COOPERATIVE PURCHASING OF FARM SUPPLIES IN OREGON - 1938

by

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PREFACE

Farm supplies have been purchased cooperatively in Oregon for over 30 years. This field of cooperative endeavor has become a sizeable business with an annual sales volume of approximately six million dollars.

The rapid development of the supply cooperatives following 1930 has given rise to numerous problems of organization and management. In recognition of the need for basic information concerning the operating methods and financial condition of supply associations, the Cooperative Division of the Farm Credit Administration has made studies of the supply movement in several states. A study of the Oregon farm supply cooperatives for the year of 1933 was carried out by John H. Lister of the Cooperative Division and the bulletin reporting the findings of this investigation was released in August, 1935.

Data contained in the present study were obtained by the writer in a personal canvass of the 62 cooperative units involved. The splendid manner in which the managers, directors, and employees responded to the requests for necessary schedule information is deeply appreciated.

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COOPERATIVE PURCHASING OF FARM SUPPLIES IN OREGON - 1938

Background of Cooperative Purchasing in Oregon

The following few pages are devoted to a brief inquiry into the development of the cooperative purchasing movement among the farm population of Oregon. Attention will be focused upon the physical growth as well as the legal foundation of Oregon cooperatives.

HISTORICAL DEVELOPMENT. Farm supplies were first handled cooperatively in this state during the year of 1908 as a service division of the Eugene Fruit Growers Association of Eugene, an association organized primarily as a marketing cooperative. By 1916 the number of cooperatives doing a supply business had increased to 4; one of which, the Farmers Union Cooperative Warehouse of Dallas, was distinctly a supply cooperative.

Development of the movement was slow until the close of the World War period; but following 1920 there came a noticeable speeding up of the cooperative farm supply business and by 1926 the number of such organizations had increased to 16, half of which were true feed and warehouse cooperatives. The spread of the petroleum cooperative following 1930 brought the most rapid numerical growth of supply associations with 33 organizations of this type being set up between 1930 and 1936. An early venture in the cooperative purchasing of petroleum occurred in Umatilla County in 1919, but it was not until 1930 that any real development was to be noted in this field.

Reference to Table 1 will serve to clarify the above discussion and to show the relative growth of the three divisions of the farm supply cooperatives. At the present time there are 62 cooperatives doing a sizeable supply business and of this number, 21 associations are primarily marketing organizations. The 62 cases studied are divided into 34 petroleum associations, 14 feed and warehouse associations, and 14 unclassified associations. This classification was adopted as indicative of the major lines of supplies handled and does not by any means delimit the field of the respective organizations because there is a great deal of overlapping in kinds of supplies sold.

TERRITORY SERVED. The most rapid development of the cooperative movement came in the diversified and thickly settled Willamette Valley of Western Oregon. With the expansion of the petroleum cooperative, the movement advanced rapidly into Eastern and Southern Oregon. At the present time the only sections of the state without cooperative supply service of some kind are contained in 6 counties, 2 on the Coast and 4 in the sparsely settled range country of Central Oregon.

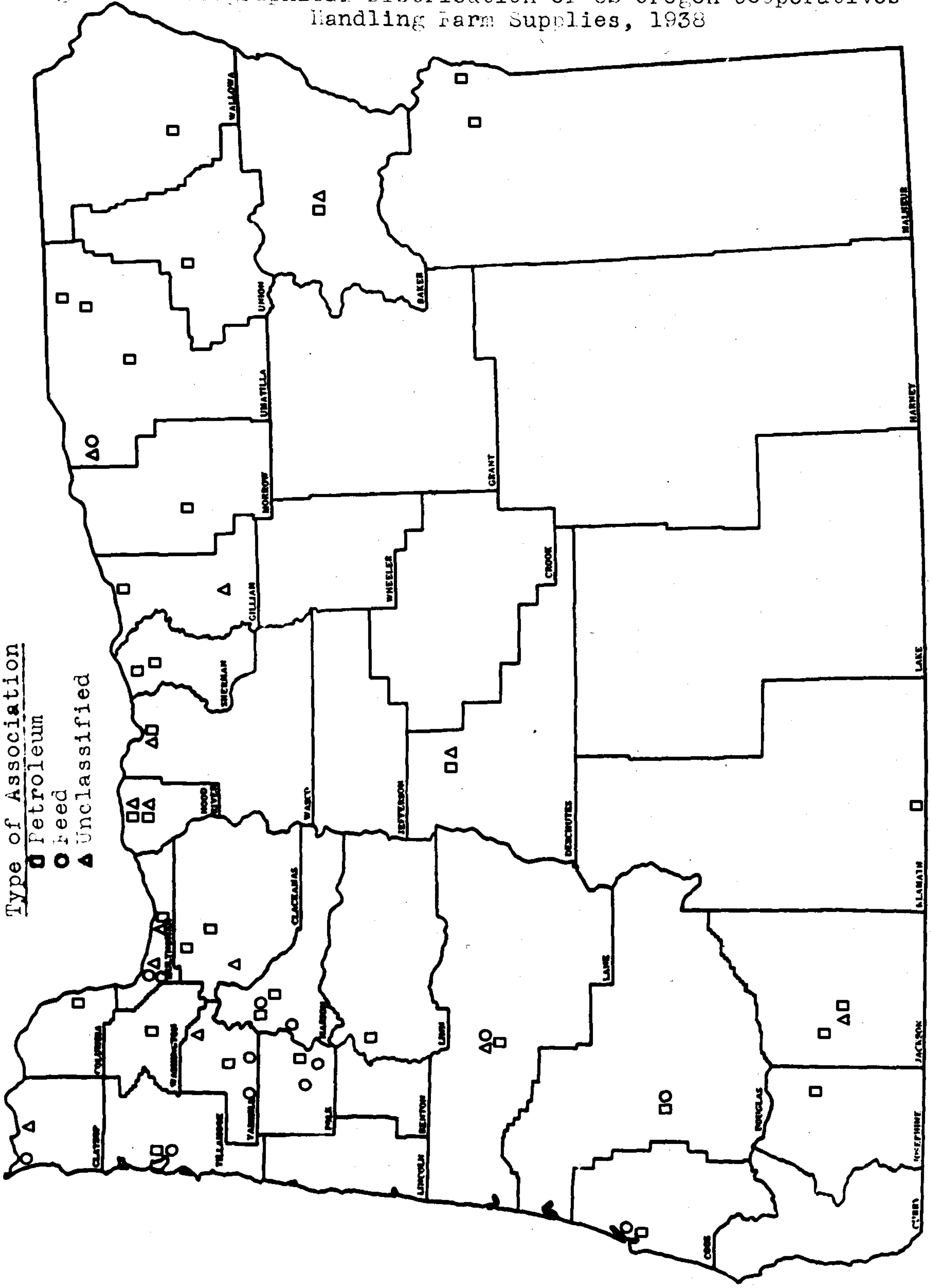
Table 1. Year of Incorporation and Year of Beginning Farm Supply Business for 62 Oregon Cooperatives Handling Farm Supplies, by Type of Association, 1938

