What is a Cooperative?

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Groups of individuals throughout time have worked together in pursuit of common goals. The earliest forms of hunting and agriculture required a great deal of cooperation among humans. Although the word "cooperative" can be applied to many different types of group activities, in this publication it refers to a formal business model. Cooperative businesses are found in nearly all countries, in numerous and varied sectors of the economy. As Ivan Emelianoff (1942, 13), a respected cooperative scholar, once remarked, "the diversity of cooperatives is kaleidoscopic and their variability is literally infinite." As a consequence of this diversity, no universally accepted definition of a cooperative exists. Two definitions, however, are commonly used.

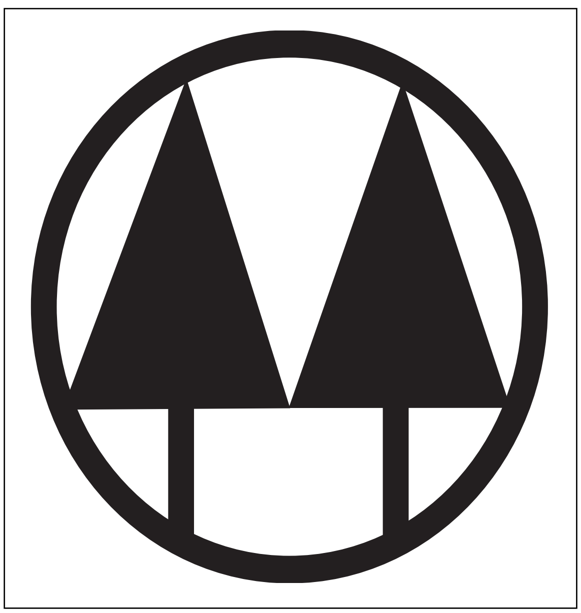

Figure 1.—*The "twin pines" is a familiar symbol for cooperatives in the United States. The Cooperative League of the USA, which eventually became the National Cooperative Business Association (NCBA), adopted it as their logo in 1922. The pine tree is an ancient symbol of endurance and immortality. The two pines represent mutual cooperation—people helping people.*

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Building that forest family of small landowners—if we can develop a vision of what forest land can be today and tomorrow, and collectively work together to bring that initiative forward, it works for everybody.

Western Upper Peninsula Forest Improvement District Member

According to the International Co-operative Alliance (ICA), a cooperative is an autonomous association of persons united voluntarily to meet their common economic, social, and cultural needs and aspirations through a jointly owned and democratically controlled enterprise. Cooperative leaders around the world recognize the ICA, a non-governmental organization with more than 230 member organizations from more than 100 countries, as a leading authority on cooperative definition and values. The ICA definition recognizes the essential element of cooperatives: membership is *voluntary*. True cooperation with others arises from a belief in mutual help; it can't be coerced. In authentic cooperatives, people join voluntarily and have the freedom to quit the cooperative at any time. Therefore, the forced collectives prevalent in the former Soviet Union, for example, were not true cooperatives.

Another widely accepted cooperative definition is the one adopted by the U.S. Department of Agriculture (USDA) in 1987: a cooperative is a user-owned, user-controlled business that distributes benefits on the basis of use. This definition captures what are generally considered the three hallmarks of cooperatives: user-ownership, user-control, and proportional distribution of benefits. The "user-owner" principle implies that the people who use the co-op (members) help finance the co-op and, therefore, own the co-op. Members are responsible for providing at least some of the cooperative's capital. The equity capital contribution of each member should be in equal proportion to that member's use (patronage) of the co-op. This shared financing creates joint ownership. Cooperatives can certainly acquire debt capital, and in fact there are banks (such as CoBank and the National Cooperative Bank) that primarily loan to cooperatives. Typically, members generally contribute at least half of the capital in most cooperatives. They can contribute their share over time or when they join.

The "user-control" concept means that cooperative members govern their organization. They approve and amend the co-op's governing principles—the articles of incorporation and bylaws. They also elect a board of directors and must approve all mergers and any bankruptcy decisions. Cooperative state statutes and bylaws usually dictate that only active co-op members (those who use the co-op) are eligible to become voting directors, although nonmembers sometimes serve on boards in a non-voting, advisory capacity. Advisory directors are becoming more common in large agricultural cooperatives in the U.S., where complex financial and business operations require the expertise of financial and industry experts.

