren't part of the program. It has provided tremendous service to Sunkist packinghouses and growers, for no charge, and pays them (through dividends) to do business with the co-op. It's an unbeatable combination."

That's not to say "business as usual" will cut it for co-ops any more than it will for any other type of business that expects to thrive in a market where competition is always king. Fruit Growers is completely revamping its information technology systems — a huge undertaking that offers increased efficiencies throughout the organization.

The effort is progressing "on time, on budget and as close to seamlessly as you can get," says board Chairman Nick Bozick. He credits that result to a collaborative effort and "many long hours put in beforehand by our planning teams."

Improving the co-op's data systems and other operations is essential as the American citrus industry has to deal with ever-growing levels of foreign competition, Bozick stresses.

Maintaining good relationships between management and directors is "like anything in life," says Lindgren. "It takes trust, communications and transparency. It takes a while in a co-op to develop full, mutual respect between board and management. So once it is established, you must nurture it, communicate and allow participation. Trust (between directors and management) can carry you a long way once established, but you can never compromise that trust."

— Dan Campbell, Editor ■

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## FEATURES



p. 4



p. 10



p. 14



p. 28

### 4 *Thinking Outside the Carton*

100 years ago, *Fruit Growers Supply* founders made investments that still bolster citrus industry

By Dan Campbell

### 9 *Farmer co-ops set net income record; gross business volume hits \$126.5 billion*

### 10 *Back from the Brink*

Support of members, employees and suppliers vital to Southern States' turn-around effort

By Jim Erickson

### 14 *Emerald Pastures*

Ireland's dairy co-ops adopt range of strategies in response to changing markets

By Michael Ward

### 28 *Worker-owned/ESOPs can help preserve business in rural America*

By Bruce J. Reynolds

### 32 *Corn Condos for Sale*

Growth and innovation key to *Heartland Co-op*'s success

By Stephen Thompson

## DEPARTMENTS

### 2 COMMENTARY

### 20 VALUE-ADDED CORNER

### 23 UTILITY CO-OP CONNECTION

### 26 CO-OP DEVELOPMENT ACTION

### 35 NEWSLINE

### 42 PAGE FROM THE PAST

#### *On the Cover:*

Board members of *Fruit Growers Supply Co.* tour some of the co-op's then new timber holdings in Northern California, circa-1910. The co-op, now celebrating its 100th anniversary, still owns timberland in the Pacific Northwest, the earnings from which benefit citrus growers.

Photo courtesy *Fruit Growers Supply Co.*





# Thinking Outside

By Dan Campbell, editor

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**T**he sight of foresters planting seedling trees in the lush conifer forests of the Pacific Northwest is not unusual. But a team of foresters planting more than 1.5 million seedling trees on 3,400 logged acres is noteworthy because of the emblem on their caps: Fruit Growers Supply Co. — a farm and packing supply cooperative with annual sales of \$165 million. The co-op is owned by more than 6,000 citrus growers and citrus packer/shippers in California and Arizona.

So why would citrus growers employ foresters to care for 350,000 acres of timberland in Northern California, Oregon and Washington? And what has the health of an evergreen forest in Washington got to do with the financial health of citrus orchards nearly 1,000 miles to the south?

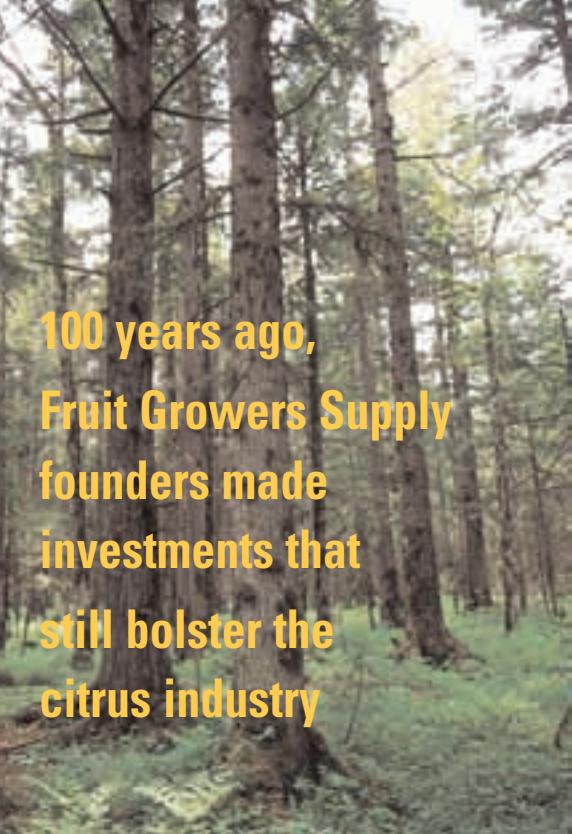
It all goes back to one of the worst natural disasters in the nation's history:

the San Francisco earthquake of 1906. The tragedy motivated the citrus growers of a century ago to take action that today's growers and packers remain thankful for as Fruit Growers celebrates its 100th anniversary this month. The co-op's founders were thinking "outside the box" a long time before that became a catch phrase for innovative, forward-looking business planning. In the true spirit of cooperative business, they weren't just thinking of themselves, but of future generations of growers who would follow in their furrows.

## Co-op born of disaster

Early on the morning of April 18, 1906, San Francisco was struck by a devastating earthquake that sparked an even more destructive fire. Together, the earthquake and fire destroyed more than 80 percent of the city and killed an estimated 3,000 people. About 300,000 of the city's 410,000 residents were left homeless, and monetary damage was put at more than \$400 million.

So great was the demand for lumber to rebuild San Francisco in the weeks and months following the earthquake



**100 years ago, Fruit Growers Supply founders made investments that still bolster the citrus industry**

that California citrus growers were unable to buy wood for fruit crates needed to ship their crop to market.

Members of the Southern California

*So much lumber was diverted to San Francisco following the earthquake and fire in 1906, that Fruit Growers Supply was formed to help source lumber needed for citrus packing crates.*





*About 80 million cartons and other fruit containers are produced each year at the Fruit Growers Supply manufacturing plant in Ontario, Calif. Opposite page: Citrus growers, such as these, in the early days of the 20th century had the foresight to buy timber resources for the future of their industry. Today, the co-op employs a staff of foresters to care for its 350,000 acres of timberland. Photos courtesy Fruit Growers Supply*

# the Carton

Fruit Growers Exchange (today known as Sunkist Growers) responded by forming Fruit Growers Supply Co. on Oct. 5, 1907, as a separate, but closely related, cooperative. Its mission then, as today, is to ensure the availability of materials needed to grow, harvest, pack and ship members' citrus fruit.

Fruit Growers soon began buying timberland and sawmills in Northern California to ensure a steady supply of raw material for the wood shooks needed for fruit crates. Eventually, the co-op became one of the largest private owners of forestland in California, peaking at about 387,000 acres in 1999.

In the 1950s, wooden fruit crates were supplanted by corrugated cardboard cartons, and Fruit Growers sold its sawmills and built a carton manufacturing plant in City of Industry, Calif., northeast of Los Angeles. But it elected to keep the timberland and to continue to use it as a renewable resource that helps reduce the overhead cost of operating the nation's oldest regional farm supply co-op. Indeed, the co-op operates without requiring any type of capital investment from its

members.

"The fact that we run this great organization without any member fees or retains, and that we get paid dividends for doing business with the co-op is a direct result of having resources such as the timberland, combined with our highly efficient management," says Fruit Growers Chairman Nick Bozick, a third-generation citrus grower with 1,000 acres of citrus and a packing operation in the Coachella Valley, south of Palm Springs.

In addition to supplying members' needs for cartons, the co-op operates a pallet-manufacturing subsidiary, United Wholesale Lumber Co., and operates six large farm supply stores, called operation centers, throughout the citrus-growing region of California and Arizona. Each operation center stocks about 8,000 items.

"Fruit Growers stocks everything we need to grow and ship our citrus: from fertilizer to pruning shears, from herbicides to chain saws and ladders," says Bozick, who lauds the operation centers for their product quality, deep

inventory geared specifically for citrus orchards, low prices and knowledgeable staff.

## A friend in need

The value of a supply store that is always there for you, especially in an emergency, is one of the primary reasons farmers put so much support and faith behind supply co-ops. That fact was recently brought home for Board Vice Chairman Mark Gillette, a fourth-generation citrus grower with 2,000 acres of trees and a 1.25-million-carton per year packing business near Dinuba, about a half hour south of Fresno.

"One unfortunate aspect of farming today in California is the big upsurge in thefts and vandalism that we have to contend with," says Gillette. Anything made of copper or brass — as is found on pipe couplings, orchard wind machines and irrigation systems — is fair game for vandals looking to make a few bucks from the scrap metal trade. Gillette recently suffered \$7,000 in damage from thieves who "probably got \$50 worth of parts. Much as we would



like to, we can't monitor 2,000 acres of citrus trees at all hours. By the time you realize you've been hit, the parts are long gone."

The expense of replacing lost parts wasn't the biggest problem the thieves caused to Gillette's orchard – it was the hemorrhaging of 400 gallons per minute of precious irrigation water in this bone-dry growing environment. Spare parts were needed fast to make the repair. A distress call to his nearest Fruit Growers operations center was made. Not only did it stock the exact parts he needed, but the parts were in his hands within the hour.

"This is not the type of stuff you can run down to your local Home Depot and buy," Gillette says. He recalls another emergency on a Christmas day when his local Fruit Growers store opened its doors and again helped him out of a jam.

Not only does Fruit Growers carry extensive inventories of irrigation system supplies geared for citrus, it will design an entire irrigation system tailor-made for a grower's operation. These days, most growers opt for micro-emitter systems for maximum efficiency and water conservation.

Bill Chaney, another board member who farms 3,000 acres (two thirds of which is leased) of citrus in Arizona, installed a new micro-emitter irrigation system 10 years ago. "We did the first 320 acres with another supplier," Chaney recalls. Unhappy with the

quality he got for the price, Chaney asked Fruit Growers to design and supply the irrigation system for another 1,500 acres.

"With Fruit Growers, I got a superior system, engineered so we didn't need any big pipes, and we saved about 25 percent on a very sizable bill," Chaney says. The co-op even convinced him that he could do the installation himself (Fruit

Growers does not do installation). He has done his own installation ever since.

The presence of Fruit Growers also has the collateral benefit of helping to keep down the farm supply prices of competitors, says Chaney.

#### **Box not just a box**

The carton manufacturing plant in Ontario is perhaps the crown jewel in the Fruit Growers system. "State-of-the-art" is an over-worked adjective in the agriculture industry, but when it comes to the Ontario container plant, Bozick says it is dead-on accurate. "It is



*In addition to manufacturing a wide variety of fruit containers in Ontario, Fruit Growers Supply also has labs where engineers design and test as many as 40 new fruit containers every year. Upper left: the co-op also operates a pallet manufacturing plant.*

simply the best, most efficient plant of its kind, although we continue to tweak it to make it even more efficient." In a typical year, the plant will produce 80 million citrus containers with a workforce of about 65 production employees.

In addition to producing all of the cartons its members need, Fruit Growers also produces containers for non-members and industrial users during periods of lower demand by the co-op. Profits from these non-member sales go back into maintaining the plant and funding member dividends. Dividends in recent years have run



*As a sister co-op of Sunkist Growers, most of the cartons and containers Fruit Growers Supply produces are used to ship Sunkist citrus. But during periods of low member demand, the plant also produces for non-members, the earnings from which help defray plant operation costs.*

about 10 cents a box.

To the uneducated eye, a fruit carton may appear to be a simple container. But looks can be deceiving. Each size and style of citrus carton is carefully engineered in Fruit Growers' own design lab to provide maximum protection, breathe-ability and moisture absorbing characteristics at the lowest possible weight. The slightest flaw, such as air vents cut just a little too sharply, can lead to damaged fruit, says co-op president Nazir Khan.

The requirements of the ever-changing retail environment into which Sunkist (Fruit Growers' sister co-op) markets fruit means that new types and designs are constantly needed. In 2005 alone, Fruit Growers was called on to design and produce 40 new cartons and other containers. This trend accelerates as the industry becomes more diversified both on the production side — where clementines and other new tangerine-type varieties are gaining popularity — and in the retail sector, where warehouse-type outlets are gaining a bigger share of the market. The warehouse store operations also require that the supplier, in effect, manage the produce sections.

At any one time, Fruit Growers may be asked to supply 200-300 different packaging items. On an hour's notice, a packing house can typically pick up any of those items.

"Sunkist responds to many market demands, and Fruit Growers must be in

lock step to meet those demands," says Khan. "In the past, containers only needed to get the product to the retail outlet. Containers were not part of the display. Today there is more demand for containers — such as clamshell trays and various sizes of bags with promotional coupons printed on them — that go directly into the hands of the consumer."

Sunkist marketers often come up with a design concept, which Fruit Growers engineers then go to work on to turn into reality. "We experiment with different weights and how a carton will ship, striving to maximize the integration of the carton with pallet and trucking configurations," Khan says. "Innovation here is constant; we strive to ensure that the containers we provide to Sunkist are the ones that the rest of the industry will try to emulate."

#### **Industry migration and future of timber holdings**

Just as the growth of metro Los Angeles has driven much of the region's once huge dairy industry into California's San Joaquin Valley and even outward into New Mexico, Idaho and other western states, so has it displaced much of the citrus industry that once thrived there. However, unlike the dairy industry, the mild temperatures citrus requires confine the West's citrus industry to the southern third of California, the San Joaquin Valley and to southern Arizona.

Today, sizable citrus plantings are found primarily around Indio, Coachella and in Ventura County. But acreage losses there have been offset by new plantings to the east, in areas such as Fresno and Tulare Counties. These areas were once deemed too hot and dry for commercial-scale production, but new varieties and advances in irrigation technology have made these Central Valley counties hugely productive. As a result, industry citrus acreage has been stable for many years at around 296,500 acres.

The situation around Phoenix and Yuma in Arizona is similar, with citrus giving way to development.

The fact that not all growers in the path of urban sprawl elect to move their operations when they finally sell their land to make way for houses and strip malls has led to a debate within Fruit Growers. It's the same debate that many co-ops wrestle with when members and their children leave the industry: the desire to sell co-op assets and distribute — or reinvest — the proceeds. In the case of Fruit Growers, this has led to discussion in recent years about the possibility of selling the timberland.

"If you are impacted by urban pressure, then your perspective is likely to be short range if you believe that you may not be able to continue farming long-term," says Khan. "But most growers see the timberland as a trust that makes both Fruit Growers and Sunkist very, very strong."



*More than 8,000 farm supply items needed by citrus growers — from special irrigation systems to gloves and picking sacks — are available at each of the six Fruit Growers Supply operation centers.*

Some of the co-op's timber acreage has been sold, which is why total holdings have decreased from about 375,000 to 350,000 acres. But that has mostly been as a result of selling less productive holdings in California, and using the proceeds to reinvest in more productive timberland in Oregon and Washington, says Tim Lindgren, currently Sunkist president but prior to that the president of Fruit Growers from 1978 to 2003.

It was during his tenure at the helm of Fruit Growers that the timberland holdings were about doubled, and when the Ontario container plant was opened. He also spearheaded the expansion of the co-op's handful of small supply stores into the large operation centers of today.

While no formal motion to divest the co-op's timberland has been made, the Fruit Growers directors (most of whom also sit on the Sunkist board) did hire a consultant in 2005 to study the economics of maintaining ownership vs. selling it and reinvesting the proceeds. The clear conclusion, Bozick says, was that maintaining ownership of the timberland was the best alternative.

"Wall Street tells you to look at all your assets and make sure they are

generating the maximum returns," Bozick says. "We did that, and it was determined that we are getting a return that far exceeds any other that could be gained from selling the timberland."

