

**CALIFORNIA'S
CONTRIBUTIONS TO
COOPERATION**



by
Leon Garoyan

**Center for Cooperatives
University of California, Davis**

THE CENTER FOR COOPERATIVES

WORKING PAPER SERIES

The Working Paper Series is designed to fulfill part of the less-formal communications objectives of the Center for Cooperatives. The series presents papers dealing with cooperative issues or topics of interest to cooperative members, employees, elected officials, and others having an interest in cooperatives. Papers in this series express viewpoints and opinions about a fairly broad spectrum of cooperative topics, but are not intended to be finished reports of formalized research by the authors. Some papers are informative only, while others are, in addition, provocative. We intend for them to be educational.

Working Papers are published at irregular intervals, reflecting the financial position of the Center, as well as the interests of authors and availability of papers. They are intended to be brief in nature because they most frequently will not be exhaustive of their subject, but no editorial limits are imposed. Likewise, because the papers reflect opinions and viewpoints of the authors, there is only minor editing involved.

We hope the papers contribute to a better understanding of cooperatives and lead readers to other more comprehensive publications on topics where further information is desired.

Because the mandate from the California Legislature, when it established the Center, intended that research and educational activities include both agricultural and mutual benefit cooperatives, the Working Paper Series may include papers of interest to both sectors. However, at times the emphasis may be stronger with only one of the two cooperative audiences. To help readers to identify the intended orientation, we follow a numbering system that distinguishes the intended audience by major orientation. Though papers are numbered consecutively during each year, those with primarily an agricultural orientation have the suffix A with the number, and those primarily oriented to mutual benefit cooperatives are suffixed by MB.

Leon Garoyan
Director

**CALIFORNIA'S CONTRIBUTIONS
TO COOPERATION**

by
Leon Garoyan

**University of California - Davis
July, 1989**

CALIFORNIA'S CONTRIBUTIONS TO AGRICULTURAL COOPERATION

Leon Garoyan
Director, Center for Cooperatives
University of California - Davis

Cooperatives have long been an important part of this nation's agricultural production, processing and distribution system. Cooperatives were developed as imperfections within the market system permitted firms to exercise independent decisions that affected alternatives and services available to farmers.

THE 1920'S SCENE

Agricultural cooperatives developed during difficult economic conditions. Consider this scenario: It is 1920. The U.S. has signed an armistice following victory during World War I. The world is seeking to return to normalcy after four years of devastation in Europe, and near economic ruin. American farmers increased production during the war years to feed our nation and its military force, and provided food to our allies. Following a brief economic recovery in the early 1920's, farm prices plummeted sharply, and agriculture slipped into a deep recession.

At this time, the nation's many farmers faced huge debts that many were unable to meet, and many foreclosures were threatened or occurring. Agricultural supplies and processing were dominated by a comparatively small number of very large industrial firms. Farmers were disorganized, farm organizations were not too effective, farmers lacked strong national leaders and agriculture and individual farmers were in deep trouble. The cooperatives that existed were young, inexperienced, threatened by powerful economic forces controlled by large corporations, and poorly or inadequately financed, often by personal commitments guaranteed by directors' or members' farm assets. The best means of transportation were the railroads, a relatively trying method. Communications were slow, and often farmers who shipped commodities to distant markets were unaware of the returns to be received from terminal market operators.

California's farmers faced an additional problem to those encountered elsewhere. They produced quality products in volumes that exceeded local requirements and which required distribution to product-deficient, populated regions in eastern markets. The marketing functions required were performed so poorly that farmers were compelled to become involved. They did so reluctantly, preferring to leave off-farm services to firms that

specialized in preparing and moving products to consumers. However, greed, inadequate facilities, poor payment practices and poor results compelled farmers to enter into activities about which they were not well informed.

There were few models after which they could pattern their cooperative organizations. There were no cooperative enabling laws for the earliest cooperatives, so some organized under general corporation laws. They faced a hostile environment, not only from the private firms that had caused farmers discontent and with which they had begun to compete, but also from federal and state trade regulators, who considered cooperatives as combinations in restraint of trade. As they faced problems of finance, directors pledged their own assets to be able to finance the new cooperative. In some cases, they assumed management responsibilities until professional managers were willing to be employed by the fledgling cooperatives.

DEVELOPMENT OF THE COOPERATIVE MODELS

From these adversities evolved several models of cooperation that reflected the problems and unique tasks required by farmers of their cooperatives. What was unique to the California experience was the problem of marketing highly perishable commodities in distant population centers under conditions of primitive and relatively slow transport conditions. It is no surprise that California farmers focused their energies and resources on the development of processing and marketing cooperatives. They developed only slight interest in providing farm supplies through cooperatives, because large private suppliers were developing fairly efficient farm input services. Besides, farmer's returns were affected more by market forces than by saving 5 to 10 percent on purchases of production inputs, since most production materials were produced on the farm in those years.