Voting rights are generally tied to membership status, usually one-member, one-vote, and not to the level of investment in or patronage of the cooperative. Cooperative law in a number of states in the U.S. and in other countries, however, also permits proportional voting. Instead of one vote per member, voting rights are based on the volume of business the member transacted the previous year with the cooperative. Generally, however, to prevent control by a minority of members, there is also a maximum number of votes any member may cast. For example, a grain cooperative might permit one vote to be cast for each 1,000 bushels of grain marketed the year before, but any single member would be limited to a maximum of 10 votes. Democratic control is maintained by tying voting rights to patronage. Equitable voting, or democratic control, is a quintessential attribute of cooperatives.

Cooperatives are bottom-up, not top-down organizations (fig. 2). Member control in a cooperative should not, however, extend into daily operations of the business. In most cooperatives, the board of directors hires a manager to take care of business. It is essential that the board understands the manager's (or management team's) responsibilities and does not try to micromanage the business. Therefore, it is important that care is taken in hiring a highly qualified, trustworthy individual as manager. The manager, the only employee that answers directly to the board, is responsible for carrying out the mission and vision of the cooperative, as established by the board of directors. In certain types of cooperatives—worker-owned or those managed as collectives—the members may also run the daily operations of the business.

"Distribution of benefits on the basis of use" is another key foundation for cooperatives. Members should share the benefits, costs, and risks of doing business in equal proportion to their patronage. The proportional basis is fair, easily explained (transparent), and entirely feasible from an operational standpoint. To do otherwise distorts the individual contributions of members and diminishes their incentives to join and patronize the cooperative.

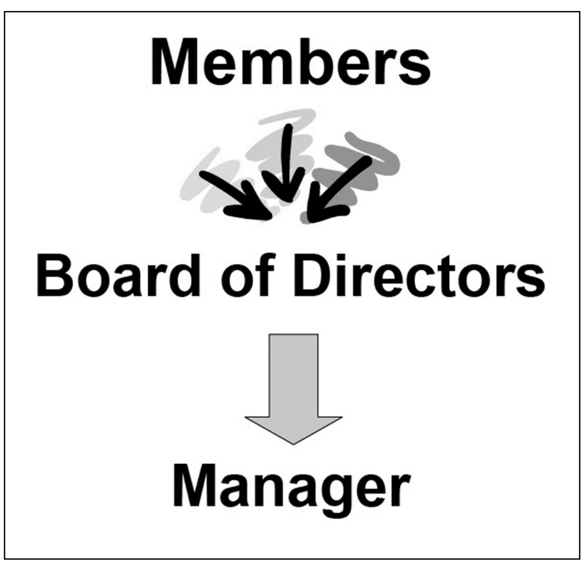

Figure 2.—*Typical organization of a cooperative. (Source: Margaret Bau, USDA Rural Business Cooperative Service).*

I think if our cooperative could gather those products and seek higher-end, higher-value markets for them, we could really help stimulate the rural economy. Again, right now, mostly we have a collection of individual businesses out there trying to make a go of it by themselves. But if a co-op could really strongly act as a marketing entity, I think it could really help raise the profitability of all those businesses collectively.

Lewis County, Washington, Potential Cooperative Member

Co-op benefits may include better prices for goods and services, improved services, and dependable sources of inputs and markets for outputs. Most cooperatives also realize annual net profits, all or part of which are returned to members in proportion to their patronage (thus, they are aptly called patronage refunds). Cooperatives also can return a portion of their profits as dividends on investment. In the U.S., however, Federal and most State statutes set an 8-percent maximum on annual dividend payments to ensure that the benefits of a cooperative accrue to those who use it most rather than to those who may have the most invested. Today, some co-op leaders and scholars consider this dividend restriction arbitrary and harmful to cooperatives. From their perspective, the 8-percent maximum makes investing in cooperatives less attractive than other forms of business. It makes cooperatives less competitive as well, especially in the agricultural processing sector, which requires a lot of capital for startup and growth.

In sum, cooperatives are organized to serve member needs and are focused on generating member benefits rather than returns to investors. This member-driven orientation makes them fundamentally different from other corporations. Additional cooperative structural characteristics and guiding principles further distinguish them from other business models. In most countries, the cooperative model represents only one of several different ways a business can choose to legally organize. One should consider many factors when choosing a business structure, including the liability of investors/owners, equity requirements, tax treatment, and ease/cost of business startup.