Lindgren agrees. "At the end of day, the amount of money we would have received back didn't justify a sale. The timber yields a very good return on investment, providing full funding of Fruit Growers and its services to Sunkist."

#### **Environmental considerations**

Constantly changing environmental regulation is something all farmers have to contend with. "But everything you experience in production agriculture, you see it first and you see it in spades in timber," says Lindgren. "Our forests still represent the American frontier, and people are very protective of the forests and watersheds and all the things forests contribute to." Forests provide wildlife habitat and recreation, provide erosion control and even help cool water in streams, which is vital for the fish, he notes.

To help manage the resource in a complex regulatory environment, Fruit Growers employs a staff of 25 forestry-trained employees who oversee timber

sales, logging and reforestation.

About 69 million board feet of timber, worth \$32 million, was sold in 2005. The co-op foresters manage the timberland on a sustained-yield basis, planting seven trees for every one they cut. As a result, actual wood fiber reserves have been increasing by about 3 to 5 percent each year.

And there may be even more benefits for members on the horizon. Carbon trading, in which landowners receive tradable "carbon credits" that have a monetary value based on the amount of carbon their trees remove from the atmosphere, could provide another return.

Studies have shown that older trees are far less beneficial in this regard than young trees, Lindgren notes. So, by taking out older trees and replacing them with younger trees, air quality benefits, Lindgren says.

With the rapid expansion of metro Phoenix and Yuma poised to displace much of his orchard land, director Bill Chaney says that if anyone should have been in favor of a sale of the co-op's timberland, it would have been him.

"I guess I could take the stance that in 10 years, I may well be largely out of the citrus business, so to heck with future of the other growers. Let's just cash in now. But the timberland is such a wonderful resource for offsetting the overhead of Fruit Growers and keeping it financially strong. It also has a residual effect that helps strengthen Sunkist. I've never had to put a dime into that timberland, but it has put a lot more than dimes back into my operation."

"The forefathers of Fruit Growers made that investment so their children and the children of their fellow growers would have this resource to help them in future years," Chaney continues. "I have no doubt we made the right decision in electing to preserve it as a trust for this great organization and future generations of growers." ■

# Farmer co-ops set net income record; gross business volume hits \$126.5 billion

*Editor's note: Information for this article was compiled by the Statistics Staff of USDA Rural Development, Cooperative Programs, including Katherine C. DeVille, Jacqueline E. Penn and E. Eldon Eversull.*

**F**armer cooperatives had a record \$3.2 billion in pre-tax net income in 2006, fueled by farm supply sales – especially by higher prices for petroleum products. This marks the second consecutive year that a new net income record was set. Net income shot up by 24 percent from 2005, when \$2.5 billion in net income was reaped by the nation's farmer-owned cooperatives.

Overall farm supply sales increased by almost 17 percent, with petroleum sales alone registering a \$5 billion gain. On the marketing side, sale of crops, livestock and value-added products by cooperatives decreased 2 percent. The biggest

Table 1—U.S. farmer cooperatives, comparison of 2006 and 2005

Item	2006 Billion \$	2005 Billion \$	Change Percent
<b>Sales (Gross)</b>			
Marketing	76.5	78.0	-1.98
Farm supplies	45.9	39.3	16.72
Service	4.1	4.3	-4.90
<b>Total</b>	<b>126.5</b>	<b>121.7</b>	<b>3.96</b>
<b>Balance sheet</b>			
Assets	47.9	46.6	2.80
Liabilities	28.0	27.0	3.35
Equity	19.9	19.5	2.03
Liabilities and net worth	47.9	46.6	2.80
<b>Income Statement</b>			
Sales (Gross)	126.5	121.7	3.96
Patronage income	0.5	0.4	24.15
Net income before taxes	3.2	2.5	24.13
<b>Employees</b>			
Full-time	123.4	125.4	-1.62
Part-time, seasonal	57.3	54.4	5.26
<b>Total</b>	<b>180.7</b>	<b>179.9</b>	<b>0.46</b>
<b>Membership</b>			
Membership	2.6	2.6	-0.08
<b>Cooperatives</b>			
Cooperatives	2,675	2,896	-7.63

Figure 1—Cooperatives' Gross and Net Business Volumes, 1979-2006

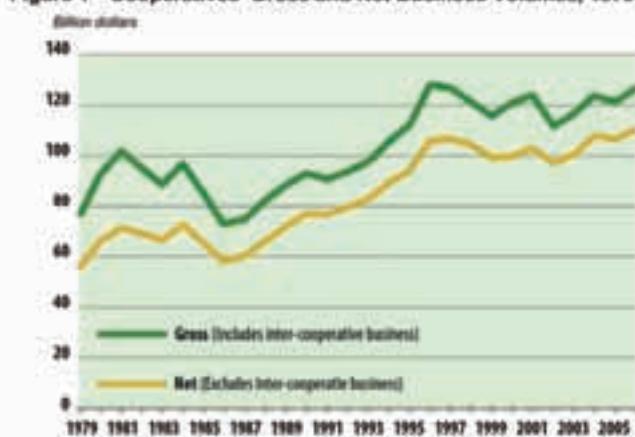
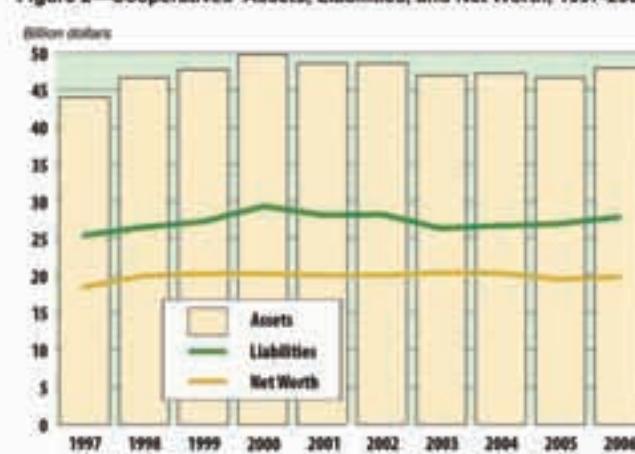


Figure 2—Cooperatives' Assets, Liabilities, and Net Worth, 1997-2006



reason was lower milk prices, which resulted in a \$2 billion decline in dairy sales. However, milk prices in 2007 are sharply higher, and with corn prices up, co-op marketing sales appear poised for a possible new record in 2007.

Gross business volume of \$126.5 billion for farmer cooperatives increased \$5 billion from 2005, nearing the record \$128 billion recorded in 1996, according to USDA Rural Development. Although not a record, gross business volume continued the general upward trend in sales that started in 2004 (figure 1).

Equity capital held by co-ops increased 2 percent, to almost \$20 billion, but remains low at 42 percent of all assets. Cooperative assets grew by 3 percent, to almost \$48 billion, while liabilities grew to \$28 billion (figure 2).

Patronage refunds grew 24 percent to \$500 million, up from \$400 million in 2005.

Farmer cooperatives remain one of the largest employers in many rural communities, with overall employment of

*continued on page 40*



**Support of members, employees and suppliers vital to Southern States' turn-around effort**

# Back from the Brink

By Jim Erickson

*Editor's note: Erickson recently retired as communications director of Southern States Cooperative, but not before writing this article about how the co-op has righted its fiscal position in recent years.*

**T**he day in late September 2002 began routinely enough for Tom Scribner, then the executive vice president and chief merchandising officer at Southern States Cooperative. Directors of the regional farm supply co-op were at the corporate office in Richmond, Va., for a regular board meeting, one where Scribner had given a report at the board's afternoon session the preceding day.

Before the new day in early fall ended, however, the board had asked him to take the helm as Southern States' president and chief executive officer, and he was quickly immersed in efforts to turn around a co-op teetering on the financial brink.

The coming days would be a never-ending stream of meetings with bankers, consultants, the co-op's member-leaders, employees and other stakeholders. The decisions and recommendations he made to the Southern States board in the following weeks and months were rarely easy or painless. But now, some 60 months later, the co-op has just posted what Scribner views as a breakthrough year with profitable results exceeding its budget goals.

How did Southern States — which in its 76-year history prior to 1999 had never lost money on its own operations — come so close to financial disaster? And how was the co-op able to turn the situation around?

## Learning lessons the hard way

Conversations with Scribner, the co-op's Executive Vice President and Chief Financial Officer Leslie Newton, and

Executive Vice President and Chief Operating Officer Wesley Wright, offer ample evidence of the roller-coaster ride Southern States has been on. Lessons learned often came the hard way, but they provide a checklist of pitfalls to avoid and management tools and practices needed to turn around a faltering business. Scribner firmly believes many of those tools and practices are just as vital for keeping a sound company moving forward and avoiding the problems that plagued Southern States.

Newton recalls that after joining the Southern States' treasury department, the co-op was performing at record levels in the 1996 and 1997 fiscal years.

"Along with others in our industry, we developed quite a corporate ego, and beginning in 1998 the emphasis turned to growth and expansion into new business ventures," she observes. "The prevailing view among many in agriculture at the time was that growth was the only way to keep from falling behind and eventually becoming irrelevant."

Meanwhile, Scribner had come on board in 1998 as a vice president in information systems after some 20 years with the Landmark and Countrymark co-ops in the Midwest. Elevated

included eliminating the negative cash flow before the co-op ran out of money, giving nervous bankers evidence the large sums they had loaned would be repaid and implementing a restructuring plan that gave the co-op a fighting chance to have a future.

Initial decisions came quickly and included:

- Cutting some 1,100 jobs, about one-fourth of the Southern States work force at that time.
- Bringing in a "turn-around" firm and appointing one of its principals as chief restructuring officer.
- Implementing rigid procurement and inventory controls tied to 16-week cash forecasts. With the co-op's liquidity at dangerously low levels, this step was especially crucial.
- Selling a number of properties, some of which were part of the co-op's core operations. But most were non-core and what Scribner describes as "nice-to-have" assets. In some instances, the underlying value of the real estate involved was more than an asset's projected 10-year earnings potential. Proceeds went to pay down debt.
- Out-sourcing business functions, such as the co-op's transportation fleet and retail credit operations, to reduce

*The chief restructuring officer said that the difference between companies that succeed and those that fail could be found in their employees.*

to executive vice president in 2001, he didn't anticipate how quickly his job responsibilities again would change.

Evidence that the acquisitions weren't working came early and continued to mount, but only after the growth spiral had caused the co-op's debt level to balloon. At the same time, weather factors and weak commodity prices applied even greater pressure on Southern States' operations. Ink on the bottom line turned red.

#### **Feeling the squeeze**

With banks demanding debt repayment and operations showing a loss, the co-op's already-thin liquidity position was squeezed even further. Newton feared it was only a matter of time — a very short time — before the co-op would be unable to make its payroll.

Farmland Industries' Chapter 11 bankruptcy filing in May 2002 and the fact Agway also was struggling for its survival had put cooperatives under the financial microscope. Rumors about the future of Southern States began to surface as well. (Editor's note: Agway later filed for bankruptcy and both Agway and Farmland subsequently were liquidated.)

It was in this environment the Southern States board acted, entrusting Scribner with the huge task of turning around the business. His initial challenges were numerous, encompassing both short- and long-term priorities. These

costs and improve service. After some initial resistance to the credit change, the new program through John Deere Credit has been well received. Equally important, credit-related losses have dropped dramatically. In the last fiscal year, Southern States posted a net gain in the credit area due to recoveries on accounts earlier written off.

#### **Fending off unsolicited buyouts**

"The job cuts and selling-off of assets were especially tough," Scribner notes. "But they were probably easier for me to deal with because being new in my position meant I didn't have the emotional ties that others had. The reality was we had no choice; delays only would have made things worse."

Scribner says another critical aspect was an early decision to separate ongoing, core business operations from restructuring activities such as closings and sales of real estate. Unencumbered by these issues and concerns, operating personnel were better able to focus on running the business.

While major changes — such as selling entire operating divisions — were never off the table, Southern States had analyzed its various activities and determined that its basic farm supply business model was viable. But it wasn't long before the co-op received unsolicited offers to acquire its

feed, petroleum and insurance operations.

"As we went through the due diligence process, one thing became clear," Scribner recalls. "The Southern States name was quite valuable and that's what the companies that approached us really wanted. We realized the value of our name, too, as well as the importance of these operations to offering a complete market basket of products and services. We ultimately opted not to sell any of the operations, even though the short-term financial benefits would have been substantial."

Communications also played a key role. Thursday and Friday meetings were begun for various management teams, and employees received updates on the co-op's evolving situation either during group meetings with management or via communications from Scribner through Southern States' Intranet site.

Scribner, Newton and others from senior management also met with boards and managers of local co-ops Southern States manages under contract. Communications efforts also extended to Southern States lenders, with meetings and conference calls used for progress reports and responding to questions.

In addition, information provided to Southern States'



*"The only way to deal with the rumor mill was to lay all our cards on the table whenever we met and talked with people." — Tom Scribner*

directors was expanded with interim board reports and by having all officers review their respective areas of responsibility at every board meeting.

#### **Easing cash-flow problems**

To ease the pressure on cash flow, Southern States needed cooperation from its vendors and suppliers. After receiving candid information about the co-op's situation and the steps being taken to deal with it, the vast majority of suppliers agreed to extend payment deadlines.

"We concluded the only way to deal with the rumor mill was to lay all our cards on the table whenever we met and talked with people," Scribner says. "If people know you're being open with them, they're much more likely to maintain trust and confidence in what you're doing."

More tough decisions had to be made, however. An existing plan to grow Southern States' farm and home products business with private dealers was scrapped due to capital constraints and because the effort detracted from serving the co-op's core agriculture customers. In addition, the number of private dealers was reduced to those the co-op could economically serve. Minimum order requirements were instituted, credit was cut off to dealers whose accounts were delinquent and the number of different products in inventory

was greatly reduced.

Another difficult, but financially important action, was freezing benefits in the co-op's defined benefit pension plan.

"Our board of directors was directly involved in virtually all these decisions," Scribner observes, adding that directors were also willing to make the tough calls.

#### **Members show confidence**

An early indicator the co-op had member support and confidence came soon after Scribner took the helm. The co-op had a program that allowed members to pre-pay for inputs and other supplies they intended to purchase and take delivery on the following year. Depending on how long their money was in Southern States' control, members earned credits that expanded their purchasing power.

For Southern States, the program was a major tool for financing the build-up in inventories needed for the spring season. Scribner and Newton concluded members would be reluctant to put money into the program for fear of its being caught up in bankruptcy, rumors of which were running rampant. Accordingly, a separate "bankruptcy-proof" account was established as an option for anyone with such concerns.

It was good news indeed when the pre-pay program

subsequently neared its budget goal. But the most interesting and, for Southern States leaders, heartening aspect was that most participants eschewed the bankruptcy-proof account and put their funds in the regular program. Because there was no difference in the amount of credits that could be earned, it was a clear indication members were confident of the co-op's ongoing viability and were willing to support the organization.

Evidence of lender confidence in Southern States' progress came in October 2004 when a new financing package was successfully negotiated. The new plan provided for long-term and seasonal funding, as well as a tremendous increase in liquidity.

Both Scribner and Newton attribute much of the co-op's turn-around success to its "rope holders" — employees at all levels whose loyalty to the organization and commitment to Southern States' farmer-members never faltered. According to Newton, the chief restructuring officer (CRO) — a veteran of working with struggling businesses — told her when he first arrived that the difference between companies that succeed and those that fail could be found in their employees.

The CRO observed that Southern States employees exhibited a greater desire to have the co-op survive than

those at any other company he had known.

### Maintaining momentum

As Southern States' position gradually improved, management moved to keep the momentum building. Drawing on earlier experience with a well known, major retailer, Wright took the lead in implementing a more disciplined approach for running the co-op's various operations and for measuring virtually every important aspect of the business.

