Journal of Cooperatives

Book Reviews

Jacobson, Robert E., and Con O'Leary. *Dairy Co-op Issues in Ireland*. Cork, Ireland: Centre for Cooperative Studies, University College Cork, 1990, 144 pp.

Cooperative leaders and educators in the United States and Canada only need to look at what has happened to the Irish cooperative dairy industry in the last six years to obtain a portrait of what could be the leaders' and educators' own worst nightmare. Leaders will be sobered by what happened to Irish cooperatives when their leaders and members supported operational practices completely contrary to core cooperative principles. Educators will sense the great feelings of failure Irish cooperative educators must now be experiencing when their students, the cooperatives' leaders and members, demonstrate an almost total lack of understanding of basic cooperative principles. Many will be critical, agreeing with the saying, "If the student hasn't learned the teacher hasn't taught."

Jacobson and O'Leary describe the history of these last few years and address the key issues now facing the remaining Irish dairy cooperatives and farmer-members as the cooperatives struggle for survival. They join the struggle, almost frantically at times, to combat the view of one observer who concluded, "It's too little, too late." Although the focus is on the Irish dairy situation the issues and their analysis have broad application to all types of agricultural cooperatives in developed countries.

The central issue is the dramatic change in dairy industry structure during the period 1985-90 due to the conversion of several traditional cooperatives into investor-oriented businesses referred to as public limited companies or PLCs. Traditional cooperatives' share of milk assembled from the farm dropped from 95 to 50 percent. The authors attribute this change to two factors: (1) the need for additional capital to finance growth objectives and (2) poorly constructed equity management programs. The combination of these two factors encouraged member-stockholders to convert their cooperatives and member equity to PLC organizations and equity.

A glossary defines nine standard terms and relates them to similar terms used in Ireland. Although prepared with an Irish audience in mind, the glossary is very helpful to non-Irish readers. Most of the terms and their definitions are very similar to U.S. usage. Defining even more terms, such as "public limited company," would have been beneficial to U.S. readers.

I see two major shortcomings in the terms as described in the glossary and used throughout the book. First, the use of the term "allocation" is confusing to all but experts and should be changed. I say this even though the authors' use is very common throughout the U.S. cooperative community. Allocation, as in profit allocation and patronage refund allocation, often is confused with allocation, as in allocated equity, by those not intimately familiar with cooperative finance. I strongly recommend that the term "distribution" be used in the first instance. Then profits are distributed as retained earnings, dividends (on equity), cash patronage refunds, retained patronage refunds, and, in Irish dairy cooperatives, "bonus shares." The distribution of profits to retained earnings creates unallocated equity and to retained patronage refunds and bonus shares creates allocated equity. Substitute allocation for distribution in the previous sentence and you see my point.

Second, the term "bonus shares" is presented as the common term for retained patronage refunds. "The amount of. . . bonus shares that a patron receives is called a patronage refund allocation." In fact, we learn much later in Chapter V that its most common meaning in Ireland is the distribution of profits to stockholders, not patrons, as retained allocated equity on the basis of stock investment, not patronage. Since the authors clearly disapprove of this practice, why didn't they simply recommend distributing profits as retained patronage refunds instead of bonus shares? Redefining bonus shares to mean patronage refunds only seems to add to the problem. More on this issue later.

A new and amusing term to me was "dry stockholder," meaning inactive stockholder. I like the term, especially for use with dairy cooperatives.

The nine chapters follow the conventional format of a scientific report. Chapter I includes introductory information and a statement of the problem, objectives, and procedures. The general problem the authors address is how to obtain sufficient equity capital and how to manage equity in a traditional cooperative in a way that allows it to continue in its traditional form. It is taken for granted that producers are better off doing business with traditional cooperatives than with other forms of business. The most prominently mentioned equity management problem is how to value member equity. However, most aspects of equity management in traditional cooperatives are reviewed, including investment and redemption alternatives.

The objectives are to: (1) determine in what ways, if any, traditional cooperative principles and practices must be changed in order for cooperatives to survive and grow, (2) determine to what extent and why PLC activity may cease or continue, and (3) identify and evaluate equity management alternatives for dealing with the problem.