There are four basic categories of business in the U.S. (table 1). The sole proprietorship is the simplest, oldest, and most numerous of all types of business. One person owns and controls the enterprise. Partnerships involve at least two individuals. The primary downside of general partnerships and proprietorships is the unlimited liability: owners may lose not only their investment in the business, but also their other assets. The Limited Liability Company (LLC) is perhaps the most popular business form for multiple investors right now. It is a special type of partnership with a lot of flexibility and the limited liability status of other corporations. The fourth category includes all corporations. A cooperative is a special type of corporation, a subchapter T. The most predominant form of corporation (e.g., those traded on a public stock exchange) is the subchapter C. Any type of business can elect to be a nonprofit. Many people think of cooperatives as nonprofit enterprises, but this is incorrect. Most cooperatives in the U.S. are profit-oriented enterprises. However, unlike C-corporations, cooperatives return a portion or all of their profits to their members on the basis of their patronage rather than their investment levels.

Table 1.—*Basic business structures in the United States.*

Structure	Variation
Sole proprietorship	
Partnership	
Limited liability company (LLC)	
Corporation	Subchapter S
	Investor-owned firm (Subchapter C)
	Cooperative (Subchapter T)

Cooperatives in the U.S. Economy

Cooperatives exist in nearly every segment of our economy and have a significant economic impact. Cooperatives range in size from just a few employees in one small office, to very large firms with multinational operations. Most people are familiar with the large agricultural cooperative brand names such as Land O'Lakes in Minnesota, Cabot Creamery in Vermont, and Ocean Spray. Farmers create farm supply and marketing cooperatives to help them maximize their farms' net profits. This requires both effectively marketing their products for better prices as well as keeping input costs as low as possible. The farmers recognize they are more efficient and knowledgeable as producers than as marketers or purchasers. By selling and buying in larger volumes through a cooperative, they also can usually achieve better prices.

Consumer cooperatives are established to sell the products a group of consumers want but cannot find elsewhere at affordable prices. The consumer members are primarily interested in improving their purchasing power—the quantity of goods and services they can buy with their income. They naturally wish to get as much as possible for their money in terms of quantity and quality. As owners, the members have a say in what products their stores carry. Most people are probably familiar with local consumer food cooperatives, which often sell a whole range of grocery and health products, but often focus on natural or organic foods.

Rural utility cooperatives, created in the 1930s but now given a new image with the touchstone energy marketing campaign, credit unions, and health care cooperatives are also familiar to most of us. But cooperatives also exist in many other industries as well—ski resorts, newspapers, orchestras, funeral homes, and more. In some cases, these are worker-owned cooperatives. As the name suggests, a worker-owned cooperative is owned and controlled by its employees. Employees establish cooperatives in the hopes of increasing their wages and fringe benefits, improving their general working conditions, and ensuring job security.

Cooperatives play an important role in the American economy. About 48,000 cooperatives, operating in nearly every business sector imaginable, serve 120 million members, or roughly 4 out of 10 Americans (National Cooperative Business Association 2003a). The National Cooperative Bank keeps track of the top revenue generating cooperatives in America. Each co-op listed on its Co-op 100 index generated at least $346 million in revenue during 2002. Several cooperatives have been on the Fortune 500 list. The top 100 cooperatives in the U.S. generated, in the aggregate, $119 billion in 2002 (National Cooperative Business Association 2003b). They represent agriculture, finance, grocery, hardware, healthcare, recreation, and energy industries. Cooperatives are especially important to agriculture. In 2002, 3,140 agricultural cooperatives—with roughly 3.1 million farmer members (many farmers are members of more than one cooperative)—marketed and/or processed farm commodities, sold farm supplies, and provided other farm-related services. In 2001, they captured 28 percent of the market share of the cash value of products marketed by farmers and of the inputs purchased by farmers (Eversull 2004). In terms of nonagricultural cooperatives, 84 million Americans are members of 9,569 credit unions; 865 electric co-ops serve 37 million people in 47 States; more than 1.5 million families live in housing cooperatives; and more than 3 million people are members of 5,000 food cooperatives (Consumer Federation of America 2004, National Association of Housing Cooperatives 2004, National Rural Electric Cooperative Association 2004, United States Credit Union 2003).

Conclusions

When people think of cooperatives, they probably tend to think of their local consumer co-op or credit union or one of the large agricultural cooperatives. But cooperatives play a much broader role in our economy. It is therefore not surprising that people are rediscovering the cooperative model for applications in forestry.

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