Year	Number Organized			Number Beginning Farm Supply Business		
	Petroleum	Feed	Unclassified	Petroleum	Feed	Unclassified
1903....	-	-	1	-	-	-
1904....	-	-	-	-	-	-
1905....	-	-	-	-	-	-
1906....	-	-	-	-	-	-
1907....	-	-	1	-	-	-
1908....	-	1	-	-	-	1
1909....	-	1	-	-	-	-
1910....	-	-	-	-	-	-
1911....	-	-	-	-	-	-
1912....	-	-	-	-	-	1
1913....	-	-	1	-	-	1
1914....	-	-	-	-	-	-
1915....	-	-	-	-	-	-
1916....	-	1	-	-	1	-
1917....	-	-	-	-	-	-
1918....	-	-	-	-	-	-
1919....	-	1	-	-	-	1
1920....	-	1	1	-	-	1
1921....	-	1	2	-	2	-
1922....	-	1	-	-	2	1
1923....	-	1	-	-	1	-
1924....	-	1	-	-	2	1
1925....	-	-	1	-	-	1
1926....	-	-	1	-	-	-
1927....	-	-	-	-	-	-
1928....	-	-	1	-	1	1
1929....	-	1	1	-	-	1
1930....	4	1	3	2	1	2
1931....	2	-	-	1	-	-
1932....	4	1	-	3	1	-
1933....	4	-	-	4	1	1
1934....	10	1	-	12	1	1
1935....	9	-	1	11	-	-
1936....	-	-	-	-	-	-
1937....	1	1	-	-	1	-
1938....	-	-	-	1	-	-
Associations Reporting	34	14	14	34	14	14

Only 3 associations are attempting to operate in territories larger than 3 counties; one of these associations conducting a state-wide business by the mail order method and the remaining 2 operating branches in territories west of the Cascade Mountains. The great majority of supply cooperatives are single county units catering to a strictly local clientele. The map in Figure 1 is a pictorial presentation of the distribution of supply cooperatives in Oregon. From this map it is clear that the supply cooperative is limited to the farming areas of the state and that the territory served forms almost a semi-circle about the range plateau of Central Oregon.

INFLUENCE OF REGIONALS. Two regional wholesale cooperatives, the Oregon Grange Wholesale of Portland and the Pacific Supply Cooperative of Walla Walla, are operating in Oregon at the present time and these two wholesale organizations have 43 affiliates among the 62 associations included in this study. These overhead organizations have confined their efforts principally to the sale of petroleum products, hardware, electrical appliances, farm machinery, auto supplies, and other lines affiliated with these items. It is the function of the regional cooperative to serve as the means of carrying cooperation one step closer to the primary sources of supply through pooling the purchasing power of the affiliated local units.

Figure 1. Geographical Distribution of 62 Oregon Cooperatives Handling Farm Supplies, 1938



The movement which led to the growth of the petroleum associations was already under way when these regionals were organized, but there can be little doubt that the regionals have contributed much to the expansion of cooperative purchasing. The influence of these wholesale groups has taken the form of actual assistance in the organization of new cooperatives; the maintenance of field men who aid the local in sales, accounting, and internal problems; and at times, the extension of credit by the regional has been of material benefit to the local. In addition to these services, the regionals have provided a cooperative source of dependable goods available at a reasonable cost. Regional associations have a great opportunity for bringing about further integration and expansion of the cooperative movement, but the attitude of most local associations is that the overhead organization must not urge the establishment of new cooperatives where conditions do not justify the ventures. These affiliates usually consider the real duty of the wholesale organization to be service to the local without jeopardizing the interests of the member associations through unjustified expansion of either local units or lines of supplies. A number of managers are adopting a broader view in the above respect and are realizing that it is very difficult for the regional to handle only lines which would satisfy all the locals.

LEGAL BACKGROUND OF OREGON COOPERATIVES. Since 1909 the state of Oregon has provided for the organization of non-profit cooperative associations under a division of the state corporation laws, but most of the cooperatives now doing business in this state are organized under the amended 1915 code. This law provides for all types of cooperatives and does not refer to agricultural cooperatives exclusively. Five or more persons may join together to form a cooperative and after conforming with the law in respect to the filing and content of articles of association and by-laws and the payment of annual license fees, the cooperative association may conduct business in much the same manner as any general corporation. However, the cooperative law limits dividends on stock to 8 per cent per annum and provides for the manner of distributing earnings on the basis of patronage. The use of the name "cooperative" is limited to associations organized under the provisions of the cooperative statute and protection for association members is provided by the section of the law which makes mandatory upon the association the issuance of an annual accounting of individual interest to any member upon request. This accounting is a statement of the interest of the member in the net worth of the organization but the law does not provide that the member may withdraw this equity upon demand. In general, the cooperative statute has proved satisfactory and of the 62 associations studied, only 2 associations remain under the general corporation law. Eleven of the 62 co-operatives have been reorganized one or more times and of the 11 so reorganized, the primary reason in 10 cases was to bring the group into compliance with the cooperative law in technical construction as well as in substance.

Method of Operation

The relative efficiency of a cooperative unit must depend to a considerable extent upon the methods employed in conducting the operations of that organization. These in turn may often be traced in varying degrees to the cooperative business philosophy of the membership, directors and personnel. In some cases these ideas of operation are not based upon past experience in similar lines of business, but seemingly follow the principle that a cooperative need not be bound by the common rules of organization and management. Those few associations in which the membership believes that the organization should be able to operate for less, sell for less, and always pay dividends have found all the problems relating to financing, management, and membership relations increasingly difficult. The most successful cooperative units are employing essentially the same methods of business operation as have been used in similar private business units.

SUPPLIES HANDLED. As an introduction to the discussion of operating methods, we must investigate the variety and types of supplies handled by these associations. Table 2 indicates the frequency with which the various supplies were handled by the 62 reporting cooperatives. Petroleum products and auto supplies lead all lines, primarily because of their frequency in the petroleum group. Hardware is the third item in the listing and is handled by almost two-thirds of the petroleum units and one-half of the feed and unclassified associations. Ranking below hardware in order,

Table 2. Frequency with which Certain Products are Handled by 62 Oregon Cooperatives Handling Farm Supplies, by type of Association, 1938

Products	All	Type of Association		
		Petroleum	Feed	Unclassified
Petroleum................	44	34	3	7
Feed......................	33	13	14	6
Seed......................	29	11	12	6
Fertilizer...............	32	13	12	7
Auto Supplies............	43	34	3	6
Machinery................	32	20	7	5
Hardware.................	35	22	7	6
Groceries and Dry Goods..	9	2	3	4
Orchard Supplies.........	19	6	6	7
Harvest Supplies.........	7	5	-	2
Dairy Supplies...........	23	6	12	5
Poultry Supplies.........	20	5	11	4
Electrical Appliances....	25	19	2	4
Building Material........	9	4	3	2
Fuel.....................	3	2	1	-
Insurance................	4	3	-	1
Hop Supplies.............	1	-	1	-
Bee Supplies.............	1	-	-	1
Wool Supplies............	1	-	-	1

and occupying the next four places, are feed, fertilizer, machinery, and seed. The real significance of this tabulation lies in the indication of the widening fields of the various cooperatives. For example, the petroleum associations starting after 1930 as the so-called "gas co-ops" handled few items outside the lines of petroleum products and auto supplies; but with the decreasing margin in these goods coupled with the desire for greater sales volume, it has been necessary to branch into new lines. These new lines have most frequently included hardware, electrical appliances and machinery. These last mentioned lines have been classed as "high margin" goods and the cooperative has found that it can return a real saving to the member when he buys such merchandise. There is a tendency among the petroleum units to add feed, seed and fertilizer in order to provide a more complete service. The same trend is found in the feed and unclassified divisions but is less pronounced than in the petroleum group.