The procedure used to obtain information of interest was a survey of 15 organizations falling into three basic groups. The first group contained eight traditional dairy cooperatives. The second group included four PLC-oriented organizations that still refer to themselves as cooperatives. They were created from traditional dairy cooperatives and, in the case of three of the four, are still producer controlled. The third group consisted of three cooperatives that sold out to pure PLC organizations.

Chapter II provides basic information on the 15 organizations surveyed concerning size, business lines (milk processing, farm supplies, and other), and financial structure including assets, equity, and equity structure. Equity structure is divided between allocated equity, called share capital, and unallocated equity, called shareholder reserves.

Four important observations are made that form the empirical basis for the authors' conclusions and recommendations. First, there is a major dry stockholder problem. About 47 percent of stockholders of record in 1989 were inactive, and about a fourth of these (13 percent of the total) were dead or not traceable. Unfortunately, no precise definition of inactive is given, but it probably means a patron who has not patronized the cooperative (i.e., sold milk to the cooperative) for at least one year. Also, the percentage of equity in this category is not given.

Second, there is a major problem with producer-customers not being stockholders. About 21 percent of the active producers selling milk to the cooperative ("suppliers") were not stockholders. No corresponding percentage of volume in this category is given. In general, only stockholders were allowed to vote, and presumably, only stockholders received patronage refunds.

Third, most profits are distributed as retained earnings, and therefore, most equity is in unallocated form. Over 90 percent of profits was distributed in unallocated form. Only 7.1 percent of equity was in allocated form on average for all 15 organizations based on 1988 or the most recent data for cooperatives that sold out to PLCs. The authors note this is completely opposite of how U.S. dairy cooperatives distribute profits. In the United States in 1988 only 12.1 percent of profits was distributed in unallocated form, and 92.4 percent of member equity was in allocated form.

Fourth, the balance sheets are relatively strong. The average ratio of equity to assets was 56 percent. Related to the first and third observations is the fact that these cooperatives did not have formal equity redemption programs. Stock was generally considered to be "worthless paper" by stockholders.

Chapter III gives the authors' interpretation of principles, discusses their recommendations on how to establish a market for cooperative equity in a cooperative context, and describes their view of how cooperative profits should be distributed. Also included is their prescription for equity investment and redemption. The first section, on cooperative principles, presents their analytical or theoretical framework, which they refer to as "a cooperative model as ultimately defined on the basis of co-operative principles." This section is central to addressing the three purposes of their study specified in Chapter I. The principles cited are the six approved by the International Cooperative Alliance. Three are selected as especially relevant in their analysis: member control, operation at cost, and member ownership.

The operation at cost principle is interpreted to mean profits should be distributed to member-patrons as patronage refunds. Tax impacts are said to be irrelevant since Ireland's income tax laws don't require a tax on retained profits of cooperatives, whether distributed as retained earnings (unallocated) or retained patronage refunds (allocated). As a consequence, there is not the equivalent of qualified and nonqualified distributions and not a minimum cash patronage refund required to be qualified as is the case in the United States. No information is presented about the taxation of cash patronage refunds or dividends on equity, perhaps because cash patronage refunds and dividends are not singled out as a recommended practice. Since dividends on equity are commonly paid by Irish dairy cooperatives, an interesting but unanswered question is whether cash payments to member-owner-patrons should be in the form of dividends or cash patronage refunds.

The member ownership principle is interpreted to mean most of the member equity should be in allocated form. They note this would be accomplished through the operation at cost principle if most profits are distributed as patronage refunds. They recommend that each owner-patron's equity investment be proportional to patronage.

The authors clearly reveal their values by promoting these three principles as the guidelines both traditional and PLC-oriented dairy cooperatives should follow as much as possible. These principles are used more as premises than testable hypotheses. But they do discuss how the problems dairy cooperatives have faced could have been avoided or minimized had these principles been practiced. In the final chapter they state, when referring to their first objective or purpose, "The study does not provide a complete basis for providing an absolute answer to this . . . objective. However, the evidence is strong that it is not co-operative principles that have been deficient but rather the failure to adhere to co-operative principles that has undermined the member investment structure in the co-operatives."