Under Wright's direction, Southern States also gathered and analyzed demographic data on its retail locations to determine the best product mix for each and to establish a priority list for various types of store improvement efforts. Some two dozen such store development projects have been completed or are



*"The job cuts and selling off of assets were especially tough," says Southern States CEO Tom Scribner (seated) of the effort to trim the co-op's costs. With him are Leslie Newton (center), executive vice president and chief financial officer, and Wesley Wright, executive vice president and chief operating officer. Photos courtesy Southern States*

on the drawing board for the current fiscal year.

In addition:

- Improved budgeting tools were implemented, details on each day's business results were made available the next morning, and the time for reporting month-end results was cut from 15 business days to five.
- Data on customer purchases was organized so it could be used for efficiently targeting the co-op's marketing efforts.
- A manager training program abandoned during the co-op's cost cutting/restructuring period was reinstated.
- Retail operations in heavy crop production areas in western Kentucky, eastern North Carolina and Georgia were reconfigured to a "hub and spokes" system designed to cut costs and maintain Southern States' presence in these highly competitive markets.

- A new retail location was opened in West Virginia, the first such facility added in more than a decade.

### Lessons learned

Actions the co-op has taken reflect many of the lessons learned during the past five years, Scribner says, but he offers others as well:

- Practice fiscal conservatism, an extremely important factor in a cyclical industry such as agriculture.
- Maintain adequate liquidity and control overhead.
- Recognize when your restructuring is complete and when it's time to begin re-growing the business.



- Establish clear accountability for actions.
- Have a well-defined scope of work for any outside consultants who may become involved, as opposed to leaving such assignment(s) open-ended.
- Make sure you have the right people in the right jobs. In a restructuring as extensive as Southern States', that inevitably requires a blend of veteran employees and new talent.

Southern States' historic mission — providing farmer-members with a complete line-up of products and related services for growing all types of crops and livestock — remains the same. But the co-op has changed in many other ways Scribner is convinced will serve the organization well in the future. ■

*Ireland's dairy co-ops adopt range of strategies in response to changing markets*



# Emerald Pastures

**By Michael Ward**

*Editor's note: Ward is deputy director of the Centre for Cooperative Studies at the National University of Ireland in Cork, Ireland. This is the first of two articles that examine the state of cooperatives in Ireland. The second article, which looks at the future of small dairy co-ops and farms in Ireland, will appear in the Nov.-Dec. issue.*



Irish farmers and their cooperatively owned businesses are operating in an environment of increasing uncertainty.

The accelerating rate of change in the agricultural policies of the European Union (EU), combined with structural changes at the processor and retail levels, have resulted in Irish dairy cooperatives adopting a range of strategic responses to address the changing demands of the agribusiness environment.

### Structure of Irish dairy co-ops

As of the end of 2004, Ireland was home to 31 dairy cooperatives with 88,569 members and total sales of 10.44 billion euros. These include co-ops with holdings in Public Limited Companies (PLCs). Co-op-PLCs were created when a number of bigger co-ops converted substantial percentages of their assets into PLCs, which were listed on the Irish Stock Exchange. The co-ops and individual co-op members still own substantial interests in these PLCs.

Membership and sales varied dramatically from cooperative to cooperative, depending not only on the size of the co-op but also on farm size. The number of co-ops has steadily declined from the 1960s as a result of mergers. These co-ops can be categorized as large, medium, small or very small.

*The three largest dairy co-ops* — Kerry, Glanbia (now one of the largest cheese producers in the United States after the opening of the Southwest Cheese plant at Clovis, N.M., in which it is the largest shareholder) — account for 82 percent of the total sales of Irish dairy co-ops and 44 percent of the members. While Kerry and Glanbia grew via the

PLC route, Dairygold recently decided to take a different route for financing growth. In 2006, instead of setting up a PLC, Dairygold Co-op created, from many of its new ventures, a subsidiary called Reox Holdings and launched it in a non-publicly listed "grey market," which sold shares to farmers and non-farmers. The value of Reox shares has gained 25 percent in the first five months since its launch (see *Irish Farmers Journal*, Dec. 30, 2006).

*Medium sized co-ops* account for 14 percent of total sales and 47 percent of members.

*Small co-ops* that process milk account for 3 percent of total sales and 5 percent of co-op members. Examples are the Newmarket co-op, which produces cheese, and North Cork, which produces casein.

*Very small co-ops* collect milk and then sell it to larger co-ops to process. For example, Boherbue Cooperative Society organizes the collection of a 4.5-million-gallon milk pool and sells directly to Cadbury's plant at Rathmore in County Kerry for manufacture of chocolate crumb, an important base ingredient in milk chocolate. In nearly all cases, the small cooperatives also operate farm supply stores and some operate grocery supermarkets, such as Supervalu outlets (an Irish wholesaler-owned chain). They account for 1 percent of the total dairy sales and 3 percent of co-op members.

### Problems and challenges

*Manufacturing milk* — Of the total Irish milk supply, 63 percent is used for butter production and 21 per cent for cheese. The price of manufacturing milk is declining because of weaker world markets and EU policy changes. Currently, the EU has surplus milk production of about 20 per cent, and

the EU Commission believes that price reductions will lead to increased consumption. In addition, export refunds have been reduced significantly, which impacts exports, according to Dr. Noel Cawley, CEO of the Irish Dairy Board. In the last year, the world market outlook has considerably strengthened.

*Casein* — The casein market is strong at the moment and is important for the Irish dairy industry, which produces almost 30 per cent of the total EU casein. Almost half of Ireland's skim milk is used to manufacture casein.

*Liquid milk industry* — The liquid milk industry is highly fragmented, with 24 processing plants run by 16 co-ops and companies. This is in marked contrast to Denmark, which is served by one liquid milk dairy co-op, and Holland, which is served by two. In the Republic of Ireland (ROI), the National Milk Agency is charged with regulating the market. Recently, this has become ineffective due to increasing imports from Northern Ireland. These imports are mainly in the form of own-label (or private-label) milk, which is cutting into the market share of the main Irish dairies.

The main beneficiaries of this trend are Northern processors rather than Northern farmers. In Northern Ireland, in contrast to the practice in the ROI, milk bought at manufacturing prices is used to supply liquid milk processors. Consumers have been moving towards "own-brand" milk, which is much cheaper than the branded products. In fact, there is enough milk being produced at manufacturing prices in the North to supply the entire ROI market.

*Supermarket own-brand labels* — The power of the supermarkets relative to processors has greatly increased. This trend has accelerated due to the

increasing use of "own-brand" labels, which restrict the prices co-ops are able to charge. Own-brand labelling identifies the product with the retailer's name, instead of the producer's or processor's name. The consumer is denied knowledge of where the product comes from and who produces it. All assurances of quality are given by the retailer, who can then source at the cheapest possible prices.

example, of the 10,842 shareholders in one of the larger co-ops, only 3,636 actually supply milk to the co-op and only 7,712 are actually alive! In addition to the member-suppliers, there are another 400 milk suppliers who are not members.

*Scale of operations* — In scale of operations, the Irish dairy industry lags behind its international competitors. In New Zealand, by comparison, Fonterra

might seem that the best way forward would be to: a) amalgamate all the existing co-ops to achieve greater scale of operations, b) cut costs by refusing to handle the milk of very small farmers and c) encourage marginal farmers to do something else with their time — perhaps convert their farm house into a bed & breakfast business and learn to nurture tourists instead of cattle!

Instead, however, Ireland's dairy co-



*This Glanbia facility in Ballyragget, County Kilkenny, includes the cooperative's headquarters offices. Photo courtesy Glanbia*

*Fewer farmers* — The continuing decline in the number of people engaged in full-time farming, especially dairy farming, is putting pressure on the turnover and profits of co-op stores, especially for animal feed and fertilizer.

*Inactive shareholders* — As farmers leave the farm and become inactive, the traditional Irish co-op problem of inactive shareholders is exacerbated. The potential for decisive control being exercised by non-users has become a serious issue in some cooperatives, including those with PLC holdings. For

Cooperative handles about 97 per cent of the country's milk. In Holland, the Friesland Coberco and Campina co-ops together account for about 80 per cent of Dutch milk. Arla Foods, with 16,700 dairy farmers and turnover of 3.8 billion euros, is the dominant co-op in Sweden and Denmark. Ireland's four largest processors (Glanbia, Dairygold, Kerry and Lakeland) would need to amalgamate to achieve similar scale.

#### **Strategic responses**

In the face of all of these problems, it

ops have shown considerable creativity in identifying new ways of diversifying their activities.

#### **Diversification and development of dairy and other ag products**

Many cooperative leaders are annoyed by criticisms from commentators about a so-called over-reliance by Irish co-ops on low-margin commodity products. They argue that reliance on commodity products happened simply because it was the most profitable option available at that

time, given the EU subsidies that were available. As times change, more and more co-ops, large and small, are diversifying.

Acquisitions and in-house innovations have resulted in quiet, but steady, diversification with value-added product lines and the opening of new niche markets. But it is not only giant co-ops such as Kerry and Glanbia that have been able to enjoy the fruits of diversification. Here are just a few examples of diversification by the smaller co-operatives:

- Lakeland's development of a food service milk business;
- Bandon co-op's involvement in growing and marketing onions;
- Connacht Gold's development of specialized herb butters for export under the Dairy Board's Kerry Gold brand and under its own brand for German supermarkets;
- Tipperary Co-op's production of Emmental and Gouda cheeses, which it markets in France through its own cheese-packing and distribution centre at Dijon.

To provide alternative income possibilities to milk suppliers with capped milk quotas, a number of cooperatives, including Tipperary Co-op, have become involved in the mushroom business. Bandon embarked on diversification into the onion business for similar reasons.

It is interesting to note that even in Denmark, the cooperative that paid the highest milk price in 2006 (and is on track for doing the same in 2007) is the tiny Bornholm co-op, which produces and markets a mind-boggling range of cheeses, including 260 varieties of yellow cheese and 25 types of blue cheese, all made to order (*Irish Farmers Journal*, Nov. 4, 2006).

### Diversification in trading and services

Both larger and smaller co-ops are engaged in diversifying their services and catering for the non-farm market. Perhaps a significant difference between large and small is that the smaller ones are more likely to be rooted in a local

community and confine their business activities to that community and its immediate neighbourhood.

Declining numbers of farmers, especially dairy farmers, Irish and EU restrictions on fertilizer use, EU commodity quotas and structural reforms resulting in less intensive farming have all combined to slow down demand for products such as animal feed and fertilizers. This has adversely impacted co-op stores, and several cooperatives have closed some smaller stores and concentrated on building up regional units with a wider selection of farm supplies.

This restructuring has not always been popular, because it further reduces communication between farmers and their cooperative. The larger cooperatives have suffered most in this regard.

In an effort to offset lost farm trade, many cooperatives have been diversifying and restructuring their retail outlets so as to capitalize on an increasing demand for do-it-yourself (DIY) supplies and hardware goods among non-farming rural dwellers and urban dwellers within their catchment area.

Dairygold Co-op has announced the launch of superstores under the new *4HOME* brand, with the intention of becoming Ireland's leading household goods and DIY retailer. Dairygold is proposing to open 30 new stores countrywide. Ten of these will be within the Dairygold milk catchment area, mainly by developing existing stores. A further 20 will be franchised outlets. The intention is to help smaller independent hardware and DIY stores compete against the major chains by 'buying in' and taking advantage of *Dairygold 4HOME*'s purchasing and marketing power.

Many smaller co-ops are adopting strategies similar to Dairygold's. For example, one of the smallest co-ops, Mullinahone, has developed a substantial hardware wholesaling business in Ireland and even has a full-time representative based in the U.K. In the words of one manager of a small co-

op, "The real market is in catering for hobby farmers and non-farming rural or small town dwellers."

Lakeland Co-op rolled out a Town and Country Stores retail concept, but more recently has been cutting back on farm stores in response to perceived inefficiencies in this sector. Wexford Co-op opened a new filling station and convenience store near New Ross in mid-2003. Tipperary, Newmarket and Boherbue Co-ops have all recently opened Supervalu supermarkets by buying into the independently Irish-owned Supervalu retail franchise. In the case of these smaller co-ops, the prime aim has been to service people in more remote communities and to maintain local employment.

This shift by dairy cooperatives to serve non-farmer customers is interesting for a number of reasons. First, the non-farmer customers are not being invited to become shareholders and join in a cooperative project. Profit and cash flow to support the core farming members are the main driving forces.

Second, the consumer emphasis is in the non-food area at a time when cooperatives and farmers are being subjected to the power of multi-national food retailers. Ireland, unlike the U.K., has no significant consumer co-op tradition in either food or hardware. Indeed, many Irish dairy cooperatives had dismantled their food shops in towns and villages around the country at about the time when the amalgamation frenzy was at its peak. This facilitated the unhindered growth of very large, privately owned food stores, such as Dunnes Stores in Ireland, Tesco and Marks & Spencer from the U.K. and LIDL from Germany.

### Non-agricultural diversification

In an effort to circumvent a declining rate of growth and falling profits in agricultural activities, both cooperatives and PLCs have been investing in non-agricultural areas. As a consequence of the rise of the "Celtic Tiger" (as the expanding Ireland

economy has been nicknamed) and the resulting property boom in Ireland, all cooperatives have been paying greater attention to managing their land and property assets.

Some cooperatives, especially those located in towns, have been relocating and/or disposing of valuable property, to the annoyance of some of their members. Some co-ops have become directly involved in the development of new commercial property interests. Both Donegal Creameries and Lee Strand cooperative have diversified into student apartments. Lee Strand has also become involved in providing urban parking spaces and its milk suppliers are being paid a four-cent-per-litre bonus from the profits resulting from this type of diversification.

### Rural development activity

Unlike most of their European counterparts, Irish agricultural cooperatives, though referred to as "dairy co-ops," are actually multi-purpose co-ops. Traditionally, they have had a broad-based developmental role. More recently, both cooperatives and PLCs have involved themselves in EU programs that promote rural development, e.g., the EU's LEADER program. Cooperatives, such as Lakelands, Town of Monaghan, Newmarket and North Cork, have drawn attention to the importance of servicing part-time farmers and providing off-farm employment. The Irish Cooperative Organization Society is also very much involved in rural development activity and offers consulting services and advice to both LEADER groups and cooperatives.

The logic of overseas acquisitions by PLCs with cooperative shareholding is supported by many farmers, especially the larger ones, as essential for development in a highly competitive global food market. Other farmers, however, especially smaller ones, are beginning to question who will really benefit from such development: milk suppliers and rural dwellers or outside investors?

Smaller farmers are increasingly

realizing that their future depends on the local availability of well-paid, off-farm and part-time employment. They are looking to their cooperatives to provide leadership and investment to this end.

Given the declining numbers of dairy farmers and the increasing scale



and economies required to dairy farm, Irish cooperatives will have to consider adopting an even broader developmental role in the rural community if they are to meet the needs of existing members. This wider focus might also provide useful roles for the retired farmer. It would also provide a wider role for those cooperatives with investments in PLCs for using their allocated surpluses from the PLCs.

The role or obligation of cooperatives in promoting broad-based development draws attention again to the membership issue. From a cooperative perspective, the development process must actively involve those to be developed. There are lessons here for cooperatives becoming involved in non-core farm

activities, whether they are large or small cooperatives.

### Marketing the co-op difference

This is one strategy which might have countered the power of the supermarkets, but it appears to have been largely ignored in Ireland. Little attempt has been made to communicate on the packaging of co-op brand products that there is something special about cooperatives — that these are businesses which are owned and democratically controlled by farmers who take a pride in the quality of their products. This is all the more surprising considering that recent surveys in America and Canada have reported that about two-thirds of consumers surveyed say that they trust cooperatives and would rather buy farm products from farmer-owned cooperatives.

A recent consumer survey suggests that Irish consumers might well have similar positive attitudes toward Irish farmers and their cooperatives.