Only 9 associations are carrying groceries and dry goods, and several of these are not at all enthusiastic over the prospects in this field. The associations not carrying such consumer goods are practically unanimous in the opinion that these goods have no place in a farm supply cooperative. Reasons advanced for this view were based upon the low margins prevailing, relative efficiency of present private agencies, inadequate cooperative personnel and the possibility of additional credit problems. The farm machinery business is being developed rapidly by Oregon farm supply cooperatives and already a number of these organizations hold the local franchise from "old line" machinery manufacturers. It appears that the supply cooperative has an excellent opportunity of developing into a well rounded business unit providing broad service and substantial savings for the membership. The one real danger of expansion into too many lines of goods lies in the difficulty of providing adequate service at low cost where the volume of sales in each line is not large.

SOURCES OF SUPPLY. Thirty petroleum associations reported purchase of 85.8 per cent of their supplies from the regional wholesale organizations to which they belong. A large percentage should be expected here because all petroleum products supplied the local units are purchased through the contract of the regionals with the oil companies. This figure of practically 86 per cent indicates the important position held by the wholesale organizations in the development of a cooperative source of supplies for petroleum cooperatives. Table 3 readily shows the lack

Table 3. Sources of Supply of 56 Oregon Cooperatives Handling Farm Supplies, by Type of Association, 1938

Source of Supply	All	Petroleum	Feed	Unclassified
	Per cent	Per cent	Per cent	Per cent
Regional Cooperatives.	48.7	85.8	1.7	9.6
Manufacturers.........	25.5	7.0	40.3	52.5
Jobbers...............	21.8	6.4	41.9	37.9
Local Producers.......	4.0	.8	16.1	none

of any regional organization to serve the feed and unclassified associations. Feed cooperatives, where most of the operation is of a manufacturing nature, purchase most of their grains and concentrates directly from jobbers and manufacturers, with about 16 per cent of their supplies coming directly from the local producers. The unclassified units handle many specialty lines and purchase 52.5 per cent of their supplies from the manufacturers. Several of the unclassified group are members of the regionals, as is evidenced by the purchase of about 10 per cent of their supplies from that source.

There may be a gradual increase in regional purchases among the feed and unclassified units as the wholesale cooperatives add lines handled by the locals, or vice versa, but the bulk of the purchases in these divisions will probably continue to be made from jobbers and manufacturers. This condition is probable; partly because of the nature of the products purchased, but mostly because there is no concerted effort among these associations pointing in the direction of collective buying. It appears that several of the feed associations might profitably pool their orders for concentrates, and that certain unclassified associations might act together in ordering fertilizers and spray; but, thus far, no group has taken the initiative in this direction.

PRICING POLICY. Contrary to popular belief, the majority of supply cooperatives are not making a practice of cutting prices below the prevailing competitive levels. In 39 of the 61 associations reported in Table 4, the pricing policy is listed as maintenance of the local competitive price level on similar merchandise. The "cost plus" plan of pricing is used most frequently by the feed associations where the bulk of the products handled are manufactured by the same organization. Several feed cooperatives reported that they practically set the price in their territories, and the logical method of pricing is cost of manufacturing plus a reasonable margin to

Table 4. Pricing Policy of 61 Oregon Cooperatives Handling Farm Supplies, by Type of Association, 1938

Basis of Price	All	Petroleum	Feed	Unclassified
Competition	39	22	6	11
Combination of Competition and Cost Plus..........	6	5	-	1
Cost Plus.....................	8	-	7	1
Combination of Competition and Below Competition.	5	5	-	-
Below Competition...............	3	1	1	1
Associations Reporting.......	61	33	14	14

cover operating costs and additions to reserves. Only 3 units deliberately set their prices below competition and at least one of these is trying to work back to the competitive level. The combination policy is used most extensively in the petroleum division where the retail price of such lines as petroleum products and machinery are set by the manufacturer. These units stay with the established prices where necessary, but do sell several of the "high margin" lines below competition.

The strong preference for maintaining the competitive price is based upon the belief that better local relations result and that this system is a fundamental of sound business operation. Most associations do not desire to stir up bad feelings among local businessmen and believe that cutthroat competition benefits no person or organization. Pricing in such a manner that the cooperative may build a reasonable working capital reserve and pay moderate dividends has proved good business procedure. The earnings accumulated serve as a buffer in case of unforseen circumstances and the dividends are generally considered a sign of health, as well as a very effective advertisement of cooperative benefits. One manager states that his only advertisement is regular dividends and to pay such dividends, there must be a fair margin on all sales. As a group, these supply cooperatives are working out their pricing plans in a very satisfactory manner and little difficulty is being experienced with this phase of operation.

SALES METHODS. The average supply cooperative has been reluctant to adopt the sales promotional methods employed by private business concerns. There is a considerable element among cooperators which believes that this type of organization should not find it necessary to advertise or actively seek out prospective customers. This view has considerable merit because there are many members who always think of their association first, and to them advertising appears to be an unnecessary expense. Some local advertising has proved of material benefit to certain associations, particularly after the association has assumed its place among the going business establishments of the community. This advertising and sales promotion has not assumed large proportions, but has been helpful in keeping the services of the cooperative before the community at large.

The most frequently used sales method of 61 associations reporting (Table 5) is solicitation by the manager and this means is employed most extensively in the petroleum group. The petroleum associations likewise use solicitation by directors and through farm organization meetings more frequently than either of the other two divisions. Advertising in local papers was reported in

Table 5. Sales Methods Used by 61 Oregon Cooperatives Handling Farm Supplies, by Type of Association, 1938

Method	All	Petro-leum	Feed	Unclassi-fied
Solicitation by Manager....	33	26	5	2
Solicitation by Directors..	13	11	1	1
Local Advertising..........	28	11	8	9
Farm Organizations.........	15	11	2	2
Truck Drivers..............	11	9	1	1
Field Man..................	8	3	1	4
None.......................	9	1	3	5

28 cases and provided the most important single sales method of both feed and unclassified associations. Truck drivers serve as salesmen in 9 petroleum units and this combination of duties appears to function well in such organizations. The truck drivers are acting as salesmen in only one each of feed and unclassified associations. One reason for this difference lies in the fact that most petroleum cooperatives provide regular delivery service, whereas the other two divisions provide such service in only a few scattering cases. Nine associations report that they do not solicit any business and this policy is most prevalent in the service departments of marketing organizations. In many of these marketing cooperatives, no emphasis is placed upon the development of the supply department, as such. Field men are employed by 8 associations and are usually an effective means of solicitation,

but such specialized help cannot be employed by the smaller units. In these latter units, the work of a field man must be performed by the manager and deliverymen as a part of their regular duties.