The California model did not mesh closely to traditional economic theories of cooperation being developed in the U.S. mid-west and central states. To understand the differences in approach, I first present a brief description of the mid-west models before discussing the California approaches.

THE COOPERATIVE AS AN EXTENSION OF MEMBERS FARMS

One mid-west theory considers a cooperative as an extension of the individual farms of members; the cooperative's objectives are said to be to maximize the welfare of individual members. The main characteristics of a cooperative within this model are:

1. An enterprise where the member's farm is the main decision-making structure. The aggregate decisions of members determine volume for the cooperative, whose function is to be prepared to handle the entire output of all members, regardless of market needs.
2. Prices established by the cooperative becomes the marginal cost or revenue to any one member, but actually represents the cooperative's average cost. Thus, reaching an equilibrium position is difficult for the cooperative and its members.
3. Often, such a cooperative deals with a homogeneous commodity- - wheat, milk, farm supplies, etc., which have distinct and undifferentiated (non-branded) markets.

While such a model seems to have been functioning satisfactorily in some situations, it has some weaknesses that did not make it attractive to many California conditions. The main weaknesses are:

1. The cooperative has no real economic authority of its own. It is passive with regard to quantities, and even the timing and conditions of product deliveries by members.
2. The Cooperative is mainly interested in decisions about how to use the products of its members, not mainly in meeting market needs. (It is production oriented, not market driven.)
3. The cooperative cannot achieve a full joint vertical integration because it is unable to match individual member's needs with the cooperative's potentials.
4. Capital, activities, production, qualities, etc., cannot be assigned in a way to maximize aggregate returns.

These weaknesses are sufficiently serious that they would cause severe difficulties for a cooperative required to meet the characteristics of many of California's commodities, both in terms of production and marketing requirements. While adequate for mid-western conditions and theoretically attractive to scholars, the model received scant attention in California.

THE COOPERATIVE AS A HORIZONTAL COMBINATION

A closely related model is the cooperative as a horizontal combination of farmers-members. The objective of such a cooperative is to select or conduct an optimal marketing or buying program for the members as a group. Its main characteristics are:

1. Free entry and exit by members.
2. The cooperative has its own production function - its own independent costs and revenues.
3. The traditional economic theory of the firm prevails, i.e., the cooperative is a maximizer which operates where its marginal cost is equal to its marginal revenue, just as with investor businesses.

While overcoming some of the weaknesses of the previous model (portraying the cooperative as an extension of member's farms), this model also has several weaknesses.

1. It assumes the interests of members are homogeneous. Where members have conflicting interest, serious member relations problems can arise.
2. Members often follow independent decisions which they consider to be in their own best interests. This presents risks when the cooperative faces investment decisions based on some minimal commitment by members.

COMPETITIVE YARDSTICK

E. G. Nourse, a renowned economist and presidential economic advisor, viewed the role of cooperatives to be to instill competition in the market system. Termed the "Competitive Yardstick" model, this views the cooperative enterprise as a yardstick for individual members to evaluate the performance of the existing market system. Nourse considered cooperatives as an integral part of the existing market system, whose main function was to contribute to business efficiency by competing with established firms. A dominant position was not necessary for a cooperative to instill competition, since all that was considered important was to establish a balance or checkpoint when services were inadequate or charges too high. John Galbraith, Professor of Economics at Harvard, later called this "Countervailing Power".

During Nourse's time, this may have been a realistic objective. Certainly, the large number of farm cooperatives organized as first handlers were so successful that they were able to virtually eliminate most profits at that level, so that as cooperatives succeeded only a few enterprises were able to operate with even normal profits.

While probably an appropriate concept for its time, cooperatives are now seldom able to be effective yardsticks at the levels within the market system where the largest profits still exist—at the finished foods markets in highly differentiated (branded) situations.

THE CALIFORNIA MODELS

The "mid-west" concepts are in sharp contrast to the Sapiro or early California school of thought of the 1920's. Aaron Sapiro, a bright young California lawyer, earned fame in U.S. agricultural history as an organizer of cooperative marketing associations in the early 1920's. He was one of the most eloquent, sensational and controversial individuals to participate in this nation's cooperative movement. Supporters have described him as a "peerless evangelist of cooperation, the father of cooperative marketing", while critics have labeled him, "an agricultural Napoleon and an exploiter of the crusade he pushed forward (2, p. 242). For a few years he enjoyed unparalleled popularity among U.S. farmers, but around 1925—when a number of his cooperatives were failing—his name lost its appeal in rural America. Yet, Sapiro made a substantial and indelible mark on U.S. agricultural cooperation. Many of the organizations he helped organize in the U.S. and Canada have evolved into large, successful food marketing cooperatives. The cooperative marketing bill he drew up in 1919, which became known as the California Plan, served as a model bill for cooperative legislation in 26 states. The California Plan language also influenced the Capper-Volstead Act of 1922, sometimes referred to as the Magna Carta of cooperative legislation. Sapiro travelled widely in the U.S. and Canada by train. Imagine what impact he would have had if present-day air travel had enabled this vigorous individual to mount his crusade against the tyranny farmers then faced.