According to a survey published by *Agri Aware*, consumers have confidence in Irish farmers as producers of quality foods. The majority of respondents perceived retailers as benefiting most from the price of foods and farmers benefiting the least.

In the age of the Enron and WorldCom scandals (not to mention recent banking scandals reported in Ireland), promotion of the cooperative difference could provide Irish cooperatives with a distinctive competitive advantage which could be difficult for others to imitate. This advantage would enable cooperatives to create a successful brand image (the sort of brand image that KerryGold has managed to create in Germany).

### Risky business?

Small can be risky, but so can PLCs. Many would argue that staying small is just too risky. The small co-op is denied economies of scale, putting itself at a cost disadvantage when dealing with the giants. Moreover, small co-ops, like small football clubs, cannot afford to buy the most expensive talent, so will be

condemned to a lingering, twilight existence in the depths of the third division.

But many of the leaders of the smaller Irish dairy co-ops point to the competitive advantages of smallness. Their arguments are supported by Arndt Reil's recent study which showed that Ireland's relatively fragmented dairy industry is, for the second year running, at the top of the profits league, well ahead of such mighty competitors as Denmark, Holland and Belgium. And, within the Irish industry, the small players have been highly entrepreneurial and are able to match and often exceed the milk prices of the giants.

Scale issues in production, marketing and purchasing are addressed with the help of a variety of federations, joint ventures and second-level co-ops. It is also argued in co-op circles that the most expensive talent is not necessarily the best. Perhaps the most successful network of cooperatives on the planet, the Mondragon Cooperative Corporation in Spain, limits the range of salaries to a ratio (lowest to highest) of about 1:6. This highly entrepreneurial group has also addressed the problem of retailing dominating the food supply chain.

The Eroski group of businesses, many of which are multi-stakeholder co-ops owned jointly by consumers and workers, has become one of the largest retailers in Spain and has achieved considerable economies of scale in its purchasing and marketing activities by setting up a joint venture with a French retailer-owned cooperative.

Perhaps the greatest risk confronting Ireland's cooperatives is the danger of demutualization, particularly in the smallest co-ops. In spite of their best efforts, many Irish co-ops, large as well as small, are in the unenviable position of having a substantial number of members who are not active farmers. This means that it may be in the financial interests of a strong cohort of non-user members to demutualize a co-op, even though it is highly efficient at meeting the needs of its user members. The PLC path brings with it the danger

of users losing control to outside investors interested in making money from farmers, not for them.

### **Co-op solutions for changing needs?**

The socio-political climate of the post Celtic Tiger years is less supportive of cooperative ways of

*The PLC path  
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working. The privatization, income tax-cutting agenda has been adopted enthusiastically. Some officials have even raised the question of whether or not cooperatives really need their own central registry. Some businesses are keen to keep a foot in both cooperative and conventional business camps.

This is perhaps why Ireland pioneered the hybrid co-op/PLC. Perhaps it is also why co-ops in Ireland seem reluctant to market the cooperative difference as a key competitive advantage. This is in marked contrast to the U.K. Consumer Cooperative movement, which is using the cooperative idea as the basis of a successful brand image.

There is also reluctance to develop new kinds of cooperative solutions to the changing problems of Ireland's agricultural co-ops. Even though some co-ops now have more workers than member suppliers, and other co-ops sell

more through their retail outlets to ordinary consumers and gardeners than to farmers, no attempts have been made to consider the possibility of developing multi-stakeholder models which could breathe fresh life into often-lackluster businesses. Again, this is in marked contrast to the innovative strategies of Mondragon and ignores Shann Turnbull's well-argued demonstration of the competitive advantages of multi-stakeholder mutuals (Turnbull, 2000) in the age of Enron.

While this paper has questioned the non-involvement of other stakeholders as cooperative members, diversification into non-agricultural activities has been driven by the desire to improve the viability of member-farmers. Agricultural cooperatives are still predominantly focused on the best ways to meet producers' needs. However, many of their diversification strategies are market-led by perceived consumer needs, but without actively involving the consumers in ownership and control.

Perhaps the most promising way forward is for consumer and producer to recognize that their mutual needs can be met more effectively only if consumers and farmers cooperate with one another. The seeds of this strategy are already evident in the farmers' markets and community-supported agriculture partnerships that are burgeoning in North America, Japan, mainland Europe, the U.K. and Ireland.

### **Cooperation between co-op sectors**

Another positive development in Ireland has been the launching in 2006 of a Cooperative Forum for Ireland. The Forum brings together all of the main cooperative sectors in the country, including farmer co-ops, housing co-ops, credit unions and community development co-ops. This has already had a valuable impact in enabling cooperation with relevant government departments in the reviewing and updating of cooperative legislation.

*Editor's note: References are available on request from the author at Michael.ward@ucc.ie. ■*



# South Dakota: great faces, great places — and great value-added opportunities



*The Dakota Provisions plant in Huron, S.D., is owned and operated by 44 turkey producers. The plant now employs 500 people and produces beef and pork food products, as well as those made from turkey. Photo courtesy Dakota Provisions*

**By Dan Schofer**

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*Editor's note: Schofer was a co-op development specialist with USDA Rural Development when he wrote this article; he recently became deputy director for outreach with USDA's Farm Service Agency.*

**S**outh Dakota's state motto, "Great Faces, Great Places," refers to Mt. Rushmore National Memorial, the Crazy Horse Memorial and many other breathtaking scenic vistas the state offers. It is also a land of great co-op and value-added venture development opportunity, which USDA Rural Development is working to promote.

"USDA Rural Development in South Dakota is interested in strengthening and developing South Dakota's rural cooperatives to provide increased economic opportunities to farmers and rural businesses," says Mike Jaspers, the state director for USDA Rural Development. "By furthering the development of agricultural products, we are securing a future for the next generation as well as providing increased economic opportunities."

Rural Cooperative Development Grants, Value-Added Producer Grants and the Small Minority Producers Grants (the later program will be featured in the next issue of "Rural Cooperatives") are all tools being used in this effort.

### **Value-Added Ag Development Center**

Since 1999, the Value-Added Agriculture Development Center (VAADC) in Pierre has been a valuable partner in helping farmers' ideas become productive, economic realities. VAADC's mission is to foster the creation of producer-owned, value-added agriculture by offering technical assistance, staff support and by championing value-added agriculture. VAADC is funded through USDA's Rural Cooperative Development Grant (RCDG) program.

Cheri Rath, VAADC executive director since early 2005, grew up on a farm near Aberdeen, S.D., and was with the Governor's Office of Economic Development before heading VAADC. Supporting the center are established agricultural-based associations, South Dakota state government agencies and South Dakota State University.

"South Dakota has traditionally lagged behind neighboring states in value-added agriculture," says Rath. "VAADC has turned that situation around with many partnerships and is now able to deliver quality technical

assistance to farmers, cooperatives and other agribusinesses. Past projects have involved aquaculture, buffalo processing and patented grain processing, all of which have demonstrated the ingenuity and entrepreneurial spirit of our farms and rural communities."

Through a vast network of federal, state and local partners, VAADC has dramatically increased its capacity to deliver technical assistance.

#### Dakota Provisions LLC

Dakota Provisions, in Huron S.D., is a state-of-the-art, poultry harvesting and processing business owned and operated by 44 turkey producers. In 2003, individual turkey growers in the community realized that they needed to capture more economic return from their birds. They were looking for a profitable, long-term market that provided stability and security. They were planning and investing for

## SDWG identity-preserved grains add value

South Dakota Wheat Growers (SDWG) began life in 1923 as a wheat pool, serving growers along the James River, which flows through eastern North and South Dakota. Today, the full-service grain and agronomy cooperative has more than 3,600 active producer-members across a region that encompasses about 37,500 square miles.

In addition to wheat, growers raise soybeans and, increasingly, corn. The rapidly expanding ethanol industry has made corn the largest volume commodity handled by the cooperative. The co-op markets more than 90 million bushels of all grain each year.

SDWG is the dominant grain and agronomy co-op of the region. Some of its central storage facilities can empty 500 trucks a day and load 440,000 bushels of grain in fewer than 12 hours. The co-op processes, transports, stores and markets grain, and offers members a menu of inputs and services.

Two joint ventures provide feed and petroleum. Six high-speed shuttle train loading facilities and eight other rail-loading facilities can link growers to ethanol plants and wheat mills to the east. They are also linked to export markets through the Pacific Northwest, as well as livestock markets.

Although SDWG is a large, diversified co-op, it still turns to the South Dakota Value-Added Agricultural Development Center for expertise (VAADC).

#### Blended grains mean added value

VAADC recently helped some of the co-op's wheat growers with a project already under way: a wheat processing facility in McLaughlin. The facility will enable the growers' cooperative to clean and blend grains to

meet flour millers' specifications for high-end flours.

Enhancing the process of segregating, blending and preserving the identity of grain prior to shipment will help area producers expand their marketing options.

For its part, VAADC staff work with all sizes and stages of development, both of producer cooperatives and of other value-added agricultural enterprises. They engage with businesses involved in grain, livestock, food processing, renewable energy, emerging technology and specialty products.

VAADC Executive Director Cheri Rath and her staff connected the co-op's management to the State AgProcessing Facility Refund monies and New Market Tax Credits. These efforts were successful, saving the co-op almost \$2.8 million for buildings, equipment and infrastructure. Co-op CEO Dale Locken says, "VAADC was instrumental in helping us...make the McLaughlin upgrade feasible." ■



*South Dakota Wheat Growers' (SDWG) wheat segregating facility in McLaughlin loads its first train. The concrete silos were already there, but the steel loading structures and new tracks were recently added. Photo courtesy SDWG*

their grandchildren's livelihood and quality of life.

In 2003, they organized an exploratory committee to look at marketing opportunities for their flocks. Working with the Governor's Office of Economic Development, VAADC organized meetings, compiled research and helped with local infrastructure issues. The research and analysis derived from a feasibility study showed that the proposed business structure and plant could be viable.

A business plan was developed using the assumptions and projections of the feasibility study. This led to the current organizational structure, financials and plant designs. The plant was financed in part by direct producer investments. VAADC helped Dakota Provisions through the funding process and forging of a comprehensive financial package.

Dakota Provisions' turkey processing plant, near Huron, also cooks beef and pork products, but is not involved with cattle or hog slaughter.

The plant came on-line in early 2006, providing ready-to-eat meats, poultry and protein products for the retail and food-service markets. The plant now employs 500 people and harvests 16,000 turkeys each day. It hopes to double that amount by 2009.

Ready-to-eat products are available cooked, oven roasted, netted or with collagen casings. For food-service customers, Dakota Provisions provides turkey breasts, boneless pork hams, natural roast beef and chicken-formed deli items, as well as deli slicing logs. Deli trays and platters with turkey, beef, pork, chicken and cheese items are available to retail partners. The plant also provides raw commodity products.

"There are very few opportunities for consumers to purchase products raised on the family farm and brought to a world-class facility that prides itself on innovation and food safety," says Rebecca Steele, director of sales and marketing for Dakota Provisions. "That is what Dakota Provisions provides."

### **Hayco Premium Forage**

Hayco Premium Forage is a partnership between a family of farmers and a processing business in Sioux Falls, S.D. Hayco owns the production and processing from seed to packaged value-added product. Products include a variety of different mixtures of high-quality forage combined with other ingredients to maximize the nutritional value for either horses or cattle. Hayco guarantees that its forage products are sun-dried, certified weed-free, blister beetle-free and dust-free. Products promote equine performance and



*Soy-based foam produced in South Dakota will be used in the seats of the 2008 Ford Mustang. Below: a sunflower snack produced by Dakota Farms International*



digestion.

The challenge that Hayco faced was to maximize the market potential of these products. "Just because you are good at sales, doesn't mean you don't need help in developing a marketing plan to take advantage of the larger market opportunities," explains Mitch Olson, director of marketing for Hayco.

VAADC helped Hayco create a unique, comprehensive marketing plan. VAADC conducted market research to determine the best and most likely customers for Hayco's premium forage products. The research showed that these target customers were

female horse owners, 30-50 years old, married in two-income households. Olson praised Rath and VAADC for providing "top-quality technical assistance."

Hayco has developed a partnership with Triple Crown Nutrition Inc. to produce "Safe Starch" brand feeds. Urban markets of the East Coast are currently the primary customers, but the marketing effort is now national in scope.

Hayco has sold shipping containers of products to livestock owners in Pacific Rim countries and is looking to expand further in this market. Recreational riders in the national parks, national forests and on other public lands are a growing market segment for Hayco because they are now required to show that any feed brought onto these lands is certified weed-free.

### **Value-Added Projects**

USDA Rural Development's Value-Added Producer Grants (VAPG) may be used for planning activities and for working capital for marketing value-added ag products and for farm-based renewable energy.

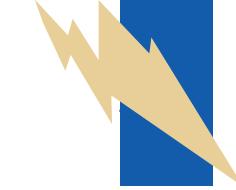
Eligible applicants are independent producers, farmer and rancher cooperatives, agricultural producer groups and majority-controlled producer-based business ventures.

### **Dakota Farms International**

The Walter family farm, near Willow Lake, S.D., incorporates more than 45 years of expertise in farming and 15 years in raising registered and certified seed. Dakota Farms International Ltd. is an agricultural products marketing company based on the Walter family farm with the objective of marketing a variety of agricultural products domestically and for export.

The company was formed in 1994 with a focus on exporting food products to Asia. In 1997, Dakota Farms completed its first shipment to Asia.

*continued on page 41*



# The Right Thing to Do



*Electric co-ops  
pursuing cutting-edge  
renewable energy,  
conservation projects*

*This 18 megawatt Minnesota wind farm is owned and operated by Dairyland Power Cooperative. Wind is just one of a number of renewable energy resources being developed by the nation's rural utility cooperatives. Photos courtesy Dairyland*

**By Anne Mayberry**

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mong the challenges facing the electric utility industry today is the need to address climate change. Increased energy efficiency and conservation, combined with alternative fuels and technology, will all play a role in reducing carbon dioxide emissions and dependence on traditional fuels.

Efforts to make significant improvements in clean-coal technology are underway because coal is still among the most reliable and affordable sources of baseload power. Indeed, coal is the source of about 50 percent of our nation's electricity. Rural electric cooperatives, owned by the consumers they serve, recognize the need to dramatically reduce carbon dioxide emissions without huge run ups in electric rates.

The Electric Power Research Institute (EPRI) earlier this year released a study on how technology can

reduce the cost of cutting carbon dioxide emissions while meeting the growing demand for electrical power. While much of the technology still needs to be developed for efficient commercial use, EPRI points out that energy efficiency and renewable energy projects are the first steps to reduce carbon dioxide emissions.

"Rural electric cooperatives are among the leaders in the electric utility industry when it comes to implementing innovative alternative energy programs," says James Andrew, administrator of USDA Rural

Development's Rural Utilities Program. "Cooperatives are owned by their members and answer to their communities. They want to find ways to reduce carbon emissions while continuing to provide safe, reliable and affordable electric power."

As a result, phrases such as "carbon sequestration," "biomass," and "methane digestors," uncommon a generation ago, are now used on a regular basis.

### **Basin Electric's renewable energy**

Basin Electric Power Cooperative in North Dakota has a history of developing alternative energy, conservation and efficiency programs. Basin Electric currently has research projects underway on both carbon sequestration and clean coal.

"In 2005, our consumer members passed a resolution to have 10 percent of generating capacity provided by renewables," Daryl Hill, spokesman at Basin Electric, explains. "Many of our members are farmers and ranchers. They support strong environmental standards."

Basin Electric's subsidiary, Dakota Gasification Co., is involved in the largest carbon dioxide (CO<sub>2</sub>) sequestration project in the world at its Great Plains Synfuels Plant, near Beulah, N.D. It is the only commercial-scale coal gasification plant in the country.