From the above discussion, it appears that the average supply cooperative has not found it necessary or advisable to spend large sums of money in seeking and retaining patronage. However, most associations report that they find a profitable investment in a nominal amount of strictly local advertising; whether in newspapers, through a news letter, or by other means. This type of advertising is not expensive and does serve to keep the name and products of the cooperative before the entire farm population in the district. Some publicity usually aids in creating a desire to be associated with the movement involved, and in line with this idea, several managers expressed the view that all Oregon supply cooperatives may well combine in a common effort to publicize the farm supply association. Such action would take the form of institutional advertising, which would emphasize the benefits of cooperative action and the place of the farm supply cooperative in agricultural production, as contrasted to the ordinary advertising of specific products offered for sale.

CREDIT POLICY. The most perplexing problem in the operation of most business is the matter of credit and cooperative organizations have experienced their share of difficulty in this line. Managers and directors report that credit in its various angles has led to many trying situations; so many, in fact, that the present tendency is toward strict 30-day credit wherever cash is not demanded at the time of purchase. Of the 61 reporting associations listed in Table 6, no special limitations on the credit privilege is the practice of 35 organizations although 5 of this number grant a discount for cash. In these cases the manager is charged with the task of granting

Table 6. Credit Policy of 61 Oregon Cooperatives Handling Farm Supplies, by Type of Association, 1938

Credit Plan	All	Petroleum	Feed	Unclassified
Cash, no Credit................	10	6	3	1
Very Limited Credit............	6	4	1	1
No Special Limitations.........	30	13	7	10
No Special Limitations, but Manager Responsible..........	6*	5*	-	1
Credit to Amount of Investment.	2	1	1	-
No Special Limitations, but Discount for Cash............	5	2	2	1
Limit Set by Directors.........	2	2	-	-
Associations Reporting.......	61	33	14	14

* Two managers in this group are on a cash basis.

and supervising the credit, but is not financially responsible for losses which may result. Twelve cooperatives report operation on a strictly cash basis and 8 other units are operating with very limited credit. The manager is personally responsible for all credit granted in 6 organizations, and although this responsibility may cause the manager to be more cautious, it is of doubtful value in case any large losses occur. Two of these 6 managers are operating on a cash basis and are taking this means of avoiding any possible losses from bad accounts. The association directors are assuming the direct control of credit extension in only 2 cases, both petroleum units. This method shifts some of the responsibility from the manager and may be a good system if the directors are well posted on the financial status of the membership. Only 2 associations are attempting to limit credit to the amount of a member's equity in the net worth of the business. This method has proved an effective means of avoiding bad debt losses because of the limitation upon the amount of credit granted and the provision for cancellation of equities to cover the unpaid balances. The above plan of credit control is used most easily where the association issues certificates of equity or indebtedness and such certificates may be deposited to secure the accounts.

Petroleum associations have most effectively controlled their credit problems according to the compilation of credit periods in Table 7. This group reports that 86.3 per cent of its accounts are on a current basis and that only .6 per cent of the credit is carried over a year. In contrast, we note the record of the feed and unclassified groups where only about 50 per cent of the accounts are of the current 30-day type and from 2.5 per cent to 4.1 per cent of the credit runs over a year. This longer credit period is primarily the result of the supply

Table 7. Length of Credit Period Reported by 52 Oregon Cooperatives Handling Farm Supplies, by Type of Association, 1938

Credit Period	All	Petroleum	Feed	Unclassified
	Per cent	Per cent	Per cent	Per cent
30 days or less....	69.3	86.3	55.0	47.1
Over 30 days........	30.7	13.7	45.0	52.9
Over 1 year.........	1.9	.6	2.5	4.1

activities of several marketing organizations which furnish the members with supplies throughout the season and collect for these advances only upon settlement for products marketed. The credit problem of these marketing units will be given further attention in the section dealing with the marketing-purchasing combination.

The most serious credit problems are to be found in those cooperatives where the credit policy has been loose over a period of time and the need for tightening of terms is now being realized. Managers find decided opposition to their efforts in the direction of credit limitation, but are finding it necessary to proceed in spite of losing a few patrons in the process. Bad debts in a cooperative supply organization dealing almost entirely with its own membership are difficult to justify because, in effect, such losses penalize the member who pays for his goods. While some credit is undoubtedly necessary in most associations, it must be limited in amount and duration and must be judiciously granted if losses are to be avoided. The successful operation of those cooperatives selling only for cash or on definite security refutes the argument that open credit is an absolute necessity in all modern business, and the experience of these groups may well serve as an example toward which others might point.

DIVIDEND AND RESERVE POLICY. The dividend and reserve policy of a cooperative association is an important element in membership relations, as well as an indicator of operating efficiency and financial soundness. In the discussion of this subject, treatment of the material is simplified through separating the two elements, dividends and reserves.

The basis upon which dividends are declared varies considerably, but the "percentage of gross purchases" method is most widely used among Oregon cooperatives. This system has the advantage of simplicity and is the means of determining the amount of dividends in 23 of the 60 associations reported in Table 8. Nine units have refined the gross purchases base into determination according to purchases in the various departments. The latter plan is obviously more equitable since it allows for the varying rates of profit on different classes of goods. The dividend based upon a percentage of gross

Table 8. Basis of Dividend Declaration in 60 Oregon Cooperatives Handling Farm Supplies, by Type of Association, 1938

Dividend Base	All	Petroleum	Feed	Unclassified
Percentage of Gross Purchases....................	23	10	9	4
Percentage of Purchases According to Department..	9	5	1	3
Flat Rate per Unit of Purchase................	8	6	-	2
Percentage of Markup on Purchases................	8	8	-	-
Combination of Gross Purchases and Flat Rate.....	2	1	1	-
Combination of Dep't Purchases and Flat Rate.....	3	3	-	-
None on Supply Department..	7	-	3	4
Associations Reporting...	60	33	14	13

markup appears most fair but involves extensive bookkeeping, since the markup on every item purchased must be recorded in the member's account. In spite of the detailed work involved, 8 petroleum associations are now making use of this dividend base. Similar to the "percentage of purchases according to department" is the flat rate per unit of purchase, which allows for varying rates of profit and is easily computed on such supplies as gas and oil. Eight associations use this flat rate method exclusively and 5 other groups are using this plan combined with the percentage of gross purchases or percentage of departmental purchases. Seven marketing cooperatives do not pay any dividends on the purchases made through the supply department. Any earnings accruing from the supply business are thrown into the reserves of the association and often serve to increase the return on the products marketed. Several of these marketing cooperatives are planning to separate the supply department from the marketing operation, and, as a separate accounting unit, it will pay its own way and dividends on supply purchases will become policy.