The second and third sections of Chapter III discuss how to create a market for cooperative equity and how to distribute profits. The PLC activity was strongly supported by many producers because the sale of assets or conversion of equity gave current stockholders value to both their allocated and their pro rata share of unallocated member equity. Therefore, the central focus of this discussion is how to provide a market and value in a traditional cooperative context. The cooperative and the PLC solutions are evaluated. The authors maintain the key is to practice cooperative principles through traditional cooperative type equity investment and redemption programs. They claim a market for members to buy or invest equity is provided through distribution of profits as patronage refunds. Similarly, a market for members to sell equity is provided through redemption of retained patronage refunds, normally at par value. Since these private exchanges between cooperative and patron are a major improvement over current practice, more open and complex exchanges are not proposed. In PLC-oriented cooperatives, in which one class of equity already has a market value through public trading, they suggest redeeming nontradable classes of equity of inactive patrons at market values and requiring underinvested active patrons to make investments sufficient to replace this equity.

This chapter describes most of their recommendations for profit distribution and equity investment and redemption. A major weakness of this presentation is the absence of a concise yet complete presentation of cooperative finance fundamentals with special emphasis on equity management. Both amateurs and experts will be frustrated by this chapter and the chapters that follow because of this deficiency. Much of the content is rambling, fragmented, redundant, and incomplete. The authors could have avoided this if they had taken as much care in presenting the cooperative finance framework as they did the principles framework.

The major profit distribution recommendation is to distribute profits in allocated form as retained patronage refunds sufficient to keep allocated equity equal to or greater than 75 percent of total equity. They admit this is an "arbitrary standard." The possibility of cash patronage refunds is mentioned but not encouraged or discouraged. Other distribution alternatives of dividends on equity and retained earnings are mentioned in other sections of the book.

One extremely important point about the profit distribution practices of Irish dairy cooperatives was not mentioned until Chapter V and was only clearly noted one time. However, the authors apparently disapprove of the practice because they make recommendations that would terminate it. Historically, when profits were distributed in allocated form, they were distributed to stockholders as "bonus shares" in proportion to stockholder investment, not to patrons as patronage refunds. This is in complete contradiction with the very essence of a cooperative, the operation at cost principle, a principle the authors strongly support and discuss throughout the book. I'm surprised the authors didn't tackle this practice head on. In any case, it further illustrates the magnitude of the industry problems for which the authors feel compelled to suggest corrective action.

Their major investment recommendation is to obtain equity from retained patronage refunds. The possibility of direct investment is mentioned. Some of the advantages and disadvantages of retained earnings are noted. Not until Chapter VIII is the possibility of per unit capital retains implied, although not by name. This neglect is surprising and puzzling since the use of capital retains is the most common method of obtaining equity investment capital in U.S. dairy cooperatives.

The equity redemption recommendations are intended to keep equity in the hands of active patrons. This objective is frequently mentioned throughout the book. The authors recommend each patron's investment should be proportional to patronage, an even more exact and demanding objective. Unfortunately they fail to recommend the redemption method that is generally the most effective in accomplishing this objective, base capital. Neither do they discuss the relative performance of each alternative method in terms of the objective, proportionality of investment. Since they state "it is [equity redemption] in which the co-operatives in Ireland have been seriously derelict" the authors could significantly improve the effectiveness of their presentation and recommendations by using state of the art information and terminology.

They recommend using special redemptions for estate settlements, move-outs, hardships, and transfers to other cooperatives. They also recommend making redemptions to owner-patrons who retire (a variation of the age of patron method) and to "aged shares" of active patrons (the revolving fund method). Estate settlements and age of patron redemptions are the least effective ways to maximize both proportionality and cash flow to patrons. The most effective, in decreasing order of proportionality performance, are the three systematic methods: base capital, revolving fund, and percentage pool (percentage-of-all-equities). The most important factor in equity management performance—profitability—was not stressed but should have been. The higher the profitability the higher the proportionality of investment when using retained patronage refunds and the less difference there is between the three systematic methods.