Because carbon capture technology for coal-fired electric utilities is still new, Basin Electric is planning to evaluate carbon dioxide removal technologies for coal-based power plants at its Antelope Valley Station, also near Beulah, to determine which, if any, are technically, economically and commercially feasible.

Basin Electric and other electric utilities with older coal-fired, baseload plants are assessing their investments because continuing to supply consumers with reliable, low-cost energy while meeting environmental responsibilities requires a balance. "We have an obligation to serve our members," Basin Electric CEO Ron Harper notes. "We

also have an obligation to grow responsibly and cleanly. We are committed to responding to the world's need to reduce carbon emissions. It won't be without challenges, but it's the right thing to do."

### **Support from USDA Rural Development**

USDA Rural Development's Utilities Program is providing financial assistance in the quest to increase use of alternative sources of electric power. It made a \$36 million loan to finance a heat-recovery project that captures waste heat from pipeline compressors. The project will generate more than 20 megawatts of electricity.

Another Utilities Program loan recently helped support a breakthrough project to produce hydrogen from renewable resources, such as wind. Basin Electric's wind generation portfolio has a capacity of about 135 megawatts and will be expanding.

Basin's wind-to-hydrogen demonstration project would allow electricity produced from wind to produce hydrogen, which could then be used as a transportation fuel or to produce electricity when wind resources aren't available. It's the first project of its kind in the region.

U.S. Sen. Byron Dorgan was on hand for a dedication ceremony at the end of July. Dorgan noted that "This project is a breakthrough for North Dakota and the wind and hydrogen energy industry as a whole. This demonstration will give us an idea of what the future might look like."

### **Cleaner burning coal & wind**

Rural electric utilities in South Carolina also recognize the value of burning cleaner coal. Because as much as 70 percent of their electric power is generated by coal-fired plants, co-ops there are partnering with the University of South Carolina to establish a Center of Excellence to research cleaner, more efficient methods to burn coal.

Mike Couick, CEO of Electric Cooperatives of South Carolina, says this statewide association has always

promoted conservation. "While the United States is considered the OPEC of the world in coal reserves, we have to work toward smarter use of our energy resources. Conservation is just part of the story. We want to make sure we have enough electricity in the future, and make sure it's as clean as it can be," Couick said.

Chicago is known as the Windy City, but a more rural area to the city's south was recently honored as the wind cooperative of the year by the U.S. Department of Energy. Illinois Rural Electric Cooperative is the first co-op in Illinois to erect a wind turbine, an effort that was supported with a \$1.3 million USDA Rural Development Utilities Program loan.

Sean Middleton, the co-op's manager of engineering explained, "We at Illinois Rural believe that if you can generate electricity from renewable resources at the right price, it's the right thing to do." This project not only generates additional electrical power, but future growth could add millions of dollars to the local tax base.

### **Co-ops investing in biomass**

In addition to wind power, rural electric cooperatives are adding biomass energy to their portfolios. Anaerobic methane digestors are a type of biomass energy — electrical power generated from wood waste, agricultural byproducts and animal waste. In addition to 18 megawatts of wind-generated power, Dairyland Power Cooperative, a generation and transmission cooperative in Wisconsin, uses landfill gas-to-energy plants to produce enough power for 8,800 homes and "cow power," through an animal waste-to-energy process, to power 1,500 homes.

Neil Kennebeck, director of planning for Dairyland, explains that anaerobic digestion of animal waste reduces the potential for ground and surface water contamination, and reduces the need for pesticides and herbicides on the farm.

"Dairyland's programs receive excellent support from members,"



*Dairyland's Five Star Dairy Farm uses a digester (upper left) to produce methane gas from animal waste, which is used to power generators. Another source of renewable energy, Seven Mile Creek Landfill Generating Station (upper right), uses waste from landfills to generate electric power. The Lake Mills, Iowa, landfill gas-to-energy facility (left) also generates renewable energy from methane gas.*

Kennbeck says. "We're ahead of the regulatory requirements for use of renewables; Dairyland has been developing alternative energy sources since 1998."

Dairyland's conservation programs are popular among the membership. One example is the cash incentives for members to purchase energy-efficient heat pumps and other appliances. Additionally, Dairyland and its rural electric cooperatives have given away about 10,000 high-efficiency, compact fluorescent light bulbs so far in 2007.

#### **Meeting demands of growth**

Florida is one of the fastest growing states in the nation and the demand for electric power there is increasing at an even faster rate. Seminole Electric Cooperative Inc. is looking at a number of solutions to meet the demand for electric power, which in Florida is growing 4 percent annually.

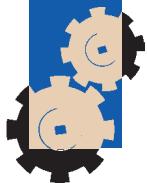
"We have one of the largest in-state portfolios of renewable energy — about 75 megawatts — which meets 4 percent of consumers' needs," notes Executive Vice President and General Manager Tim Woodbury. Seminole is one of the largest nonprofit generation and transmission electric cooperatives in the United States, providing wholesale power to 10 rural electric distribution cooperatives.

Seminole recently formed a partnership with Landfill Energy Systems (LES) for use of methane from municipal landfills to generate electricity. LES will build two landfill gas-to-energy projects — its first in Florida — and Seminole will get 15 additional megawatts from these two projects, giving the co-op enough renewable capacity to power 50,000 homes.

"Seminole is working to build its renewable portfolio with cost-effective

projects because they're a win for our members and the environment," says Jeff Fela, Seminole's senior public affairs representative. Like more than 90 percent of the rural electric cooperatives, Seminole is also actively promoting energy efficiency, including use of compact fluorescent lighting.

Electric cooperatives nationwide — often in response to their consumers' requests — have played an active role in alternative energy, conservation, and efficiency programs and are increasingly looking to technology to help address climate change. EPRI's study notes that all technologies — ranging from efficiency and renewable energy to carbon capture and distributed energy — will play a role in protecting the environment while meeting the need for affordable, reliable electric power. ■



# New Hybrid on Great Plains

*Increased consumer access, education paying off for local producers & shoppers*



**By Jane Livingston,**  
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In 2004, the Food Processing Center (FPC) at the University of Nebraska was researching ways to improve the profitability of small farmers in the region. Its producer-driven research showed that farmers wanted better ways to distribute and market their food locally. At the same time, consumers were saying they had a hard time finding enough locally produced food.

In a survey of existing producer-consumer linkages around the country, the FPC came across the Oklahoma Food Co-op. It had many of the attributes the Nebraskans were looking for, including strong leadership. They invited the co-

op's dynamic president, Bob Waldron, to speak at the annual banquet of the Nebraska Sustainable Agriculture Society. The event was attended by staff of the Nebraska Cooperative Development Center (NCDC), which has joined FPC in supporting the Nebraska effort.

## How the hybrid model works

The Oklahoma Food Co-op is owned by its members, as are all food co-ops, but it is unusual in that it has both vendors (producers) and customers (consumers) as members. It's also different in that it has no storefront or market stall. Instead, the co-op maintains a "virtual marketplace" on a Web site where vendor-members each month post their available products.

These vendor-members set their own prices and fill orders

placed on-line by customer-members during a week-long ordering window. Deliveries are made to a central drop-off site and sorted so that customers pick up a single order and pay a single invoice.

As the Nebraska group discovered, there are other benefits to the on-line hybrid co-op model. Vendors — farmers, ranchers and value-added processors, such as bakers — also post their methods of production, product details and other important information for consumers on the Web site.

Educating customers about their food is a priority for many producers. Now, the co-op's member-customers have easier access to local food and information about it.

The Nebraska co-op was launched quietly during the midst of the summer growing season of 2006. The plan was to "go slow," feeling its way forward during the first year. By May 2007, the co-op had grown to around 120 members — including about 24 producers. By August, the membership had climbed to 171, including 33 producers, with more new members joining every week.

#### **Developer's role**

"They really took the ball and ran with it," says FPC's Mark Hutchison about the proactive role taken by NCDC, which also awarded the co-op a small grant to cover legal fees



*The Village Pointe Farmers Market in Omaha, Neb., counts a number of Nebraska Food Co-op producer-members among its vendors. Opposite page: Farmers markets are great places to teach children about nutrition and marketing skills — and to have fun! Photos courtesy Village Pointe Farmers Market*

as the innovative, hybrid-ownership model was hammered out. In addition, NCDC helped the co-op procure a liability insurance plan for producer members — a big draw for small-scale farmers and ranchers who want to sell to institutional buyers, such as the university.

## **CooperationWorks! draws top names to training program**

CooperationWorks!, the national co-op of cooperative development centers, has recruited some highly regarded instructors to the faculty of its popular training program: "The Art and Science of Cooperative Development." The program consists of two intensive five-day sessions.

In September, James Baarda, an agricultural economist with USDA Rural Development's Cooperative Programs, and long-time co-op developer Gerald Ely, who served as director of USDA's Cooperative Development Division from 1990 to 1995, joined other co-op leaders to inform and instruct participants in the second session of the 2007 program.

Topics included co-op legal and tax matters, finance and capitalization strategies, feasibility and financial analyses, governance and management issues, conflict resolution and developing stakeholder capacity. CooperationWorks!' curriculum combines case studies, site tours, small group work and presentations.

The spring session of the 2008 program will be held in Madison, Wisc. For more information, contact: Audrey Malan at: [cw@vcn.com](mailto:cw@vcn.com) or (307) 655-9162. ■

Co-op Vice President Libby Broekemeier (also one of the co-op's most active consumer-members) says, "Having some resources lined up — the planning and development grant and the funding for legal advice — and just having those folks with us — was a big help. It gave us the sense that we'd have the money and other resources we needed to take the next step."

Broekemeier, a professional volunteer coordinator with prior experience in food co-op marketing, has (like the other 10 board members) generously shared her expertise with her co-op. She organizes the monthly Delivery Days to meet the expectations of both producers and consumers, and to make sure volunteers have a good time working together.

"A real key to the co-op's success," says NCDC's Cranford, "is that it addresses distribution. By pooling their resources and getting all the product together at once in the same place, producers are leveraging their valuable time." Some farmers and ranchers even organized themselves so that only a few drivers have to make the delivery run each month.

#### **Volunteers with vision**

Although the co-op depends on a few volunteers to sort each month's orders at the two drop-off sites, Hutchison notes that farmers already put in longer hours than most people. By becoming member-owners of the cooperative, they reallocate some of those hours in order to better move

*continued on page 40*



*Brian Foster is one of 28 employee-owners of CENTROL, a crop consulting business in Twin Valley, Minn. Employee-ownership proponents say this business model can help many types of rural businesses survive. Photo courtesy CENTROL*

# Worker-owned/ESOPs can help preserve business in rural America

**By Bruce J. Reynolds, Economist**  
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**E**mployee ownership can help a business prosper by creating financial incentives for performance and by providing more self-management of working conditions and policies. These benefits may accrue whether businesses are organized as cooperatives or as Employee Stock Ownership Plans (ESOPs) when workers have a majority control.

Employee owners in rural communities also help retain businesses that may otherwise be closed down. Worker cooperatives and ESOPs are more prevalent in some urban centers of the United States, but conditions are favorable for

their expansion in rural America. Worker cooperatives operate a wide variety of businesses, as demonstrated at a recent conference (see sidebar, page 31).

This article examines the potential growth of worker-owned businesses in the rural economy.

## **CENTROL Crop Consulting**

Many rural businesses, especially in farming areas, were historically established as farmer cooperatives to provide better marketing services and farm supplies for their members. As farmers use more specialized and technologically complex agricultural services, there can be efficiencies for them to target which ones are most and least critical for their ownership and control. Spin-offs from farmer cooperatives that involve employee ownership may improve operations of some services and, at the same time,

concentrate farmers' business monitoring and governance where they can have more impact, as shown by the example of CENTROL, in Twin Valley, Minn.

Services such as CENTROL's — with highly individualized staff expertise not centered in a hierarchy of management and supervisors — are readily operated as worker-owned businesses. CENTROL Crop Consulting assists farmers in agronomic decisions. At one time it was owned by local farmer cooperatives and CENEX (now CHS), but in 2002 it was spun-off as a 100 percent worker-owned ESOP.

One reason for CENTROL's conversion is that agronomic consultants often leave farmer cooperatives to start their own businesses, but may create firms too small to offer jointly shared expertise. Dennis Bergland, CENTROL's CEO, points out that its primary asset is the expertise of its staff of 28 consultants. And although their work is carried out individually, they work together in sharing information.

Ownership by the staff has improved performance and the prospects for longevity of the business. Like a cooperative, CENTROL has democratic governance.

### **Home care market**

Most jobs in rural areas are in non-farm services, and the off-farm share of employment is steadily increasing over time, according to a study by USDA's Economic Research Service. Retirement related services, such as home care, are a growth segment for both the urban and rural economy.

Home care businesses are ideally suited to be owned by their workers. Indeed, the largest worker cooperative in the United States is Cooperative Home Care Associates in New York, which has inspired the formation of similar cooperatives in several cities.

Home care services can greatly improve quality of life in small towns that lack specialized housing and care centers for the elderly. Since many seniors want to remain in their communities, they will seek home care that enables them to age in place. Recent cooperative development work by local

community action agencies and USDA Rural Development's office in Wisconsin has helped establish home care cooperatives in rural communities (*Rural Cooperatives*, May-June 2003).

Cooperatives provide the elderly with care-givers who are owners of the business, with a larger stake in maintaining quality than hired workers. This advantage is particularly important for elders who receive unsupervised care in their homes.

These two examples are encouraging because of the potential in rural America for either start-up worker owned businesses or for sustaining small businesses as cooperatives or ESOPs.



*The success of Cooperative Home Care Associates in New York has inspired many similar employee-owned co-ops to be formed, including this home care co-op in Wisconsin (seen during a board meeting).*

ownership to their employees may offer mutual benefits.

John Logue of the Ohio Employee Ownership Center finds that as sole proprietors in urban areas sell their businesses, they often either find another proprietor/investor or are bought by a larger business seeking multiple locations. By contrast, he observes, retiring-owner sales of rural businesses more often result in closure.

Competing firms often buy such businesses to acquire inventory and customer lists and are not interested in operating at these locations.

Such acquisitions are frequently closed and the employees are released. It may not always be the case that these locations are unprofitable. The employees might be able to own and operate a sustainable business that benefits themselves and local customers.

Self-employment entities, without any hired employees, are by far the most numerous type of business in the United States. But most rural jobs are provided by small businesses that employ workers, defined as having fewer than 500 employees. The Small Business Administration (SBA) reports data for several different sizes of businesses based on their

employment range ([www.sba.gov/advo/research/st\\_msa\\_nonmsa95\\_04.txt](http://www.sba.gov/advo/research/st_msa_nonmsa95_04.txt)).

Rural businesses in selected ranges of employment size for three regions of the United States in 2004 are reported in the table below. It includes subtotals for the four different ranges of employment size. There were 198,590 small businesses reported for rural America in 2004. Of rural businesses with employees, the most common size is 5-9 employees. Businesses that employ from 10-19 and 20-99 workers each account for more than 46,000 businesses in rural America.

benefit to retiring owners for keeping a small business going by selling to its employees.

### 1042 Rollover

Changes in federal tax laws in 1984 provided for deferment of capital gains taxes on stock sold to employees. The initial owners defer the tax by rolling the proceeds into another business investment, and hence it is dubbed the "1042 rollover." The investment rollover can include a simple purchase of stock in a U.S.-based company, but its key feature is the incentive created

percent of a company, they could gradually transfer more ownership to employees and take the 1042 rollover on all incremental transfers.

Furthermore, as pointed out by Dan Bell of the Ohio Employee Ownership Center, when ESOPs have a majority share of ownership they can establish effective democratic governance of the business.