Of the 56 associations reporting the frequency of dividend declarations, 36 organizations are on an annual basis which seems to have proved most satisfactory from the accounting angle. Eight units pay dividends semiannually, 2 associations pay quarterly and 4 groups pay monthly. All but one of these last 14 associations are petroleum organizations in which the dividend computation is comparatively easier than in the feed and unclassified divisions. This computation is usually easier in the petroleum association because of the relative ease of taking inventory at frequent intervals and the use of the flat rate per unit method of dividend payment. Although this flat rate dividend may be continued from one period to the next without alteration, any dividend period of less than a year greatly increases the office work of the association. Six cooperatives are using a combination of the above dividend periods because they have found it desirable to set different times of payment on the sales of the various departments. The wide preference for the annual dividend is logical because such a dividend may be declared after examination of the annual financial reports and computation is held to a minimum, usually being performed during the slack season from January to March.

Cash is the most frequent method of dividend payment and is used by 28 of the 53 associations reporting in Table 9. The cash plan is probably the most effective practice from the standpoint of the patron and can be used by those associations with adequate reserves and capital. In addition to the necessity of adequate financial backing, the association attempting to pay a cash dividend must be in a good current position at the time of dividend payment. A few associations have weakened themselves materially by paying a cash dividend which practically destroyed their current cash position at the time.

The certificate of indebtedness or dividend certificate under a number of different names, usually bearing from 3 per cent to 5 per cent interest, is used by 12 organizations for the purpose of building a working capital revolving fund. Most of these latter associations plan to revolve these certificates in a maximum of five years. This type of revolving fund is, practically speaking, a member loan to the business bearing a nominal rate of interest, ordinarily non-transferable and without definite maturity. Stock dividends are issued by 5 units and a book credit is the practice of 4 associations. The stock dividend is not widely used and several managers report considerable member resistance to this type of dividend. The book credit is the same as cash to the member since it serves to reduce his account or may be used to purchase goods. One manager of an organization using the book credit dividend reports that the plan has a tendency to slow up payment on accounts receivable, because a member tends to let payment "slide" when he believes a dividend will be declared to reduce the account. Partial cash dividends are paid by 4 associations who pay the balance in stock or certificate of indebtedness.

The tendency in the payment of dividends is toward the cash dividend, payable annually and based upon departmental purchases. This method is coming to be considered most effective from the standpoint of both member and association, and its use is being contemplated by a number of organizations now operating under other plans.

Table 9. Methods of Dividend Payment in 53 Oregon Cooperatives Handling Farm Supplies, by Type of Association, 1938

Form of Payment	All	Petroleum	Feed	Unclassified
Cash	28	17	3	8
Certificate of Indebtedness	12	7	5	-
Stock	5	2	3	-
Book Credit	4	2	-	2
Combination of Cash and Certificate	3	2	1	-
Combination of Cash and Stock	1	1	-	-
Associations Reporting	53	31	12	10

RESERVE POLICY. The reserve policy of a cooperative is closely related to its dividend policy, since the method and time of dividend payment have a bearing upon the need for working capital reserves. Most associations make use of the valuation reserves, such as depreciation and bad debts, as a matter of regular procedure and additions to these reserves are treated as expenses of operation. It is when we consider the working capital reserves that the wide range of practice as between associations comes into view. Of the 60 reporting units, 35 groups state that some consistent plan is followed in regard to maintaining or building the association reserves. Approximately 50 per cent of the petroleum and unclassified cooperatives report the use of a consistent reserve plan, and about 65 per cent of the feed division are following a regular system. Of course, the consistent plan differs a great deal as between associations of the three major divisions, and even among organizations of the same general classification. A number of the regional affiliates are making a practice of retaining the wholesale dividend as the regular addition to the reserve. Where either the certificate of indebtedness or the stock methods of dividend payment are in use, the usual practice is to declare the bulk of the earnings in dividends since this amount is retained in the revolving fund or stock retirement reserve until the association sees fit to start the turnover. Where the cash or book credit dividend is used, the usual hold-back of earnings is about 10 per cent, but has approached 100 per cent in several cases during the early development and expansion period.

In order to comply with the cooperative laws of Oregon, any association retaining all or part of its earnings without declaration as dividends should maintain an accurate record of patron equities in such reserves. The declaring of all earnings as dividends, in any desired form, precludes the need for such records; because it is to be assumed that the dividends are based upon patronage and have equitably divided all available savings. Only 8 of 59 associations report the maintenance of such a ledger in which the reserve equities of all patrons are recorded.

The 25 cooperatives reporting no consistent reserve plan are doing whatever appears to be advisable or necessary at the close of the accounting period. The most apparent advantage of a definite plan in this respect lies in the assurance to the patrons that dividends will not vary greatly under similar conditions. Further, the association management and directors can plan for working funds in view of the reserve policy. The establishment of a definite reserve plan is much easier of accomplishment after an association has operated over a period of several years and has established itself financially. The majority of the older cooperatives of the group included in this survey are now following a planned and consistent policy in regard to their operating capital reserves.

Membership and Directors

No single section of this study evoked more interest among the associations concerned than did the questions of membership and membership relations. Managers and directors alike are deeply concerned over the problem of maintaining the interest of members in their associations. This question of membership is of primary importance to every manager, and constitutes one of the most pressing and ever-present problems of cooperative management. The management is concerned not only with making the member feel ownership, but also must give attention to the growth of membership and to the most effective division of responsibility as between directors and employed personnel.

MEMBERSHIP AND PATRONAGE. The total reported membership of the 62 associations studied was 31,411, or an average of 507 members per organization. It appears that these 62 cooperatives serve practically 50 per cent of the farm units in their territories. The problem of membership interest is very apparent when the percentage of inactive membership is considered. This percentage of inactive members is over 20 per cent in all three divisions, varying from 23.6 per cent in the feed group to 21.3 per cent in the petroleum group with the average falling at 22.4 per cent. Most of the persons interviewed expressed the opinion that some means of either bringing these dormant members back into active participation or clearing the organization of such "dead timber" should be devised. This body of inactive members is of little, if any, value to the association.

Non-member business served to bring the total active patronage to 30,014, an average of 484 patrons per unit, and these non-member patrons form a primary source of new members. Feed cooperatives show the largest percentage of non-member business with an average of 29.9 per cent as compared to 8.7 per cent for petroleum and unclassified associations and 18.8 per cent for all associations. The

Table 10. Membership and Patronage of 62 Oregon Cooperatives Handling Farm Supplies, by Type of Association, 1938

	All	Petroleum	Feed	Unclassified
Total Reported Membership..	31,411	10,631	13,108	7,672
Active Membership Reported.	24,381	8,364	10,019	5,998
Percentage Active Members..	77.6	78.7	76.4	78.2
Average Membership.........	507	313	936	548
Total Patronage Reported...	30,014	9,159	14,284	6,571
Percentage Member Patronage	81.2	91.3	70.1	91.3
Average Patronage..........	484	269	1,020	469

average patronage and average membership per unit are tabulated in Table 10, and it is interesting to note that non-member business serves to more than compensate for the inactive membership of the feed cooperatives. Petroleum associations have the smallest average membership and feed associations the largest, the range being from 313 to 936 with the general average standing at 507.