ELEMENTS OF SAPIRO'S PLAN

Sapiro's Plan for cooperative marketing contained eight basic elements, all of which he felt were necessary for success, but which were not necessarily original with him (5, p.9).

1. Organization of the cooperative on a commodity basis.
2. Long-term, legally-binding contracts with growers members.
3. Centralized organization.
4. Pooling products according to grade.
5. Controlling a large enough proportion of the crop to be a dominant market factor.
6. Democratic control of cooperatives by members.
7. Use of experts in technical positions.
8. Limitation of membership to growers.

When outlining the California Plan, Sapiro often included four additional "Principles of successful merchandising": (1) Grading and standardizing products to improve quality; (2) Packaging products for effective shipment and to attract buyers; (3) Extending markets by time, place and increased use; (4) Earning profits by matching market supply with demand.

EVALUATION OF THE SAPIRO MODEL

Commodity Organization

Sapiro believed that cooperatives should be organized on the basis of the commodity involved, not with regard to the locality in which it operates. He felt that locality is important for the production of agricultural goods, but that the commodity is the sole interest in marketing. He did draw some practical limitations here, usually consisting of state boundaries, because of the difficulties interstate organizations might encounter in enforcing their contracts. He also conceded that local associations might handle perishable products and that one organization might handle two or more similar commodities. For example, Sunkist markets navel and Valencia oranges, lemons, and grapefruit. However, Sapiro felt that the advantages of specialization outweighed the advantages of diversification. Commodity marketing was basic to his ultimate goal of a legal monopoly for producers of a given commodity.

Under the circumstances that prevailed in those days, where buyer specialization was common, and substitution among products was fairly low because of the short seasonal availability of competing commodities, Sapiro's orientation toward strong, single commodity marketing organizations is understandable.

While there are both advantages and disadvantages to specialization on a commodity basis, it is unrealistic today to conclude that this model meets all

requirements for cooperative organization. U.S. agriculture is by definition highly diversified and the geographic specialization that once characterized much of U.S. agriculture is no longer as strong. There are many farm products whose handling, processing, and marketing actually complement each other, in terms of facility requirements and customer buying practices. Transportation of products may necessitate the consolidation of several products to meet modern-day merchandising requirements.

Generally, advantages of multiple-commodity marketing firms include the following:

1. They eliminate the necessity, expense and effort of setting up several marketing associations to perform the same business functions, often to the same buyers.
2. They increase the volume of business of a cooperative without necessarily increasing overhead costs.
3. They facilitate continuous operations of the cooperative if marketing seasons of respective crops are consecutive.
4. They enable the cooperative to deal in a full line of products to attract large-scale retailers.
5. They facilitate use of broadly-advertised consumer labels for a family of products marketing strategy.

Some single-commodity organizations continue to effectively market their members' products, although this seems to be breaking down. Some once specialized dairy co-ops, such as Land O'Lakes, are now diversified into many product lines.

We can identify some criteria in which single commodity organizations remain appropriate. These include situations where the commodity is the main product in a region, such as Kansas wheat; where regional production isolation exists, such as California rice; where the commodity is subjected to further and substantial processing or manufacturing before being sold to consumers, such as beef; where the demand is so unique that the commodity has little complementarity with other products, such as cranberries; and where the processing technology is so specialized or complex that large scales of operation are required, such as vegetable oil crushing. Under such circumstances single commodity organizations appear to be appropriate, but under circumstances other than those identified, single commodity marketing cooperatives would appear to be at a disadvantage under today's economic environment.

We doubt that Sapiro was concerned with such criteria, however. It is more obvious that he understood the concepts of monopoly power, and built his organizational concepts around the ideal of achieving monopoly power. We suspect that public policy today would look with disfavor on monopolizations of agricultural marketing, if it were possible to be achieved by cooperatives under present circumstances.

Marketing Contracts

It is evident that Sapiro recognized the marketing contract as the main basis for establishing and retaining a monopoly position. Sapiro, an advocate of long-term enforceable contracts with members, made the following statement in 1923:

"The contract should always be a long-term agreement. It is impossible for farmers in a period of less than five years to develop trained personnel, to perfect the process of receiving the commodity, to make good and wise commercial connections, and to effect satisfactory banking arrangements. A short-term contract is hardly worth the paper it is written on. A long-term contract gives the farmer a chance. There should be no right of withdrawal whatsoever, except at the end of a specified long term. If the farmers intend to try the cooperative marketing system, they should go into that work seriously, honestly, and on a permanent basis."

Sapiro also stipulated that the contracts take effect only after a fixed minimum sign-up was achieved. This sign-up varied from 30 percent to 75 percent of qualified growers, depending on the commodity and the local conditions. He made it clear that any man who signed a contract was legally bound to deliver his entire crop to the cooperative.