While ESOPs are more flexible than cooperatives in regard to ownership shares, they involve more administrative cost because of their regulatory linkage to the Employee Retirement Income

### Rural businesses in selected ranges of employment size, 2004

Employees	5 - 9	10 - 19	20 - 99	100 - 499	Row totals
West	19,492	11,612	11,306	5,628	48,038
Central	37,003	21,472	22,188	11,923	92,586
East	23,947	13,734	12,741	7,544	57,966
Rural U.S.	80,442	46,818	46,235	25,095	198,590

*Source: Small Business Administration*

Of course, there is no way to know how many of these firms have family members or other sole proprietors lined up for ownership succession. Many small businesses lack a succession plan and the owners are unaware of the advantages of selling to their employees. SBA reports that about 30 percent of family-run companies succeed into the second generation, but only 15 percent survive into the third generation ([www.sba.gov/success-series/vol7/success.txt](http://www.sba.gov/success-series/vol7/success.txt)).

These employees are likely to prefer keeping their jobs and the retiring owners may want to see their lifetime of work survive as on-going businesses. Customers are better off if the local businesses they patronize keep operating. There is, in fact, a special tax

for proprietors or owners in a closely held business to develop a succession plan of transferring ownership to employees.

ESOPs have been more frequently used for the 1042 rollover than worker cooperatives. One reason for this is that accomplishing a 100 percent purchase of many companies by employees in a 3-to-5-year period can be financially prohibitive. Whether organized as an ESOP or a worker cooperative, 30 percent of the stock must be purchased in the first year as the minimum amount to qualify for a 1042 rollover. But a worker cooperative, unlike an ESOP, cannot remain for the long-run with 30 percent ownership.

The ESOP is flexible in this regard because if outside investors owned 70

Security Act (ERISA). Such costs include the appointment of a trustee to administer the reporting requirements for holding employee shares as part of their retirement plan and having annual firm value appraisals. In the case of CENTROL, they incur annual ESOP costs of about \$10,000-\$15,000. A worker cooperative is not subject to ERISA regulations, so it can be applied to businesses with relatively small employment and modest earnings.

### Challenges in ownership transfers

The transfer of ownership to a worker cooperative during a relatively short period of three-to-five years is challenging. Technically, a 100 percent ownership transfer follows in a matter of days or months after a cooperative is

formed, but the original owners become members of worker cooperatives with a maximum of 70 percent of the equity.

Over the following years, the cooperative is committed to redeeming the remaining 70 percent of the original owners' member equity. Succession plans aim to accomplish such redemptions in a relatively short time frame, such as three-five years, but flexibility can be built into these agreements to deal with economic contingencies.

Another challenge is the transfer of management know-how in leading and administering an effective business operation. Many small business owners doing hands-on management may not have bothered with written policies and operating manuals. During the period of their membership in a worker cooperative, they need to put their know-how in writing and transfer their specialized knowledge to the new leadership of the business.

Worker financing of the initial 30 percent of the business and subsequent purchase of the original owner's remaining shares usually requires the cooperative to borrow from a bank. For businesses with good customer relations with a local bank, continued banking relationships to help cooperatives sustain operations would be desired by all parties.

USDA Rural Development can play an important role in assisting small business owners with certain key aspects of succession planning. Foremost is disseminating information about opportunities in transferring ownership to employees. Other policy actions may include various types of financial support to workers interested in owning the company where they are employed.

These types of support may include grants to enterprises or to rural development centers and making it possible to use loan guarantees.

The impact that worker cooperatives can have on the rural economy in retaining businesses and jobs has not been accorded sufficient recognition. This strategy deserves a place on the agendas of rural development planning and policy discussions. ■

## Worker-owned businesses share ideas during North Carolina conference

Workers who run their own cooperative businesses came together at the University of North Carolina campus in Asheville, N.C., for the Eastern Conference for Workplace Democracy (ECWD), July 20-22. It was the first time the conference has been held in the South.

The event was hosted by the Southern Appalachian Center for Cooperative Ownership and the Federation of Southern Cooperatives/Land Assistance Fund, a group of 35 predominantly black farmer cooperatives and credit unions in Alabama and Mississippi. The event drew 145 people from 24 states, including members of other cooperatives, unions and other organizations.

The ECWD is a regional organization of employee-owned and -operated businesses, including worker cooperatives and Employee Stock Ownership Plans (ESOP). Members include Equal Exchange, a fair-trade coffee and cocoa producer near Boston; Chroma Technology Corp., a 100 percent employee-owned ESOP lens manufacturer in Rockingham, Vt.; and Little Grill Collective, which operates a café in Harrisonburg, Va. ECWD is a regional partner of the United States Federation of Worker Cooperatives (USFWC).

With a theme, "Building Cooperation East and South," the conference organizers this year hoped to help re-ignite the worker cooperative movement in the South, which was home in the 1980s to 11 worker cooperatives, many of which are no longer operating.

Conference-goers heard a keynote by former United Steelworkers President Lynn Williams, who has helped convert traditional businesses to worker ownership. A tour of local co-ops, a fundraising auction, films on worker cooperation and a skit by young people were also part of the conference.

A committee was formed to work with the USFWC to collaborate with unions to foster worker cooperatives as a possible solution to job loss and for mutual support. The resolution also called for supporting legislation for a U.S. employee-owned bank.

Participants in one session discussed finding concrete ways of working with other types of cooperatives, such as the need for a local farmer network to help restaurant co-ops to find local produce. Worker co-ops were also considered as a possible strategy to provide jobs for the hard-to-employ, and to help to provide jobs and bring services back to New Orleans.

"The conference provided many opportunities to talk with other cooperative leaders about the key issues cooperatives face, from structure issues, to capitalization challenges, to questions of member participation and governance," said Lynn Benander of Co-op Power, a consumer-owned energy cooperative.

For a more detailed version of the ECWD history, visit:  
<http://www.usworker.coop/about/history/regional>. ■

— By Ajowa Nzinga Ifateyo  
Eastern Conference on Workplace Democracy

Heartland Cooperative in West Des Moines, Iowa, has grown through a number of mergers, and today has 340 employees and projected sales of \$560 million. This grain bin in Rippey, Iowa, was built in 2006. Photos courtesy Heartland Cooperative



# Corn Condos for Sale

*Growth and innovation key to Heartland Co-op's success*

**By Stephen Thompson**

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The strategy for success for Iowa's Heartland Cooperative is based on an aggressive approach to growth, providing superior customer service and business innovation at all levels of the operation.

Heartland, a West des Moines-based marketing and service cooperative for farmer-members in central Iowa, has grown through consolidation and merger with more than a score of smaller cooperatives, some going back to the early years of the 20th century. The latest merger occurred July 1,

when it joined with the smaller Central Counties Cooperative, creating a co-op business with 340 employees and projected annual sales of more than \$560 million.

Innovations include new grain storage options for members and offering increasingly advanced levels of precision agriculture to help ensure that farmers apply only the fertilizers and crop protectants needed.

## Grain 'condos'

One recent innovation is Heartland's "grain condominium" program, which provides storage space for members. The cooperative didn't invent the grain-condo concept, but co-op management adopted it after taking a

careful look at existing arrangements in North Dakota and Minnesota.

Grain storage is, of course, a vital part of doing business for commodity farmers. Being able to store grain after harvest frees producers from having to sell when prices are seasonably low. Shortages of grain storage space in recent years, combined with transportation bottlenecks, have resulted in grain in some areas being stored outdoors for extended periods. This often results in quality losses.

One answer is for farmers to build storage facilities themselves. This not only requires a sizable capital investment; farm-based storage also imposes costs and inconveniences that many farmers would prefer not to deal with.

Under Heartland's condo program, an LLC is set up as the ownership entity for two storage bins, each of which can hold 500,000-700,000 bushels of grain. These are built on co-op property near an elevator.

Shares for 5,000 bushels of storage are available to co-op members for \$5,750 each. The shares are valid for the life of the facility and are freely transferable. Just as important, the owner retains title to the grain, so he or she can continue to participate in USDA non-recourse marketing loan programs. The 5,000-bushel storage rights apply to any combination of soybeans and corn. Members can call ahead before delivering to arrange for proportions.

### Many advantages

The grain-condo project offers numerous benefits to farmers. Besides being substantially cheaper than the equivalent space in grain bins built on the farm, the facilities are constructed of more durable materials and potentially offer a much longer service life. In addition, much of the worry and bother of maintaining on-farm grain bins are thus eliminated for the farmer.

The risks of storage, such as quality issues, are transferred to the LLC, and, without the day-to-day responsibility, farmers are free to travel – all without paying commercial storage prices.

"A lot of our members are in their fifties or older," says Tom Hauschel, executive vice president for grain. "And they don't like having to climb to the top of the bin to inspect the grain. The co-op takes care of all that."

Shareholders are billed for electricity, maintenance, insurance, handling and other expenses at a current rate of \$230 per year. Another benefit: though each shareholder owns part of a specific storage facility, he or she can take their grain to any of the participating storage sites, adding a welcome measure of flexibility.

In keeping with the co-op's business philosophy (see sidebar), the grain condominium project helps not only its members, but the cooperative itself. "We only have so much capital," says Hauschel. "Not having to spend it on additional storage allows us to focus on new receiving capacity, so we can serve more communities."

The grain-condo project was started in 2005 in

## Core business principles guide Heartland

Heartland CEO Larry Petersen says the Iowa cooperative is run in accordance with six core business principles:

- Profitability — both for members and for the cooperative. Petersen says that the cooperative exists to help its members grow and prosper. But that mission requires good profitability for the cooperative itself, so that it can best serve its members' needs.
- Adherence to honesty and ethics in running the business.
- A willingness to confront hard facts — to "take the bull by the horns," in making decisions. "We took a good look at getting into ethanol production," says Petersen, "but after two years we decided it wasn't a good fit for us. We do have small investments in ethanol, but we think that our own plant would expose us to some serious risks. Currently, there's such a euphoria about the whole industry that some kind of shakeout is bound to happen."
- Empowerment, with accountability, for co-op employees. "We don't believe in a centralized management model," says Petersen. "We think we have to allow our people on the front lines to make decisions." That means employees must be held accountable for their actions. However, Petersen stresses that they mustn't be afraid of making the inevitable mistake once in a while. "You have to allow people to have occasional failures without fear of losing their jobs," he says. This approach requires training and on-the-job coaching to be effective, Petersen says. "You've got to have the right people for the job. Some people are just too nervous to accept the responsibility."
- An orientation toward growth. "We keep an eye open for possible mergers," says Petersen. "And we're constantly exploring new ways to pick up market share."
- Continuous improvement. "We're always looking at ways to improve processes," Petersen says. ■

cooperation with six other Iowa cooperatives. Together, they hired counsel to draw up the legal documents. Each co-op runs its own condominium project. They share only the jointly developed legal framework.

Other member services include such standard service co-op programs as agronomy services, livestock feed and petroleum supply. Heartland also offers training in the principles of grain marketing.

## Taking precision ag to next level

Heartland's efforts to expand its support for precision farming is another major thrust of the co-op, Heartland CEO Larry Petersen says. Precision agriculture uses data on variations in soil conditions and plant development in a single field to determine such variables as seed planting density and depth, and chemical application, from one part of the field to the next. Satellite monitoring and Global Positioning System (GPS) data are used to automate these processes.

Using technology available today, precision agriculture systems can determine the position of a piece of farm machinery to within a centimeter, and application rates can be controlled just as precisely. The benefits include greater yields and lower costs while preventing wasteful chemical application, cutting down significantly on harmful runoff.

"Precision ag isn't new, but we're taking it to the next level," says Petersen. Heartland offers cutting-edge, precision ag technology in alliance with two Iowa-based companies, KINZE Manufacturing Inc. and Ag Leader Technology Inc. But technology is only part of the equation. "Having a good



*Heartland was inspired to begin its "grain-condo" program by similar systems in North Dakota and Minnesota. These three bins in Malcom were erected in 2004-2006.*

working relationship with the farmers is just as important as offering the right services."

Hauschel is quick to point out the advantages of size in serving the needs of co-op members. "We have a large elevator base, and that gives us better access to more markets," he says. "We get a lot of direct pick-ups to ethanol plants." And Heartland's merger with Central Counties further enhances its marketing advantages.

## Merger offers better rail transport

Heartland's recent merger with Central Counties Cooperative fits well with its core principles, Petersen says. The two co-ops had little geographical overlap, and didn't really compete with each other, except possibly at two locations. Their corporate cultures were compatible. Moreover, Central Counties operated a shuttle-train loading facility on the Union Pacific Railroad and one on the Iowa

Northern — both of which, Petersen says, will integrate nicely with Heartland grain-handling facilities. Iowa Northern is an innovative line known for offering shippers switching services on its tracks, saving time and money.

"We have a Union Pacific loading site elsewhere, along with a Norfolk Southern facility in Des Moines and four locations on the Iowa Interstate Railroad," Petersen says.

Together, the locations will offer a higher degree of flexibility in shipping grain to markets on the West Coast, the South and the East. Hauschel puts it this way: "At different times of the year, some markets pay more for grain than others. But to take advantage of the better price, you have to be able reach that market economically and on time. Having multiple access to more rail routes means that we're better positioned to do that."

"It's not full arbitrage," says Petersen, "But the Central Counties facilities will be closer to some of our locations."

Merging the two co-ops did not mean that employees were let go. Speaking before the merger was completed, Petersen emphasized, "We're committed to keeping everyone. Some may have to change locations, but we're going to try to keep the inconvenience to a minimum."

## Management duties shift

In such mergers, it's usually the upper managements that are most affected. The new Heartland found room for Central Counties executives, some with similar positions, others whose responsibilities changed markedly.

Mark Melhus, the former CEO of Central Counties, is now vice president for operations. He says that the transition has gone "as well as can be expected." The Central Counties facilities have been incorporated into the existing business structure, requiring employees to learn new practices and adapt to new equipment.

Adopting Heartland's accounting system meant new computers and software. "People are learning a lot of new stuff," says Melhus, who adds that the inevitable small mix-ups and delays have caused some frustrations for customers.

Asked how Heartland's different corporate culture has affected employees, Melhus says, "It depends." Heartland's "empowerment" doctrine means that facilities managers are being asked to do more in some ways, but in others things are more centralized.

Petersen says that the Central Counties merger won't be the last.

"The board continues to see that consolidation has positive benefits for our producers," he says. While the co-op has no immediate plans for further expansion, "We're keeping the door open for when something appropriate comes along."

Petersen says he believes that mergers not only improve infrastructure, but help reinvigorate the organization. "You get new expertise. You get to see how the new people do things differently. It's a chance to re-create the company." ■



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## AGP rejects hostile takeover bid

Ag Processing Inc. (AGP), an Omaha, Neb.-based soybean processing cooperative, has rejected what it terms a "hostile takeover bid" made by Ag Processors Alliance LLC (APA), a company that was recently formed to attempt to buy the co-op. The would-be-buyer is offering \$850 million for AGP, which is owned by more than 200 Plains and Midwest grain cooperatives.

AGP, which had \$2.4 billion in sales and earnings of more than \$62 million in 2006, held a special board meeting in mid-August to respond to the unsolicited buyout bid. "AGP's board of directors and management staff maintain a constant and open dialogue with member-owners, and there has been no interest expressed in selling the company," said AGP President and Board Chairman Brad Davis. "AGP continually reinvests in our core business, and our members have expressed support for the strategic direction of their cooperative.

"This hostile attempt is not in the best interest of AGP, our cooperative members, or their business operations either today or in the future," he continued. "After review, the unsolicited bid was soundly rejected by the AGP board of directors and we do not intend to have any discussions with this newly formed group."

"It's done, finished, over," Mike Maranell, AGP senior vice president, told the *Omaha World News*. "Our board of directors doesn't want to do business with those people. Our board responded very firmly, and the answer was 'No.' I don't think there's going to be any meetings."

The paper also quoted Mark Lakers, president of Ag and Food Associates, as saying he believed a majority of AGP's member co-ops want the board to consider the offer. He said APA planned to hold informational meetings in late August to explain the offer and to answer questions.