MEMBERSHIP SOLICITATION. The solicitation of new members rests in the hands of association employees in 19 of 60 cases as reported in Table 11. No solicitation

Table 11. Membership Solicitation in 60 Oregon Cooperatives Handling Farm Supplies, by Type of Association, 1938

Method of Solicitation	All	Petroleum	Feed	Unclassified
Employees...............	19	11	5	3
Employees and Members..	10	6	1	3
Members or Directors...	10	7	2	1
Truck Drivers..........	2	2	-	-
Field Men..............	5	1	1	3
None...................	14	5	5	4
Associations Reporting..........	60	32	14	14

of any kind is the policy of 14 cooperatives and it appears that the petroleum group is most active in campaigning for membership. In the petroleum division members aided solicitation in 13 of 32 cases reported. A number of managers stated they were charged with the responsibility of seeking members but had little time away from the plant in which to do this work. From the evidence presented, it appears that the association members could do much more than at present in the obtaining of new members, particularly by working through their farm clubs and organizations. Field men provide an effective means of solicitation but are available only to the larger cooperatives. A good man in the delivery service of an organization has a fine opportunity to combine solicitation with his regular duties and a few units are using this method to advantage.

MAINTENANCE OF MEMBERSHIP INTEREST. The task of retaining the interest of a cooperator in his organization after a few years of operation is not so simple as might be assumed. Many cooperatives have been organized because the farmers felt they were not receiving a square deal from existing agencies. Too often the member has lost much of his fervor as soon as the real or fancied injustice has been corrected, and when the organization settles down to ordinary every-day business there does not seem to him to be much advantage in membership. In several cases, managers reported that their membership problems could be traced back to pre-organization days when some "high-powered" orator had promised the people too much benefit from cooperation.

So long as the business is running smoothly and everyone is satisfied, it is very difficult to arouse interest in the affairs of the cooperative. Six associations are using dinners, picnics, or shows once or twice a year in an effort to maintain interest. A few associations use a plan of holding monthly unit meetings in the various localities which they serve. One cooperative has had fine success with the dinner idea and in recognition of the fact that the average member hesitates to express himself before a crowd, the manager and directors prepare a set of pertinent questions concerning the management and policy of the organization and each member indicates his attitude on the mimeographed form at the time of the dinner. The response to these questions has been very good and a similar plan might be used successfully by other groups who find it difficult to get a membership opinion. News letters have been issued more or less regularly by 24 associations and are reported to be one of the best mediums of acquainting the member with the operation of his cooperative. These news letters carry some advertising of association products, discussion of farming conditions and problems, and items of a local nature which are of interest to the membership. Farm organizations are used most extensively as a means of furthering the cause of the cooperatives in the case of the petroleum group where 13 associations reported material benefit in membership relations through farm organization meetings. Three feed associations are closely affiliated with farm organizations, and one miscellaneous association reported the use of this method of furthering membership relations.

Another method of acquainting the member with his association is the "associate director" plan used by several Eastern Oregon cooperatives. The essence of this plan is the election for one-year terms of associate, non-voting directors in the same number as regular directors with no re-election for these associate directors. In this way it is hoped that over a period of years a fair percentage of members may have come into close contact with the actual operation of the business. These associate directors attend all regular board meetings and, while they do not vote, they do see how the organization is operated. The only difficulty discovered in the plan lies in the keeping of any confidential information by such a large group of persons. This difficulty may be avoided through the use of a special meeting attended only by the regular board when matters which should not be made public are to be discussed.

ASSOCIATION DIRECTORS. The number of directors serving 61 reporting associations varied from 5 to 17; but the most popular sizes are 5 and 7, which are used by 33 and 16 organizations respectively. There seems to be little reason or need for a board of over 7 members in a local cooperative because the larger board is usually more unwieldy and slower to take action. A larger board should delegate most of its authority to an executive committee composed of a small number of directors in order that this committee may be easily assembled and its members made more fully conversant with association affairs. In 46 of the 61 associations, directors' meetings are held monthly, and the frequency of meetings in the remaining 15 organizations ranges from weekly to annually with 7 units reporting meetings "on call." The monthly meeting has met with greatest favor because it allows for an examination of the current financial position at the close of the regular accounting periods.

The term of office for directors in 16 of 61 reporting associations is one year, although the tendency is toward elimination of the one year term wherever possible in favor of a two year period which is the maximum prescribed by the Cooperative Code of Oregon. This trend is the result of unfavorable experience resulting from the complete turnover of directors at one time. It is customary to offset the terms of directors where the period is two years, and in this way only a part of the board is subject to change at any one election. Managers are almost unanimously agreed that the longer terms are preferable because of the possibility that the existence of an entirely new board at one time may upset the operating policy of the business.

Directors received no remuneration in 28 of 60 units as indicated by the tabulation in Table 12. The directors of petroleum associations were remunerated least frequently with about 60 per cent serving without charge to

Table 12. Remuneration of Directors of 60 Oregon Cooperatives Handling Farm Supplies, by Type of Association, 1938

Type of Remuneration	All	Petroleum	Feed	Unclassified
None..................	28	19	4	5
Per Diem...............	14	6	3	5
Per Diem plus Mileage..	12	4	5	3
Mileage................	6	4	2	-
Associations Reporting..........	60	33	14	13

the association. Per diem and per diem plus mileage were the most popular methods of payment and were reported in 26 cases. The per diem rate was usually less than $5.00 and the mileage allowed averaged about 5 cents per mile traveled. There is considerable division of thought in the matter of giving directors a nominal allowance for services rendered, but the tendency seems to be toward some remuneration for their time and expense. This tendency has probably been stimulated by the practice of production credit associations, agricultural conservation associations, and other similar agencies which allow their directors per diem plus mileage. However, there are many cooperators who feel that the member elected to the board should be interested enough in his organization to devote his time without compensation.

Cooperative directors have, in general, left the actual conduct of the business to the manager and have, in some cases, probably passed even policy determination to the employed personnel. For best results over a period of time, the board of directors and the membership should constitute an effective policy-determining body which outlines the boundaries and direction of the business. The handing of full control to the personnel is often the line of least resistance for a cooperative, but the result is sometimes unfortunate when the person or persons so charged with full responsibility must leave the organization.

Management and Personnel

One of the principal criticisms of cooperative endeavor, as brought to light in many studies, has been the lack of effective and efficient personnel. In any study of cooperatives some attention should be devoted to the conditions of employment surrounding association managers and other employees if we are to draw any conclusions regarding the effectiveness of cooperative personnel. In this category we may well look into such things as previous experience of managers, their remuneration and tenure, as well as the rate of remuneration for other employees and general conditions of employment.