Chapters IV through VIII present many of the results of the survey and deal primarily with their implications. Special attention is given to how to meet the challenge of providing additional capital for dairy firm growth and providing a value and market for member equity without resorting to the PLC alternative. Chapter VIII also discusses how PLC-oriented cooperatives can apply cooperative principles to maintain majority ownership and control in the hands of producers through the cooperative component of the PLC.

Chapter IX provides a brief summary of the problem situation, purposes, procedures, conclusions, and recommendations presented in earlier chapters. Two additional recommendations are made as a "logical extension" of this information. First, that education of members, directors, and managers will be needed to implement their recommendations. Second, that laws should permit cooperatives to operate as recommended. Only one needed change is noted, the removal of the 20,000 pound upper limit on ownership.

This book is frustrating to read because of its flaws in presentation and content, but without a doubt it makes a major contribution to the Irish dairy cooperative industry. These cooperatives have followed some of the least cooperative-like practices of cooperatives anywhere in the world. Their members and leaders clearly don't understand the unique aspects and essence of a cooperative. The consequences suffered by this industry and their causes, while supporting the conventional wisdom of most cooperative experts, serve as a good object lesson in the reality of some nightmares. Cooperative leaders and educators everywhere, take note.

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Fairbairn, Brett; June Bold; Murray Fulton; Lou Hammond Ketilson; and Daniel Ish. *Co-operatives and Community Development: Economics in Social Perspective*. Saskatoon, Saskatchewan: Center for Cooperative Studies, University of Saskatchewan, 1991, 141 pp.

The authors state the central ideas of the book are that cooperative, rather than individual, action is the key to answering many questions facing society, and that globalization and changes driven by the market and government policy tend to adversely affect those without economic or political power. In their view, an ecological model is needed that puts business in the context of the social environment and sets up positive feedback to benefit that environment. As the title indicates the book is specifically directed at the role of cooperatives in present day community development. Problems of community development in Saskatchewan motivated the book and provided its examples.

The writers state communities are suffering from adverse effects of the latest wave of the internationalization of markets. Moreover, "rural communities like those on the Prairies also face an environmental crisis [because] their economic base is heavily dependent on high-production agriculture, which not only is vulnerable to world market fluctuations and brings low returns, but is not environmentally sustainable." Their primary strategy for community development is to develop a more diverse, sustainable agriculture in which farms and rural communities become less agricultural. They emphasize that community power has been replaced by transnational firms and powerful lobbies (globalization), which are countered by consumerism, as individuals act alone in the big market and split away from their communities. They believe that conventional development with its provision of limited encouragement to ordinary entrepreneurs is ill-suited to communities that are "victimized" by the operations of national and global markets. Conventional development is viewed as the disease, not the cure. The solution is "unconventional" development that takes in far more than the economy. This development involves processes of education and empowerment by which local people take responsibility for what used to be done "to" them.

Cooperatives are the institutions best suited to design and implement this unconventional development strategy. Collective action at the local level is the approach that will result in long-term success. The authors have little faith in free markets as a long-run solution to the community development problem. They state "the logic of the self-regulating market and of individualism is such that, even though one generation in one community finds its answer and builds its institutions, the solutions fade away."

The social role of cooperatives in the community and community interest versus self-interest are discussed in considerable depth. Although the authors advocate cooperatives as the most effective community development institutions, they caution against "frozen cooperatives." There are two categories of leaders in "frozen cooperatives." In one category, leaders believe that economic criteria solely should drive decision making; in the other, leaders are idealists who are prepared to compromise economic criteria in order to adhere strictly to cooperative principles. Neither approach results in rapid improvements in sales or profitability. A balance is required to achieve successful growth and development. The authors prefer a holistic management approach that thinks in terms of the needs of the whole community. Cooperatives need to contribute to community development in a variety of ways such as leadership, education, organization, energy, and some equity and financial relationships. Moreover, "new" or "young" cooperatives are much more effective than "old" established cooperatives in community development programs.