AGP member cooperatives each hold one vote. ■



*Ag Processing Inc., with annual sales of \$2.4 billion, is resisting a hostile takeover bid.*  
Photo courtesy AGP

### Retiring dairy farmers concerned by production costs, succession issues

Most of the 333 farmers who participated in Cooperatives Working Together's (CWT) fourth herd retirement this year cited high production costs as a key reason why they chose to sell their herds, according to a survey. CWT mailed questionnaires to all of those farmers whose bids were accepted in the CWT herd retirement earlier this year. About 62 percent of the 333 farmers returned the survey, conducted to provide greater insight into the reasons why producers submit bids and whether they intend to continue dairy farming in the future.

Major factors cited in making the retirement decision included:

- Increased production costs: 59%
- No one to pass the dairy on to: 40%
- Pursue other types of farming: 37%
- Wanted to retire: 26%
- Family health issues: 25%
- Financial difficulties: 20%
- Environmental pressures: 15%
- Pursue non-farm employment: 12%
- Opportunity to start with a new herd: 8%
- Opportunity to sell farm: 7%
- Wanted to move dairy: 1%
- Other: 4%.

Three-quarters of the producers were age 50 or older. More than half relied on dairying for more than three-quarters of their income.

Just 12 percent said they planned to enter dairy farming again, with 80 percent of that group planning to start again at their current location, but most with a smaller herd.

CWT Chief Operating Officer Jim Tillison said that the survey "confirms that increased production costs, especially high feed and fuel expenses, have really changed the economics of the dairy sector, to the point where they are pressuring some producers out of the business."

"The survey is also consistent with anecdotal stories and survey results from previous herd retirements that while economics drives many to submit bids, many producers also are looking for an opportunity to stop dairying permanently because of health or family succession issues," Tillison said. "In fact, many just want a graceful way to exit the business after many decades of milking cows."

Cooperatives Working Together is being funded by dairy cooperatives and individual dairy farmers, who are contributing 10 cents per hundredweight assessment on their milk production through December 2007. The money raised by CWT's investment is being apportioned among several supply reduction programs to improve the national all milk price. For more on CWT's activities, visit [www.cwt.coop](http://www.cwt.coop).

### **DFA closing Calif. cheese plant**

Dairy Farmers of America Inc. (DFA) has announced changes to its American cheese division, including the closure of the cooperative's Corona, Calif., cheese plant and the transfer of DFA's American cheese (large-bag shredded and packaged) business in Corona and Zumbrota, Minn., to Wisconsin-based Schreiber Foods Inc.

The cheese plant has lost much of its local milk supply as housing development in the Chino Basin has accelerated in the past decade. Many dairy farms have relocated to the state's San Joaquin Valley or other states.

More than 300 employees at DFA's Corona facility were notified that the facility would operate at a reduced capacity beginning Aug. 31 and would cease production of American block cheese and whey products by Dec. 31. An additional 70 employees at the



*High production cost was the biggest reason for producers retiring their herds under the CWT program. Photo by Larry Laszlo*

Zumbrota facility and 11 employees at DFA's headquarters in Kansas City, Mo., also were notified that their positions would be eliminated. A comprehensive effort is underway to ease the burden on workers and their families.

"Although it is difficult to make decisions that result in the elimination of jobs, we have an obligation to our members to make decisions that benefit them," DFA Chairman Tom Camerlo, a dairy farmer in Florence, Colo., said in a press release announcing the closure. "Market conditions and operating results have hindered success at our Corona plant and in our American Cheese division. We constantly look for ways to end losses, and stimulate profitability."

David Parrish, chief operating officer of DFA's Western Area Council, which supplies milk to the Corona facility, noted that the members support the changes. "Although dairy farmers never want to see the plant they ship milk to close its doors, our member-owners understand that we need to operate profitably," he said. "With many DFA customers providing multiple outlets for milk, our members will continue to have a market for their milk. This is the very nature of cooperative membership."

"Schreiber will continue to produce top quality products for our customers," Carmelo said.

Block cheese and whey production employees in Zumbrota and Monett,

Mo., will not be affected as DFA plans to continue its commodity American cheese operations in these facilities. Additionally, these changes will have no impact on DFA's Borden branded or private label retail cheese business.

### **Oregon electric co-op to pursue ocean wave power**

PNGC Power of Portland, Ore., and Ocean Power Technologies Inc. (OPT) have signed an agreement to float a wave-energy buoy off the coast of Oregon. If this test project is successful, they plan to expand the scope of the project.

PNGC will pay \$500,000 to OPT to build and install the first PowerBuoy® system at the Reedsport (Ore.) OPT Wave Park. OPT will build and deploy a 150 kilowatt, non-grid-connected PB150 PowerBuoy.

This effort is the first phase of OPT's plan to install about 14 of the buoys that would generate two megawatts of power about 2.5 miles off the coast near Reedsport. OPT has been issued a preliminary permit by the Federal Energy Regulatory Commission (FERC) for up to 50 megawatts of capacity at the site, the largest such facility in the nation.

Major portions of the system will be fabricated in Oregon and integrated near Reedsport.

PNGC Power is a Portland, Ore.-based electric power cooperative serving 15 distribution cooperatives with service territory in seven western states. In

addition to this agreement for the first PowerBuoy, PNGC will be supporting OPT in the permitting process and with on-shore power transmission for the project. PNGC Power also intends to work cooperatively with OPT and to provide its expertise regarding grid interconnection and its experience in meeting the standards of the Bonneville Power Administration, which operates much of the region's power system.

"Working with OPT on the project is consistent with our desire to investigate promising new generating



*PNGC will be using huge buoys such as this to harness the power of ocean waves off the coast of Oregon. Photo courtesy PNGC*

technologies," says PNGC President and CEO John Prescott. "The Reedsport OPT Wave Park represents innovative renewable generation technology which holds the promise of helping us meet our future energy needs."

An agreement previously signed by OPT and PNGC provides a framework under which PNGC and OPT may continue to work together in connection with a 50MW wave power park. PNGC will have the option to participate in ownership or power purchase in future commercial phases of the project. PNGC Power also plans to

work with other utilities to increase participation in this first-of-a-kind project in Oregon.

### **New book examines utility co-op's struggles**

*Co-op Survivor* is the title of new book tells the story of Harrison Rural Electrification Association (HREA) in West Virginia. It covers the co-op's eight-year struggle, from very dark days until today, when the co-op is an important and trusted community partner.

HREA, the only electric cooperative headquartered in West Virginia, is a small cooperative with about 6,000 members. It has been plagued by perceived high rates and a poor public image.

*Co-op Survivor* illustrates how sound crisis communications techniques and the value of teamwork within a cooperative family can help turn even the most troubled cooperative around. For more information, visit: [www.dopeydogs.com](http://www.dopeydogs.com).

### **Cooperative Foundation grants supporting co-op education**

The Cooperative Foundation has approved cooperative education-based grants to four organizations: Consumer Cooperative Management Association (CCMA), Minnesota Association of Cooperatives (MAC) Education Foundation, the National Cooperative Business Association (NCBA) and NCERA-194 Research on Cooperatives.

CCMA received a \$5,200 grant to support its 2007 annual conference. Designed by the University of Wisconsin, the conference provides training for directors, managers and staff of retail food co-ops with a focus on co-op and community sustainability.

The MAC Education Foundation received a \$2,500 grant to sponsor the seventh annual Senior Cooperative Housing Conference, which provides educational resources for senior cooperative housing members, board members, managers and developers/professionals.

NCBA is getting a \$5,000 grant for a federal research project on cooperatives. It will collect and analyze economic data on cross-sector cooperative activity and identify a strategy to develop research of topics leading to a deeper understanding of the impact of cooperatives.

The NCERA-194 received a \$1,000 grant to support six students and/or faculty members at Kansas State University to attend both the NCERA-194 Research on Cooperatives Annual Meeting and the Farmer Cooperatives Conference in November 2007.

### **CHS acquires DDG business; sells Brazilian soybean shares**

CHS Inc. is purchasing a distillers dried grain (DDG) business from Commodity Specialists Co. (CSC). Steve Markham and Sean Broderick, current managers of this operation for CSC, will continue to direct the activity of the unit as employees of CHS.

The DDG business provides "exceptional sourcing for current CSC customers and provides an excellent supply complement to CHS grain and by-product customers, both domestically and internationally," says Rick Browne, senior vice president, CHS Grain Marketing. "Putting together CSC's marketing and industry expertise with our global access and established distribution capabilities will enhance the already high level of service and market execution to both ethanol plant suppliers and DDG customers."

In another move, CHS is selling a portion of its share in Multigrain AG to Mitsui & Co. LTD. Multigrain AG is a holding company of Brazil-based agricultural commodity business Multigrain SA. Multigrain is primarily involved in soybean origination and marketing through multiple locations in the rapidly expanding agricultural regions of northeast Brazil. The company is also involved in other commodity trading, including wheat and sugar.

Under the agreement, Mitsui will own 25 percent of Multigrain AG,

acquiring shares also from the other majority shareholder, PMG Trading.

## NMPF partners with USDA on animal identification system

The U.S. Department of Agriculture announced a partnership with the National Milk Producers Federation (NMPF) to register dairy farm, dairy calf and heifer-grower premises as part of the National Animal Identification System (NAIS).

"This landmark agreement is another tremendous step forward as we move ahead with NAIS," said Bruce Knight, undersecretary for USDA's marketing and regulatory programs. "It builds on agreements previously announced with the National Pork Board, the FFA and the U.S. Animal Identification Organization to promote animal health by providing producers with the information they need to take the important step of registering their premises and protecting their animals."

NMPF is spearheading the effort of IDairy, a consortium of dairy cattle associations formed in 2005 to promote NAIS in the dairy industry. Since IDairy was established, more than 30,000 dairy producers have registered their premises under the NAIS, but as many as 35,000 commercial dairy farms and dairy calf and heifer-grower operations are yet to be registered. IDairy's goal is to have 100 percent of the operations registered to help animal health officials quickly respond to an animal health emergency.

Under the agreement, NMPF, with the cooperation of the rest of the IDairy consortium, will conduct an outreach campaign, including direct mail, advertising, Internet activities, dairy and trade show presentations and individual contacts with producers, including on-site visits.

NAIS consists of three components: premises registration, animal identification and tracing.

Earlier this year, USDA announced the availability of \$6 million for cooperative agreements, subject to availability, to support nonprofit

agricultural organizations to promote NAIS and to increase participation in premises registration.

## Organic Valley distribution center to boost economy of southwest Wisc.

After more than a year of planning and construction, Organic Valley employees, state and local officials, business leaders and community members gathered in Cashton, Wisc., July 27 to celebrate the grand-opening of a new, \$17.5 million Organic Valley Distribution Center. The new facility will serve as the primary warehouse and distribution center for Organic Valley, America's largest cooperative of organic farmers and one of the nation's leading organic brands.

The new facility provides ample evidence that organic products have moved from a niche market into mainstream consumption, co-op officials say.

The 80,000-square-foot distribution



*This artist's conception shows how Organic Valley's new distribution center should look upon completion. Groundbreaking for the \$17.5 million complex was held in late July. Photo courtesy Organic Valley*

center is located on 40 acres in the Cashton Greens Business Park, an innovative new development where businesses will create and use renewable energy, such as biomass conversion of manure and sawdust, biodiesel and wind energy. It includes an automated storage and retrieval system.

"The new Organic Valley Distribution Center is a symbol of our

co-op's growth and its ongoing commitment to creating sustainable communities through organic farming," said co-op CEO George Siemon. "Anchoring our distribution in Cashton is a step to fulfill our mission to help bring economic vitality to rural Wisconsin."

The facility was built using a number of "green" building practices, including fly ash in the cement, recycled cotton for insulation in the walls and recycled steel throughout the building; a white roof to reflect the sun's heat and decrease energy costs in refrigeration; waterless urinals; and automatic faucets that recharge their batteries with the flow of water.

Organic Valley sales hit \$334 million in 2006.

## Green Plains Renewable Energy, Great Lakes Co-op to merge

Green Plains Renewable Energy Inc. has entered into a merger agreement with Great Lakes Cooperative, Everly, Iowa. Under the agreement, Great Lakes' members will receive cash and Green Plains' common stock valued at about \$20 million. Grain from Great Lakes' elevators will be used for Green Plains' ethanol production as well as marketed locally and throughout the United States.

The transaction must be approved by Great Lakes'

members, and Green Plains will be required to file a registration statement with the Securities and Exchange Commission ("SEC") in connection with the proposed merger.

Created in 2001 from the merger of two longstanding northwest Iowa cooperatives, Great Lakes is a member-owned cooperative that operates one of the largest networks of grain elevators

in Iowa. It operates a federally-licensed public grain warehouse, provides grain marketing services and supplies feed, fertilizer, chemicals, petroleum in northwestern Iowa and southwestern Minnesota.

It has about 100 employees and 14.5 million bushels of grain storage capacity at its seven sites in northwestern Iowa, including four locations with mainline rail facilities.

Green Plains' second ethanol plant is currently under construction less than one mile away from — and on the same rail line as — Great Lakes' Superior grain facility.

Great Lakes' investment in other regional cooperatives, worth about \$11.3 million, would be placed in an escrow account for its members and excluded from the merger.

### **East Iowa Central to merge with Members Mutual Oil**

Members Mutual Oil Co. has approved a merger with East Central Iowa Cooperative. About 86 percent of Mutual Oil members voted in favor of the merger. Members Mutual Oil will now become part of the Energy Division of East Central Iowa Cooperative.

The merger provides farmers and consumers with additional marketing opportunities, reduced costs and increased efficiencies, the co-op said in a press release. Other efficiencies created by the merger could include lower employee insurance costs and fewer equipment needs. Both co-ops had been supplying the same basic territory with propane and diesel.

The Energy Division will have its office in Waterloo and the general administration office is in Hudson, Iowa. Kurt Raymond will be the operations/administration manager, and Terry Grant will be the sales/marketing manager. Both will report to East Central Iowa Cooperative General Manager Dennis Maas.

### **Minnesota Soybean Processors in agreement with Bunge**

Minnesota Soybean Processors has entered into a service agreement with

Bunge North America for its soybean processing facility in Brewster, Minn. Under the agreement, Bunge will provide commercial and administrative support to the processing operations.

"While we have strong relationships with our local farmers, we will look to Bunge to expand our markets, since the company has extensive experience marketing meal and oil both domestically and for export," says Bruce Hill, president of Minnesota Soybean Processors. "We will also be able to tap into Bunge's operational expertise as needed."

"This service agreement with Minnesota Soybean Processors gives Bunge access to additional meal and oil supplies in an area of the country where we don't currently have a presence," said Greg Bechtel, general manager, Bunge Oilseed Processing. "We look forward to working with the co-op in serving its members, current customers and in reaching new markets."

The facility has approximately 70 employees who will retain their positions.

Minnesota Soybean Processors was founded as a farmer-owned cooperative in 1999 with the goal of building and operating its own soybean processing plant. The co-op has grown to nearly 2,400 farmer members from Minnesota, South Dakota and Iowa. In December 2003, Minnesota Soybean Processors opened a crushing plant in Brewster, Minn., that has expanded to include a vegetable oil refinery and a biodiesel plant.

### **Tillamook selects new CEO**

The Tillamook County Creamery Association (TCCA) board of directors has selected Harold Strunk as its chief executive officer. Strunk has more than 25 years of consumer packaged-goods experience. He joins the dairy cooperative from Eagle Family Foods Inc., where he simultaneously served as executive vice president of sales and international vice president and general manager of the Canadian division since 2001.

As executive vice president of sales,

he was responsible for all U.S. retail, special channel and foodservice sales activities. His duties as vice president of international included sales, marketing and supply chain for all international businesses.