Sapiro's "ironclad" contracts emphasized their enforcement through the courts, with provisions for substantial liquidated damages when breaches in contract terms occurred. This emphasis is still an important ingredient for contract performance.

Since Sapiro's time, contracts have played an expanding role in coordinating U.S. agricultural production, processing and distribution. Cooperatives and other firms use contracts to coordinate various stages of the food industry. It is estimated that the proportion of all U.S. farm output produced under contract was about 15 percent in 1960 and 17 percent in 1970, to perhaps over 25 percent today. Contract marketing for specific commodity groups include:

Over 95 percent for broilers, fluid milk, sugar beets, and vegetable seeds.

About 90 percent for potatoes and vegetables for processing, and hybrid seed corn.

About 85 percent for turkeys.

Seventy-five percent for citrus.

Fifty percent for fresh market vegetable and potatoes (1).

Firms processing and marketing these commodities find contracts a valuable instrument for coordinating procurement, processing and sales.

Sapiro's emphasis on contracts was sound, but he failed to perfect its mechanics. He advocated agreements with lengths of from five to 15 years, which terminated only at the end of this time. Three serious objections to long-term contracts are: (1) Many producers will not obligate themselves for such a long period of time; (2) by themselves they do not ensure that an organization will be successful; (3) contracts do not assure equity between buyers and sellers. Equity must usually be negotiated. Also, Sapiro's recommended minimum volume is too large; a much smaller proportion of a commodity's producers could form a cooperative and significantly improve their marketing efficiency.

Perhaps in the light of day in the early 1920's, the objective to organize countervailing monopoly power for farmers through strong commodity cooperatives with long-term supply or production contracts was necessary. Even under today's economic conditions, contracts are a necessary condition to bring about production-marketing coordination, and to provide cooperatives with a predictable quantity of products for sale. Sapiro was correct in emphasizing the needs for contracts, but viewed under today's environment, he was correct for the wrong reason. The benefits of coordination appear more important than does the need for monopoly power.

Centralized Structure

Sapiro advocated large-scale commodity associations with a centralized membership and management structure. His favorite organizational method was to hold a grower meeting at which his eloquent verbal presentation and his extraordinary store of information frequently induced the audience to set up an overhead organization. This organization would then conduct an intensive membership campaign, and growers would sign an enforceable contract to deliver to the association all of the commodity they produced for a period of five to 15 years. The centralized cooperative would coordinate delivery of the crop, and perform needed marketing functions.

Sapiro's "top-down" organization philosophy was diametrically opposed to the traditional mid-west cooperative leaders of his era, such as Nourse and John D. Black, who favored the "ground up" approach to cooperative development.

The latter believed that federations of local cooperatives should perform central sales and other overhead services, gaining size advantages while maintaining democratic control at the local level.

Centralized cooperatives have both advantages and disadvantages. They can be organized relatively quickly, they facilitate decision-making and information-generation during unstable periods, and they may reduce costly duplication of facilities, personnel and services. On the other hand, producers usually give up participation in some decisions and personal interaction in a large, centralized organization. Also, the importance of effective two-way communication increases as the size of the centralized cooperative increases; when members are dispersed geographically over a large region; and when diversity of interests exist among members.

During the past decade there has been some movement toward centralized structures among U.S. cooperatives. The need for timely, consistent decisions probably will induce cooperatives toward the centralized type of organization during the next decade. Various theories of motivation developed by social scientists, can be employed to improve opportunities and incentives for membership participation in centralized structures, thus minimizing this possible disadvantage.

Use of Capital Stock

Faced with the necessity of financing large investments in cooperative facilities and processing equipment, Sapiro evolved a non-voting preferred stock system of financing corporate subsidiaries of cooperatives. It was a scheme designed to enable farmers to undertake functions calling for large expenditures, such as processing or packing plants. Upon the formation of a capital stock subsidiary for the purpose of acquiring facilities, its non-voting preferred stock was sold to interested growers or outside investors while the cooperative held the common stock. In time, the subsidiary would repurchase part of the preferred stock annually, financed by withholdings from the proceeds of the members' products sold by the cooperative. After a period of years, the parent cooperative acquired ownership of the facilities through its ownership of the common stock.

Sapiro made extensive use of this method of financing. By his estimate, more than \$100 million worth of properties were acquired before the cooperatives even had any ability to pay for them. In time, banks withdrew their support for the scheme, but in the interim it made it possible for

farmers to organize cooperatives. In view of depressed commodity prices and low farm incomes, perhaps few cooperatives could have been financed from within agriculture alone.

Some believe Sapiro did not make a lasting contribution to cooperative finance. I do not share that view. He encouraged innovations that for a period served cooperative members' needs, and which even today, may prove helpful. At least one of the newer cooperatives organized in California as a result of plant closures by proprietary firms is being financed along concepts developed by Sapiro 60 years ago. When Pacific Coast Producers organized as a cooperative in 1970, it established a limited partnership for investors, (including members of the cooperative), which committed capital for the purchase of plants and equipment, and a general partnership comprised of cooperative members. The cooperative then entered into a long-term lease for use of the assets owned by the limited partners.