An ecological model for cooperative and community organization is discussed with recommendations for cooperatives to position themselves in appropriate niches in the community. Local control of cooperatives is essential for successful development. One chapter deals with capital and income flows and leakages. Another examines Canadian cooperative law and its effect on cooperative performance and development. It is pointed out that intervention by the law and the courts to protect individuals sometimes may prevent collective actions designed to protect individuals. Also social audits and plans for cooperatives (as well as other business organizations) are recommended. Procedures for social audits are outlined.

Bits of history of cooperative development in Europe and in the Prairie provinces of Canada are presented in the book. The majority of examples center on consumer cooperatives and credit unions. Readers will find the vignettes on cooperative history especially interesting. Useful insights, information, and some new ideas are presented.

The book, however, has limitations. The concepts of comparative advantage and opportunity cost were ignored. The impact of new technology on efficient economic organization was not explored. More information on Saskatchewan communities, institutions, economic organization, and problems would have been helpful since the authors' recommendations for community development centered on those communities. The book does not analyze in depth the noncooperative community development approaches—collective and individual—nor adequately explain their alleged shortcomings. Those individuals working in community development and cooperatives will need to analyze additional approaches and situations. Finally, it is interesting to note that while much of the socialist world is shifting to free markets and capitalism, including globalization, as means of developing their economies and communities and improving the well-being of their citizens, the writers have serious reservations about the effectiveness of free markets and individual action in promoting effective long-run community development.

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Rasmussen, Wayne D. *Farmers, Cooperatives, and USDA: A History of Agricultural Cooperative Service*. Washington, D.C.: Agricultural Information Bulletin 621, July 1991, 292 pp.

This book was written to celebrate the 65th anniversary of the Cooperative Marketing Act of 1926 and document USDA's role in helping producers and other rural residents to form and use cooperatives. Rasmussen presents an informative and interesting perspective on the history of farmers and cooperatives, particularly the earlier years of cooperative development in the United States. He also provides insights into the efforts of USDA over the years to provide research, education, and service to cooperatives and their members.

The contents of the book are divided into 10 chapters: Agricultural Cooperatives: What and How; American Cooperation in the Beginning; Early Federal Work with Cooperatives; Farm Depression, Cooperatives, and Capper-Volstead; Cooperative Marketing Act of 1926; Federal Farm Board and Farm Credit Administration, 1929—1953; Independence, Change, and Challenge—1953—1969; Good Times for Farming: The 1970's; Farm Depression and Recovery: The 1980's; and Agricultural Cooperative Service: Today and Tomorrow. Rasmussen manages in those 10 chapters to give a concise flavor of developments in cooperatives and USDA's efforts to be responsive to demands for research, education, and service as expressed through the political system. Much of the early political demand was the result of a social movement with cooperatives seen as a major way to improve farmer well-being.

The history of the Agricultural Cooperative Service (ACS) is closely linked to that of agricultural economics in USDA and to those agricultural economists who were influential not only within the department but also in the development of the profession itself. Early leaders include Henry C. Taylor, Alexander Legge, and Frank Peck, who all had roles in the later founding and initial direction of Farm Foundation.

The thrusts of cooperatives in marketing farm products, purchasing farm inputs, and providing farm credit were developed through the legislative process in response to farmers' interests. Early cooperatives were hampered by meager capital and poor management. Opposition from some private business firms made it necessary to struggle to get state legislation allowing cooperatives as a form of business. Management of cooperative organizations has been a problem over many years and remains so for numerous smaller cooperatives, hence the need for USDA's continuing assistance to cooperatives.

There apparently was more political support for provision of credit under the cooperative format than for other activities. When the Farm Credit Administration was placed under the Department of Agriculture in 1939, it immediately stirred political support for regaining independence. It was separated from the department in the Farm Credit Act of 1953, which also kept the Division of Cooperative Marketing under the control of the secretary of agriculture.