PREVIOUS EXPERIENCE OF MANAGERS. Of the 59 associations reporting on this question, 32 stated that their managers had come to the cooperative with previous business experience. This percentage is over half, and indicates that some preference is being given the applicant with business training. Seven of the 59 reported a combination of business and farming, and 13 managers reported only farming experience. Seven association managers have had neither farming nor business experience. The largest percentage of business-trained men is to be found in the feed and unclassified divisions where the size of the business unit is usually larger and the rate

Table 13. Previous Experience of Managers of 59 Oregon Cooperatives Handling Farm Supplies, by Type of Association, 1938

Type of Experience	All	Petroleum	Feed	Unclassified
Farming................	13	10	1	2
Business...............	32	14	9	9
Other..................	7	5	1	1
Farming and Business...	7	5	1	1
Associations Reporting..........	59	34	12	13

of remuneration generally higher. The petroleum cooperatives have a larger percentage of managers with farming experience and with the farming and business combination. This fact may probably be explained in part by the close affiliation of many petroleum associations with farm organizations which have acted as sponsors of the cooperatives.

REMUNERATION OF MANAGERS. The average rate of remuneration for cooperative managers has been comparatively low throughout the history of such organizations. This general view is substantiated to a considerable extent by the tabulation of managerial salaries in Table 14. Ten associations reported the use of a commission plan for their managers and 5 organizations used a combination guarantee and commission. Most managers are not favorable to a straight commission plan because of the difficulty encountered during the slack months. The combination of

Table 14. Remuneration of Managers of 59 Oregon Cooperatives Handling Farm Supplies, by Type of Association, 1938

Amount of Remuneration	All	Petroleum	Feed	Unclassified
Commission..................	10	8	-	2
Guarantee and Commission...	5	3	1	1
Less than $50.00 per mo....	1	1	-	-
$50.00 to $75.00...........	2	2	-	-
$75.00 to $100.00..........	12	8	3	1
$100.00 to $125.00.........	7	4	-	3
$125.00 to $150.00.........	4	2	2	-
$150.00 to $175.00.........	3	1	-	2
$175.00 to $200.00.........	5	1	3	1
$200.00 to $225.00.........	2	-	1	1
$225.00 to $250.00.........	3	-	3	-
Over $250.00 per mo........	5	2	1	2
Associations Reporting...	59	32	14	13

guarantee and commission meets with greater favor because it does provide at least a living wage throughout the dull season. As will be noted, the commission plan is used most extensively in the petroleum associations where gross volume is relatively smaller and the seasonal fluctuations of volume more severe. Of the remaining 44 associations operating on a salary basis, 22 paid their managers less than $126.00 per month and 15 paid $100.00 or less. The lowest salary scale prevailed in the petroleum associations and the highest salaries were usually found in combination marketing-purchasing organizations where the manager's duties are of a more distinctly executive type. There are undoubtedly many managers who are doing a much better job than their salaries would indicate and are deserving of increased remuneration.

Few associations can expect to hold a good manager at a rate of less than $100.00 per month and too often the efficient operator leaves the cooperative for more lucrative employment elsewhere. A number of associations are one-man affairs where the manager is the sole employee and is expected to maintain the plant, to handle sales and deliveries, and to keep the books. Several of these cooperatives are offering a deliveryman's salary and hoping they may be able to get a salesman and manager thrown into the deal. It would appear that the only method of reducing the turnover of managers in the lower brackets is to increase the volume of business enough to justify the employment of a qualified man and to provide him with part-time help, either in the office or in the field. While it is very easy to confuse cause and effect when considering managerial efficiency and rate of remuneration, there is probably a minimum wage below which good management cannot be maintained over a period of time. Data accumulated during this study would place this minimum at $125.00 per month for an association of average volume.

TENURE OF MANAGERS. The discussion of tenure ties in very closely with the matter of remuneration since length of tenure is at least partially determined by the prevailing salary. In 17 of the 59 cases reported, managers had been in their present capacities less than 2 years. Managers of feed and unclassified cooperatives have both longer average tenure and greater average remuneration. Shorter tenure is to be expected of the petroleum group because these associations have all been organized since 1930, but it appears that some of the reason for the rapid turnover of managers, as indicated in Table 15, must lie in the extremely low salaries

Table 15. Tenure of Managers of 59 Oregon Cooperatives Handling Farm Supplies, by Type of Association, 1938

Length of Service	All	Petroleum	Feed	Unclassified
Under 6 months.........	8	8	-	-
6 months to 1 year....	3	2	1	-
1 year to 2 years.....	6	4	2	-
2 years to 3 years....	5	2	1	2
3 years to 4 years....	12	8	1	3
4 years to 5 years....	7	5	1	1
5 years to 10 years...	12	5	1	6
Over 10 years.........	6	-	5	1
Associations Reporting.........	59	34	12	13

ranging from \$50.00 to \$100.00 per month. Most of the marketing associations with supply departments fall in the feed and unclassified divisions and their longer average tenure of managers aided materially in improving the showing of these two divisions. From Table 15 it is apparent that the median of service falls in the "3 years to 4 years" grouping and that slightly over 30 per cent of the managers have held their positions for over 5 years. This showing is very good, but efforts should be made to reduce the numbers serving less than 1 year. This reduction can be realized through more careful selection and by adding to the attractiveness of the manager's work in some associations.

REMUNERATION OF EMPLOYEES OTHER THAN MANAGERS. Full-time office employees of 33 associations received from \$40.00 to \$160.00 per month with the average rate between \$75.00 and \$100.00 per month. Salesmen and clerks in 34 cooperatives were paid from slightly less than \$75.00 per month to \$165.00 per month. The average of this group of employees was about \$100.00 per month, and most of these workers are men as contrasted to the office classification in which the majority are women. Delivery employees were reported by 22 organizations and their average wage was close to \$100.00 per month. Miscellaneous employees of petroleum cooperatives were paid about 40 cents per hour while this group in the feed and unclassified divisions received from $110.00 to $125.00 per month as an average. Most of this latter group are engaged in manufacturing processes and many are skilled laborers, which accounts for their relatively high average wage.

BONDS ON EMPLOYEES. Table 16 is a tabulation of the amounts of bond required of managers in 59 reporting associations. Forty associations require bond ranging from $1,000 to $10,000 on their managers, but only 14 cooperatives reported bonds on employees other than their managers. Petroleum associations were least strict in the matter of bonding with no coverage whatsoever in 14 of 33 cases. Blanket bonds covering all employees hand-

Table 16. Amount of Manager's Bond in 59 Oregon Cooperatives Handling Farm Supplies, by Type of Association, 1938

Amount of Coverage	All	Petroleum	Feed	Unclassified
None..................	19	14	2	3
$1,000 or less.........	5	5	-	-
$1,000 to $2,000......	10	7	1	2
$2,000 to $3,000......	7	1	6	-
$3,000 to $4,000......	2	1	-	1
$4,000 to $5,000......	5	1	1	3
$5,000 to $10,000.....	4	4	-	-
Blanket Bond..........	7	-	3	4
Associations Reporting.........	59	33	13	13

dling or having access to company funds were used in 7 associations of the feed and unclassified groups. Most managers who are not under bond reported that they would prefer to be bonded and several cooperatives are planning to bond their managers but have not "got around to it yet." The requiring of bond on the manager should be a matter of routine in the conduct of a cooperative business, because this bond will often serve to increase confidence in the fidelity of a manager while at the same time the association will be protected in case of actual misconduct. The fact that many cooperatives do not keep close check on the conduct of their business is all the more reason for enforcing the bond requirement. Blanket bonds are to be recommended in the larger organizations where the manager cannot keep in close contact with the daily transactions of the business.