Pooling

Some consider the key to the California plan to have been the use of marketing pools. Sapiro held that provisions should be made for pools to which the growers' products were assigned upon receipt by the association. Any number of pools could be formed by the cooperative; they would be differentiated by quality, size, or type of products, with each pool made up of uniform products. Through the use of pooling, Sapiro contended, a group of farmers could collectively realize "absolute cooperation". He set no definite time for the final and full payment to members for their crops; this decision rested with the cooperative association and its banks.

Pooling is widely used by many California marketing cooperatives today. Its application varies from a single pool for several commodities to many pools (based on season, quality, and type of finished product) for the same commodity. There are both problems and benefits which cooperative marketing associations encounter in using internal pools.

Problems:

1. Farmers supplying higher-quality products are penalized when pooling is not structured properly, different-quality products are mixed, or settlement is made on a flat-price basis. There is no economic incentive to produce or market high quality products through the cooperative in such cases.
2. A large number of grade and variety pools may cost more to operate than their benefits justify.

Benefits:

1. Pooling spreads marketing risks among many producers. Members seldom can guess when the highest price will occur, and often may suffer financially as they try to “top” the market price.
2. Management gains flexibility in merchandising the association’s products.
3. Pooling may enable the association to finance its operations more easily.
4. Pooling may be an important factor in determining the market price of a product if the cooperative controls a relatively large market share.

Pooling, like marketing contracts, may be very helpful to a cooperative if used properly. Sapiro failed to recognize that the desirability of the use of internal pools in marketing cooperatives is heavily dependent upon the nature of the commodity and the characteristics of the membership of the cooperative. If the commodity is non-perishable, and quality variation is relatively small, pools normally are conducive to the success of the cooperative. Pooling may also be effective even where large differences in product size and quality exist if there is sufficient volume available to the cooperative to take advantage of these differences to meet specific market demands. Some believe marketing of highly perishable commodities may not be adapted to the pool method, but experience dispels this belief.

The significant contribution of Sapiro was in advocating pooling as a method of marketing commodities. I consider pooling to be a significant procedure for cooperative marketing which still has wide-spread application even to wheat, feed grains, livestock, and other commodities for which grades and standards exist. As use of long-term contracting increases, and where contract prices are unspecified, pooling may be an effective means to establish value for individual producers.

Market Control

The cooperative association should control a large proportion of the total crop to be marketed, Sapiro argued. While it need not be a complete monopoly, it should be the largest single firm in its particular field. Price leadership was implied and sometimes explicitly stated as an objective. This principle correlated with his minimum sign-up of 30-75 percent before marketing contracts went into effect.

Commodity marketing cooperatives that emerged under Sapiro's influence were designed to achieve monopoly control over the market supply of a commodity (5,p.208). Control of a large market share has been considered as a reasonable business objective, but the concept of monopoly power as a means of specifying producer prices was not widely accepted by cooperative leaders even during Sapiro's years.

At the time of his influence, the debate was between form of organization, either as centralized commodity associations as advocated by Sapiro, or as federations of local cooperatives where the "regional" provided marketing activities. Both organization structural forms persist today. But increased emphasis is given to market power rather than monopoly power. Sapiro emphasized market control through monopoly. Others emphasized market power through marketing programs and activities.

Today, bargaining cooperatives remain more nearly in alignment with Sapiro's concepts than do cooperatives performing other functions. Public policy as interpreted by the courts and more vigorously advocated by bureaucrats looks with disfavor not only with the exercise of market dominance, but also with the possession of it. Thus, Sapiro's structural concepts would not now be favorably accepted.

Democratic Member Control

Sapiro believed that each association should be governed democratically, which he defined as the nomination and annual election of a board of directors by members, each of whom had a single vote. He insisted on voting "by men and not by bales of cotton, bags of walnuts, boxes of oranges, or cows".

Most cooperatives before and during Sapiro's era were organized on a one-man, one-vote basis. Many associations today also adhere to this principle, which is most appropriate in regions and commodities where farm size is fairly uniform and membership investment and use of the cooperative's facilities are homogeneous.

Many California cooperatives allow voting on the basis of patronage, a concept more appealing to the relatively large producer with the most to gain or lose through cooperation. The most common method provides all producers with one vote, and additional votes based on acres or tons or dollar volume, with some maximum number of votes for the largest members. Where producers size varies widely, this system usually is more equitable than the one-man, one-vote method. When disproportionate use of a cooperative's facilities exist among members, the concept of equitable treatment of members may be more realistic than equal treatment.

Expert Management

Sapiro contended that the "modern cooperative marketing organization is a highly technical form of business institution....devised for the most successful marketing of farm products in the interest of its member farmers, and for nothing else". Members should concentrate on their proper function—production—and should hire experts, at adequate salaries, to sell their products.