This led to the formation of the Farmer Cooperative Service, forerunner of ACS, in 1953. Joseph G. Knapp, its first administrator, was a strong influence in defining the mission and scope of agricultural cooperatives as we know them today.

The Agricultural Cooperative Service and its predecessors have been subject to continuous change. Administrator stability may be much greater now since the current administrator is a civil service employee as opposed to a political appointee. But budget pressures and personnel limits have varied from severe to slightly favorable.

During the 1950s and 1960s as growth and consolidation took place among cooperatives, the Farmer Cooperative Service played a direct, as well as indirect, role. It was involved in helping bring about the merger of some cooperatives, and it published information advising cooperatives on how to handle problems related to mergers. During the 1960s the Farmer Cooperative Service became involved in rural development efforts. It helped farmers organize various types of cooperatives in different areas, as well as recreation associations in rural areas.

In conjunction with its rural development efforts, the first field office of the Farmer Cooperative Service was established in 1969. The field offices have been located in a few states over the years, serving producers in the vicinity by helping organize cooperatives and providing assistance in developing management and related services. Given these offices' scattered nature and varying focus, perhaps the resources could have been better devoted to preparing educational materials and programs to reach a broader range of producers and cooperatives than the few served directly.

USDA has focused primarily on family farmers who make up the largest portion of cooperatives' membership. It has been argued that a strong cooperative system is important to the survival of family farmers, even though there is recognition that cooperatives need to maintain the patronage of larger farmers to be economically viable.

As farming came upon difficult times during the 1980s, numerous cooperatives failed. The result has been fewer but larger cooperatives just as there are fewer but larger investor-owned agribusiness firms and fewer but larger farmers.

Over the years farmers have generally maintained a relatively low interest in and use of cooperatives. This has been blamed on a lack of understanding of cooperatives' advantages by farmers, despite the ongoing educational efforts of the Agricultural Cooperative Service and its predecessor agencies. A number of land-grant university economists also have devoted their careers to assistance, research, and education related to agricultural cooperatives. Cooperative leaders have stressed the need for education throughout the years. The apparent modest success of education efforts raises a question of why they have not been more effective in creating demand for cooperatives and making them more prominent in the marketing system.

Research publications from the Agricultural Cooperative Service have been helpful to cooperatives and farmers interested in forming cooperatives. Technical reports involving particular cooperatives have not been made public because of confidential business data contained in them. Is it appropriate to conduct such technical analyses at public expense? Are there not qualified consultants available to do such work?

As the early nineties come upon us, the future role of cooperatives is an important issue. The Agricultural Cooperative Service has pointed out its potential to help citizens in rural areas create activities or businesses that contribute to economic development. Is that the future strength for cooperatives in rural areas? What will be the role of cooperatives in the future of the agricultural and food system? Obviously there are a few major cooperatives that have become significant actors in the food system, but do they bear much resemblance in types of businesses, management style, and general philosophy to the more numerous and smaller cooperatives that exist throughout the nation? Given that cooperatives will likely continue to be a relatively modest player in the total agricultural and food system, under what conditions will they play significant roles in certain geographic areas or commodities? Can the cooperative system serve the needs of large commercial farmers and small or part-time farmers simultaneously?

The final chapter provides a heavy dose of optimism about the important role that the Agricultural Cooperative Service can play in making cooperatives a more important player in the economic and general development of rural areas. Since the agency has had a continuing struggle to maintain resources and personnel, it remains to be seen whether the resources will be available for it to carry out the ambitious goals set forth.

This book is an interesting view of the development of cooperatives and the role of USDA in that development. Rasmussen's interpretation certainly reflects favorably upon ACS and its predecessors. No doubt much of the praise is well deserved, but at times the author appears to leap to strong conclusions based on a bit of anecdotal evidence. The book offers very little in the way of supporting statistics and analyses.

Anyone interested in cooperatives, their development, and the role of USDA in serving the needs of cooperatives will find this book informative and interesting. Paraphrasing Rasmussen, this book is a valuable resource about the Agricultural Cooperative Service and its role in assisting farmers and rural residents.

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