Before working at Eagle Family Foods, Strunk was with Borden Inc. He started at Borden in 1986 as retail development manager of Borden Grocery, and served in positions of



*Tillamook CEO Harold Strunk*

increasing responsibility until 1996, when he became director of process improvement for Borden Food Corp. He held that position for two years until Borden was purchased by Eagle Family Foods, and he was appointed director of sales support.

"I am very impressed with what has been accomplished over the past few years and look forward to working with the Tillamook team to continue to build this great enterprise," said Strunk. He will be the seventh CEO of the 98-year-old cooperative.

### **Co-op strategies to be focus at Farmer Co-op Conference**

The 10th Annual Farmer Cooperatives Conference, organized by the University of Wisconsin Center for Cooperatives, will be held November 5-6, 2007, in St. Paul, Minn.

The conference will focus on "Valuing the Cooperative Business in the 21st Century," and will include sessions

*continued on page 40*

## Newsline

*continued from page 39*

that explore the value maximization of cooperative assets and business structure strategies for the future. It will look at the business structure changes at FCStone Group, South Dakota Soybean

Processors, Gold Kist and others. Other topics will include benchmarks and performance optimization and understanding the value of the cooperative during times of change.

Conference, program and registration information is posted on the University of Wisconsin Center for

Cooperatives website at

[www.uwcc.wisc.edu/farmercoops07](http://www.uwcc.wisc.edu/farmercoops07).

For questions about the conference, contact: Anne Reynolds, University of Wisconsin Center for Cooperatives, (608) 263-4775, [atreynol@wisc.edu](mailto:atreynol@wisc.edu).

## Co-ops Set Net Income Record

*continued from page 9*

181,000 workers. The number of full-time employees fell 2 percent, to 123,000, while part-time and seasonal employees grew to 57,000.

Farm numbers continue to decline and grow in size, as do farmer cooperatives. Cooperative memberships were 2.6 million in 2006, slightly lower than in 2005. Many farmers are members of more than one cooperative, hence cooperative memberships exceeds U.S. farm numbers. There are now 2,675 farmer cooperatives, down from 2,896 in 2005, due primarily to mergers and consolidations. ■

## New Hybrid on Great Plains

*continued from page 27*

their product.

This strategy seems to be working. Not only is the membership growing, the co-op is attracting some pretty hefty new members, such as the University of Nebraska at Lincoln, where the whole idea for the hybrid co-op took root.

"The university can have 1,000 seatings at one meal," says NCDC's Elaine Cranford, who has been involved with the co-op since the first meeting in 2004. "That's a lot of food. Now it's at a point where we need to develop strategies for serving the wholesale markets." Her use of "we" is

appropriate, because Cranford is rapidly becoming one of the most knowledgeable people in the region regarding sustainable, local food systems and linking producers to consumers.

Broekemeier says people who aren't even co-op members have volunteered to help it succeed. "Their incentive is to help create a new system that increases accessibility to local foods and provides farmers with an outlet for marketing. It's a community-based effort instead of looking at big corporate conglomerates as the guys we want to have taking care of our food needs. We'd rather do it ourselves." ■



## Economic Impact.

From Main Street storefronts to Fortune 500 companies, cooperative business creates jobs and economic growth.

We generate over \$273 billion in revenues annually.

We employ more than half a million Americans.

Our payrolls top \$15.5 billion a year.

And because cooperatives are owned by their customers, what's spent there stays there, benefiting our communities again and again.

## Cooperatives.

Owned by Our Members,  
Committed to Our Communities.

Figures published Dec. 2006



## South Dakota: Value-added Opportunities

*continued from page 22*

Dakota Farms markets a wide variety of bulk, non-processed products, including soybeans, barley, corn, buckwheat, rye and many varieties of wheat. Non-GMO, transitional, certified-organic products — as well as traditionally grown products — are available.

Packaging can be tailored to customer specifications. Value-added products include several types of wheat flour, soy flour and meal and a soy trail mix.

"The challenge is to gain more of the end price by moving further up the supply chain," explains Tim Walter, president of Dakota Farms. "The higher the risk, the higher the return. We wanted to get out of the commodity business, where even premiums for certain grains eventually trail off as production increases and markets adapt."

In 2004, Dakota Farms received VAPG funds for marketing barley tea. "The grant helped a great deal," Walter says. "Costs involved with a start-up of a new product line are high. Developing products and marketing internationally is tough, and we could not have stayed afloat without assistance from USDA Rural Development."

A roaster was purchased from Turkey, shipped and set up at Dakota Farms. The process of making the tea was not easy, and there were several setbacks. Specialists from Turkey had to be flown to South Dakota to perfect the process. Initially, the tea was going to be made from conventionally grown barley, but strong competition from China made this economically impossible. Dakota Farms then looked at using organically grown barley for a high-value boutique tea.

Walter then cultivated a relationship with a Japanese distributor. Dakota Farms produced a tea in bags and packaged the product under the Japanese firm's name. Organic barley was purchased from several farmers in South Dakota, as well as Iowa and North Dakota.

Dakota Farms recently developed its own brand of organic, boutique tea packed in tins for the domestic market. The brand name, "Bushido," is Japanese for "Way of the Samurai Warrior." Dakota Farms unveiled Bushido last June at the World Tea Expo in Atlanta, Ga., where the response was "overwhelming," Walter says.

Markets are always changing, and the Japanese tea market has begun to move away from individual bags to ready-to-drink teas. Dakota Farms is moving with the market, developing a ready-to-drink product line of Bushido barley tea which should be test-marketed this fall.

### South Dakota Soybean Processors

South Dakota Soybean Processors (SDSP) is a value-added LLC, owned and operated by its 2,100 farmers in South Dakota and Minnesota. The crushing plant in Volga, S.D., employs 60 people and crushes an average of 80,000 bushels per day, or 28 million bushels annually. SDSP's goal is to be a

financially solid business that maximizes the economic return to its members through development of quality products and competitive marketing.

"We are a stand-alone, independent cooperative business, owned and controlled by our farmer-members," explains Tom Kersting, commercial manager for SDSP. The challenge SDSP faced was to create better returns for members by further processing soy oils. To develop innovative products and stay competitive, SDSP had to vertically integrate.

SDSP received VAPG funds to conduct a feasibility analysis and to establish a working capital account for new value-added products. SDSP set up an independent company, Urethane Soy Systems Co. (USSC), in which it holds a majority ownership. Due to price increases for petroleum-based inputs, soy oil is now very competitive.

USSC looked for various applications, including spray-foam seat components, insulation for buildings and spray-on bed liners for pickup trucks. "We are one of the few companies in the United States that provides soy-based products to the polyurethane industry," says Eric Geiger, director of research and development for USSC.

USSC cooperated in a research consortium with the Lear Corporation (one of the world's largest suppliers of automotive-interior systems and components), Ford, Henosol, Bayer and the United Soy Board to develop and use soy-based polyurethanes. Soy-based foam has been used in seat cushions for the Ford 500 and Chevrolet Impala models, and will be used in the 2008 Ford Mustang.

Since 2005, USSC has been providing materials for spray insulation used in homes and industrial buildings. This market is strong and growing. The spray-on truck bed liner, trademark named "Bio Tuff," is the first soy-based, spray-on bed liner.

"SDSP is appreciative of the support provided by USDA Rural Development," says Kersting. "The VAPG program has had an impact here at SDSP. It is a good investment in South Dakota and our community."

### Program delivery and customer service

"Our programs have a lot to offer cooperative and rural businesses, especially small and limited-resource producers," explains Gary Korzan, cooperative development specialist for South Dakota.

In many cases, outreach to potential rural businesses and communities is the starting point in a working relationship with Rural Development. For several years, Korzan made presentations to students in Co-op 101 classes at South Dakota State University. He participates in the annual Value-Added Conference meeting in Brookings, S.D., to create awareness and promote the availability of the VAPG program. Participating at the South Dakota State Fair is another annual opportunity for outreach and education.

For more information on USDA Rural Development programs, visit: [www.rurdev.usda.gov](http://www.rurdev.usda.gov). ■



## *From the archives of Rural Cooperatives and its predecessor magazines*

### 50 Years Ago...

From the September & October 1957 issues of *News for Farmer Cooperatives*

#### **What's in a name? (cover article)**

What's in a name? A number of cooperatives answer: "Plenty." They know from experience the value of adopting as their corporate names the brand names thoroughly familiar to the trade and consumers. Even before the formal change occurred, the brand names of these co-ops were well known.



Adopting their brand names has helped keep their brands before the public and has supplemented brand advertising and product merchandising.

Sunkist Growers probably had more years of experience under its previous names than most. Incorporated in 1895 under the name Southern California Fruit Exchange, in 1905 it changed to California Fruit Growers Exchange. In 1952 it changed again

to Sunkist Growers.

"We feel that from the trade and public relations point of view, there is much to be gained in incorporating the brand name in the corporate name," said general manager F. R. Wilcox. "When the brand is included in the corporate name, all printed matter adds to the total publicity for the firm."

No special problems were involved in the Sunkist changeover. Of course, it had to revise stationery and other printed material. It made no change to packaging as a result of the change in corporate name, although changes in printing the packages had to be made.

Gold Spot Dairy Inc. of Enid, Okla., has had several years of experience since adopting its brand name as its corporate name. Organized in 1930 as Enid Cooperative Creamery Association, the change to Gold Spot Dairy was made in 1954.

"Much of our mail and checks came in made out to Gold Spot Dairy," Manager Ralph T. Goley said. "Since the public was better acquainted with Gold Spot than Enid Cooperative, we feel that there is considerable advantage in having the name Gold Spot before the public as much as possible. The

only disadvantage was the necessity of changing our letterheads, statements, signs and so forth. And we used up most of our old material before making these changes." This co-op made no special changes in packaging, production, or distribution. Since the trade and public were well acquainted with the Gold Spot name, there was no special reaction to the change.

Cooperatives cautious about whether to join the group with new names may hear in this combined voice of experience an encouraging: "Come on in, the water's fine."

#### **Credit union serves rural families and groups**

Noble County Credit Union, Albion, Ind., is demonstrating how a rural credit union can render service to rural groups, as well as to rural families. The credit union has over 2,800 members and its share savings and annual loan volume each exceed \$1 million. Both are increasing rapidly.

Official members of this credit union include 78 rural organizations, such as 4-H Clubs, dairy herd improvement associations, township Farm Bureau groups, PTAs and others.

These groups have regular share accounts and borrow from the credit union when necessary. Several rural churches have used credit union loans for erecting new buildings or for making repairs.

The credit union's service program keeps it abreast of growing community needs. Two illustrations pretty well represent how it renders quality service to its members and the community, which is both timely and adequate. When building its new office, the credit union provided for a basement conference room and immediately made it available for community group meetings, free of charge. It is in use almost daily.

When it hired a fieldman, the credit union selected one of its outstanding young farmer-members — its "Corn King" for two successive years — to represent and serve the credit union. It equipped him with a new station wagon and equipped it with two-way radio "in order to better serve Albion County farm families." The new fieldman helps farm families with farm planning and money management problems in addition to his work of expediting regular saving and lending operations.



# 30 Years Ago...

From the September & October 1977 issues of *Farmer Cooperatives*

## Co-op in Denmark invests \$100,000 in U.S. co-op

Officials of a new associate member cooperative of Farmland Industries, Kansas City, Mo., thought \$25 was too little for membership. So, the new associate member, Dansk Landbrugs Grovvareselskab (DLG), of Copenhagen, Denmark, sent along another check for \$100,000 to be invested in Farmland equities.

Farmland officials decided to put the money in loan capital notes. DLG looks to Farmland as a possible source for the 250 tons of soybean meal it needs every year.

The Danish cooperative also markets grain, feedstuffs, fertilizer and agricultural chemicals to its 15,732 members and 150 branches.

Associate members may buy common stock in Farmland Industries and may receive all privileges and rights of common stockholders except that of voting. Another associate member of Farmland is Zen-Noh, a national Japanese cooperative with headquarters in Tokyo.

## After the harvest, gleaning by cooperation aids needy

Metro area gleaning cooperation is "putting it all together" in a four-county area of Oregon. The elements are senior

citizens, the handicapped, low-income families, farmers with leftover crops, community service and government agencies, and the old-time "helping hands" principal.

Under the program, local farmers are asked to donate what they have left after commercial harvest is completed. The crops are picked by people with marginal income and shared with handicapped and elderly citizens.

The gleaned items involve surplus from gardens, weather-damaged crops, late-ripening items on plants, misshapen products and items that are of non-marketable quality, size or condition.

The gleaning program began when Monika Belcher of the Washington County Community Action Organization of Hillsboro, Ore., took the idea from agency to agency to try to stir interest. In 1973, a committee was formed, and the

program grew rapidly and guidelines were established. Some 125 households benefited from the gleaning program's first year.

By 1976, the program served 3,290 people in 1,129 households. In-store value of donated produce was estimated at about \$102,000.

# 10 Years Ago...

From the September/October 1997 issue of *Rural Cooperatives*

## Record gross revenues, but not net profits, for Top 100 co-ops

The nation's 100 largest agricultural cooperatives reported record revenue for the second year in a row in 1996. Operating revenue totaled more than \$74 billion, up nearly \$11 billion from the 1995 record. However, net margins for the year were down.

Strategic alliances, higher grain prices and increases in value-added processing by cooperatives were major contributors to the rise in revenue. However, 52 percent of that increase was realized by just two cooperatives: Farmland Industries and Harvest States Cooperatives. They represented nearly a quarter of total operating revenue for the Top 100 co-ops, up from 20 percent in 1995.

Crop, dairy and livestock marketing sales continue to show tremendous gains, increasing more than 18 percent, to \$55 billion, from the \$46 billion recorded in 1995. This increase doubles the gain made the previous year.

While three-quarters of the cooperatives that market their members' products had higher sales in 1996 than in 1995, 75 percent of the gain was generated by just 10 cooperatives.

Grain sales accounted for about 65 percent of the total increase, followed by milk sales, which accounted for about 20 percent of the increase.

Farm supply cooperatives enjoyed substantial sales gains in 1996, following a year of relatively small gains in 1995. Farm supply sales rose 15 percent, to nearly \$19 billion. However, 70 percent of that gain was due to five co-ops.

Sales increased for nearly every supply category, with 85 percent of the increase attributed to higher feed, fertilizer and petroleum sales. ■



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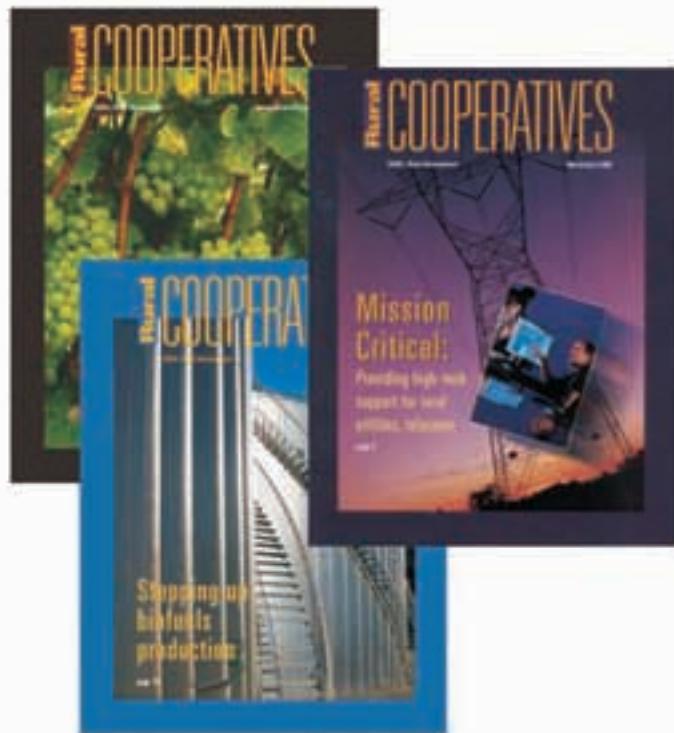
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