Sapiro's philosophy probably is more widely accepted today than it was in the 1920's, and we have both good and bad implications. During Sapiro's era, many cooperatives hired farmers (on a part-time or full-time basis) as managers. Some associations by policy required management to be farmer-members. Vestiges of this philosophy can be found in a few organizations today. But most contemporary cooperative members recognize the value of sophisticated, well-trained management personnel, and are willing to pay the salaries necessary to attract and retain such expertise.

On the other hand, we find it unacceptable under the current economic environment to discourage producers from keeping abreast of the market place. A market-oriented philosophy involves producing products designed to meet consumer demands. This implies a changed function for the cooperative, whose objective has been constantly articulated to be to serve the producer's needs. A market-oriented philosophy would involve the cooperative as an instrument for meeting customer—not producer needs; meeting the customers' buying needs as a means of fulfilling farmers' production needs.

Grower Members

Sapiro's plan called for cooperative associations composed exclusively of farmers, to prevent widespread diversity of interests among members. This practice has been followed since the cooperative marketing movement began and still prevails today. In fact, cooperative law and tax regulations place limits on the proportion of non-farmer and non-members allowed to patronize an association. No distinction is made between full-time farmer and persons who produce agricultural commodities as an ancillary activity, however.

OTHER CALIFORNIA MODELS

Few cooperative leaders today recognize the Sapiro features to be found in their cooperative organizations. Yet the features are present and strongly supported. Cooperatives today seem to believe they are more structured to market conditions than was Sapiro. They take active roles in industry

matters; they strongly support marketing orders when applicable; and they tend to consider themselves as operating business organizations formed as cooperatives. This view is supported by the two cooperative models described below which many believe to be typical of the current cooperative organizations of California.

COOPERATIVES AS A COMMON BUSINESS ORGANIZATION

The Helmlinger-Hoos model views the cooperative as a common business organization but which operates at cost, and proportionately returns its earnings to members. Its objective is to maximize benefits to members through the identification of market requirements, which it seeks to meet by entering into contracts with members for the production of specific volumes of desired varieties and commodities. This model comes closest to describing the typical California marketing cooperative.

Other characteristics of this model include:

1. The cooperative operates as a decision maker in its own interests, which it translates to members in terms of product, volume and time of delivery decisions.
2. Investments made for brand differentiation and processing facilities are based on scale economies necessary to remain efficient and to meet market needs without holding large surpluses of commodities. The cooperative assumes less of a role as industry leader than as a leader in the markets in which it operates.

Some criticisms of this model are:

1. Its apparent detachment from farmers self-interests and the imposition of production decisions on members. Some would criticize the model because it differs only slightly from a vertically-integrated business. A significant difference is that the board of directors of the cooperative are farmer-members and the direct representatives of the membership.
2. The practice of allocating volumes, monitoring cultural practices, and determining planting and harvesting schedules may not be consistent with every member's needs for production planning.

BARGAINING COOPERATIVES

California has a number of cooperatives whose function is to negotiate prices to be paid for members commodities and terms of trade to be in effect. In reality, bargaining cooperatives are a variation of marketing cooperatives, and in some cases, both types of cooperative may function within the same commodity sector.

Bargaining cooperatives seek to represent a minimum of 35-40 percent of the volume for a commodity, excluding volume of other marketing cooperatives. They are supported by commercial farmers who may prefer to sell to non-cooperative processors, or are unable to be members of marketing (processing) cooperatives because of membership restrictions.

California's bargaining cooperatives have been effective in increasing returns to all growers, since non-members benefit from the umbrella effect of cooperative bargaining. Bargaining cooperatives face tough, large-scale processors who previously have been able to independently determine prices and terms of trade. Bargaining cooperatives have needed to develop a strong grower base and market share, and to rely on accurate market and economic information to be credible negotiators on behalf of members.

CURRENT COOPERATIVE ISSUES

Sapiro contributed immensely to the development of California's agricultural marketing cooperatives. Many of his concepts not only guided early cooperative development, but still remain as features of existing cooperatives. What we have learned is no model meets cooperative membership needs into perpetuity, because external forces compel internal structural changes. Cooperatives are living, dynamic enterprises and they are subject to change as economic conditions require. California's cooperatives that operate as business organizations, and bargaining cooperatives are indications that changes are being made.

Sapiro's concepts were appropriate for a time and a place, and in some instances, are still valid. Yet Sapiro, as brilliant and pragmatic as he was, must surely agree: Cooperatives must accept the best of philosophies, abandon those inappropriate, and get on with their work. Some of the work they may need to get on with are described in the following section.

HOW TO DEFINE A COOPERATIVE

At issue is the question, what is a cooperative? How should it be organized, financed and operated?

One definition considers a cooperative to consist of two essential elements: (1) a democratic association of persons, and (2) an economic enterprise. "In separating these two for the purpose of analysis the essential is lost, since it is in the manner in which the two are coordinated that forms the basic problem of cooperation". (Fauquet, 1935).

"Cooperatives are not merely businesses but businesses with a social as well as an economic aim. This concept of economic objectives united to a body of social ideas is in fact one of the pillars of cooperative philosophy". (Laidlaw)

Few U.S. economic theories of agricultural cooperatives emphasize the social side of cooperatives. The California model completely ignores it. Emphasis is mainly on the economic role of the cooperative, and the debates in this country have been in terms of the focus of power within the structure. That is, who makes the ultimate economic decisions within the cooperative system?

Torgerson (7) has written that, "Cooperatives are, in practice and theory, an off-farm extension of the farm firm, an integral part of the farming enterprise that allows farm operators to participate in one or more stages in the marketing channels. An "agency" relationship therefore, exists between the farm firm and the cooperative".

As the California plan has evolved, the cooperative interjects its authority on such traditional farmer decisions as varieties or species, planting and harvest dates, maturity standards, and often, cultural practices that affect quality or market acceptance, including meeting government regulations. Such cooperatives are more than the off-farm extension of the farm firm. In reality, the typical California cooperative is a primary coordinator of production to marketing, and a partner in the members' decision process. In this manner, it is able to assure that the output from the farm and the cooperative are joint-products developed to meet market requirements.

FACTORS AFFECTING CALIFORNIA COOPERATIVES

1. The concept of single product cooperatives is being challenged by structural changes resulting from the acquisition of single-product processing firms by multi-product and multi-national firms. Such firms are able to sell both "families of products" as well as diverse food and non-food items to retail food chains. This increased concentration resulting from recent trends raises questions of future effectiveness of cooperatives as single-product marketers.

This becomes increasingly a serious problem where a cooperative has assumed an industry outlook and the resultant costs associated with

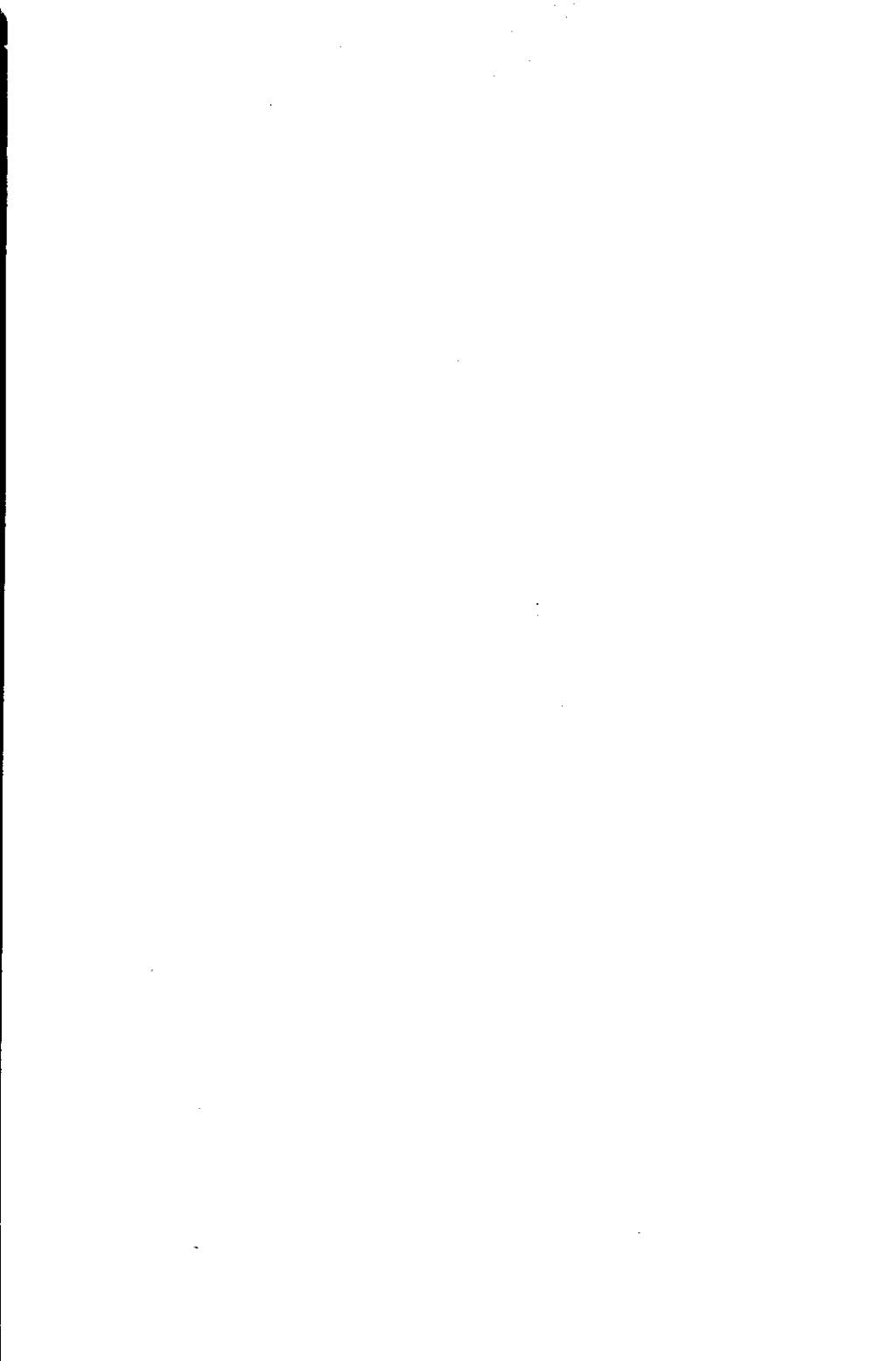
maintaining the industry and its surplus inventories. This practice may prevent the cooperative from being the lowest cost producer, and may affect its ability to make competitive returns to members, thus enhancing the stature of new entrants who do not carry industry burdens and costs.

Cooperatives have often assumed an industry posture in matters of marketing orders, price leadership, generic advertising, in holding industry surpluses, and when management makes public appearances on behalf of industry matters.

2. The entrance of large, multi-product, multi-national firms into processing and marketing may present the need for the organization of new bargaining cooperatives to represent interests of farmers. Traditionally, the operating cooperative has provided an "umbrella" benefit to non-cooperative members who supplied local marketers, without materially affecting the cooperative's competitive position. With the entry of large, often conglomerate firms which lack a local orientation and which impose their own values on grower returns, the role of bargaining cooperatives may take on great importance, even with established processing cooperatives. The Sapiro concept may again come into the forefront as new relationships develop.
3. Changing economic forces that bear on farmers' financial statements are encouraging them to seek ways to reflect current values of the cooperative's assets on farmers' balance sheets, as compared to traditional evidences of financial interests. In some instances, cooperatives have established a system for the sale and purchase of equity positions within the cooperative structure. A few cooperatives have established non-cooperative holding companies to acquire physical assets which are leased and operated by the cooperative. In such cases, the ability to buy/sell/trade equity has tended to reflect current values.
4. The questions of future capital requirements suggest the need to consider hybrid organizations which may have characteristics of private companies with securities trading, but which are cooperatives engaged in the operations and marketing of products. Perhaps joint ventures with food manufacturing firms may help cooperatives gain access to higher margin sectors of the food industry, while retaining a cooperative level at more basic processing functions. Costs of "slotting" charges required to gain access to retail shelf spacing, and changes in distribution network facilities to become competitive may be important factors for consideration of cooperative strategies, and which may make hybrid structures necessary.

REFERENCES

- (1) Garoyan, Leon, "Fruit and Vegetable Industry Pressures for Increased Coordination", NC117 Report, University of Wisconsin, May 1974, p.3.
- (2) Larsen, Grace C. and Henry E. Erdman, "Aaron Sapiro: Genius of Farm Cooperative Promotion", Mississippi Valley Historical Review, September 1962, p. 242-268.
- (3) Steen, Herman, Cooperative Marketing: The Golden Rule in Agriculture, Doubleday, Page and Co., 1923.
- (4) Knapp, Joseph G. and Associates, Great American Cooperators, American Institute of Cooperation, 1967, p. 446-454.
- (5) Knapp, Joseph G., Advance of American Cooperative Enterprise: 1920-1945, The Interstate Press, 1973, p. 9.
- (6) Vitalliano, Peter, "The Competitive Yardstick School of Cooperative Thought: Its Development and Relevance to Contemporary Cooperatives". Processed. Paper presented at the 1980 Graduate Institute of Cooperative Leadership, University of Missouri, Columbia, 1980.
- (7) Torgerson, Randall E., "What is Cooperation: The Philosophy of Cooperation and its Relationship to Cooperative Structure and Operations". Paper presented at the Graduate Institute of Cooperative Leadership, University of Missouri, Columbia, 1980.



ABOUT THE CENTER FOR COOPERATIVES

The Center for Cooperatives was established by the California Legislature in 1987 as a center in support of research, education, and extension activities to advance the body of knowledge concerning cooperatives in general and address the needs of California's agricultural and nonagricultural cooperatives.

The Center's objectives are to promote:

1. **EDUCATION:** The Center offers formal and informal educational programs to those involved in cooperative management and develops teaching materials for all levels of interest.
2. **RESEARCH:** To help the state's cooperatives reach their objectives, research is conducted on economic, social, and technical developments. A practical aspect of this research, the provision of competitive research grants, and studies for government agencies on how cooperatives can help achieve public policy objectives.
3. **OUTREACH:** The Center is prepared to inform the public on cooperatives and their significance to the economy of California.

While the University of California is responsible for its administration, the Center is intended to serve statewide; its teaching and research resources are drawn from interested professionals from all UC campuses, the State University System, other colleges and universities, and sources indigenous to the cooperative business community.

The Center is prepared to receive gifts and contributions from the public, foundations, cooperatives, and other like sources.

THE CENTER FOR COOPERATIVES
UNIVERSITY OF CALIFORNIA
DAVIS, CA 95616