Financial Structure

The financing of the cooperative business unit has always been of much interest to those involved in the movement. The average cooperative must practically always make its start without adequate financing because of the difficulty of collecting for stock or memberships at the time of subscription. The brunt of the organization responsibility must ordinarily be assumed by a small group of people, and many times it is difficult for these organizers to find anyone willing to contribute financial support until the business has proved itself through successful operation. Lending agencies are ordinarily not interested in advancing funds to the infant cooperative without personal endorsement of the organizers or directors. Inadequate financing and inefficient management have been cited as the greatest single causes of cooperative failure, indicating that ample justification is to be found for investigation of the investment requirements and loan conditions prevailing among the associations here under study.

AUTHORIZED CAPITAL STRUCTURE. The authorized capital of a cooperative refers to the amount and types of units into which the evidences of capital ownership are divided and which are established in the articles of association filed by the organization. The authorized capital of Oregon cooperatives is composed of either shares of stock or membership certificates. The membership certificate is usually more limited in its prospective sale because it carries the voting membership in the association. Stock is more flexible because it may be divided into common and preferred, with differing degrees of preference and voting rights being attached as the association may elect. Eighteen of the 62 units are of the membership type and the remaining 44 organizations have authorized stock ranging from no par to $500,000 par value stock. Table 17 indicates that the most common

Table 17. Authorized Capital Structure of 62 Oregon Cooperatives Handling Farm Supplies, by Type of Association, 1938

Type of Capital	All	Petroleum	Feed	Unclassified
Membership Certificates	18	11	5	2
Capital Stock:				
Under $5,000..........	7	5	-	2
$5,000 to $10,000....	8	6	1	1
$10,000 to $20,000...	3	-	2	1
$20,000 to $30,000...	12	8	1	3
$30,000 to $40,000...	1	1	-	-
$40,000 to $50,000...	4	1	2	1
Over $50,000..........	8	2	2	4
No Par Value..........	1	-	1	-
Associations Reporting..........	62	34	14	14

size of authorization is from $20,000 to $30,000, and the relation of common stock to preferred stock is usually either 1 to 1 or 2 to 1.

Most of the stock organizations have provided for preferred stock which does not ordinarily carry the voting right and which has preference in the matters of income and security. It was believed by some cooperatives that this preferred stock could be sold to business men or investors who were not eligible for membership. In fact, very little of this stock has ever been sold because when the cooperative is in real need of funds for getting the business under way, it is not ordinarily a very attractive proposition for the average investor. The most frequent use of preferred stock has been in connection with the withdrawal of a member where he ceases to be eligible for membership. In these cases preferred stock has been issued in place of the common stock held by the member involved and this new issue is usually retired within a relatively short time from a revolving fund for stock retirement. For the average local association, an authorized capital stock of $20,000 common and $10,000 preferred has proved satisfactory where a share unit of $10.00 or less has been used.

INVESTMENT REQUIREMENT. All associations require the purchase of a share of stock in the case of stock associations, or of a membership certificate in the membership type of organization, as a minimum requisite of membership. This requirement varies widely but reference to Table 18 indicates preference for a low investment with 45 of the 62 associations requiring $10.00 or less. Financing of the cooperative is the more difficult in the

Table 18. Investment Requirement of 62 Oregon Cooperatives Handling Farm Supplies, by Type of Association, 1938

Amount of Investment	All	Petroleum	Feed	Unclassified
Membership Certificates:				
$10.00 or less..........	18	11	4	3
$10.00 to $20.00.......	-	-	-	-
$20.00 to $30.00.......	1	-	-	1
Common Stock:				
$10.00 or less..........	27	16	5	6
$10.00 to $20.00.......	3	3	-	-
$20.00 to $30.00.......	8	4	1	3
$30.00 to $40.00.......	1	-	1	-
$40.00 to $50.00.......	1	-	1	-
Over $50.00.............	1	-	-	1
Variable Amount..........	1	-	1	-
Member of Farm Organization...........	1	-	1	-
Associations Reporting............	62	34	14	14

beginning when only $10.00 per member is asked and probably only a small fraction of this amount collected upon subscription. However, to place the required investment higher would undoubtedly bar many prospective members who are not interested enough in the venture to risk any considerable amount of money, even on a subscription note. The petroleum associations usually require the smallest investment as evidenced by the fact that almost 80 per cent of the group require $10.00 or less.

PAYMENT OF CAPITAL SUBSCRIPTION. As a further inducement to membership, most associations do not require the payment of cash in full at the time a member subscribes. Cash in full was reported by only 11 of 60 associations, and part cash is the practice of another 15 organizations. The most popular method in use and reported by over half the petroleum units is to require no cash at subscription, but to apply any dividends which may accrue to the member until the stock or membership is paid (Table 19). Marketing associations usually make use

Table 19. Method of Paying Subscription in 60 Oregon Cooperatives Handling Farm Supplies, by Type of Association, 1938

Means of Payment	All	Petroleum	Feed	Unclassified
Cash in Full.............	11	4	3	4
Negotiable Note..........	1	-	1	-
Deduction from Dividends	23	17	4	2
Part Cash and Balance from Dividends........	15	12	1	2
Deduction from commodities Delivered....	9	-	3	6
Any Method..............	1	-	1	-
Associations Reporting...........	60	33	13	14

of deductions from the proceeds of commodities delivered for sale through the cooperative. One association reported that any method which suited the member would be satisfactory to the cooperative, and a considerable number of associations are not requiring any formal subscription note. The tendency in most cases is to make the membership process as simple and easy as possible, especially after the organization is in operation and does not need the subscription funds so much as in the early days of the association.

SOURCES OF LOANS. The availability of loans is of real importance to many cooperatives, particularly those handling large stocks of seasonal goods or marketing farm products. Managers have reported that most local bankers demonstrated antipathy, if not outright hostility, toward the initial efforts of cooperatives in various localities. However, this attitude has disappeared in most of Oregon where the cooperatives have been proved through successful operation. Local banks are now the most frequently used single source of credit for the 61 associations reported in Table 20. The Spokane Bank for Cooperatives provided credit facilities for 10 associations of the marketing-purchasing type, but no distinctly supply cooperative had obtained funds from this source. Only 9 associations had no outstanding loans

Table 20. Sources of Loans Outstanding in 61 Oregon Cooperatives Handling Farm Supplies, by Type of Association, 1938

Reported Source	All	Petroleum	Feed	Unclassified
Members................	12	8	3	1
Local Bank.............	37	19	9	9
Bank for Cooperatives..	10	2	2	6
Individuals other than Members..........	6	2	4	-
None Borrowed..........	9	7	1	1
Trade Creditors........	1	-	1	-
Others.................	2	-	1	1

and these units are firm in their belief that the supply business should be on a "strictly cash" basis in respect to both the association buying from the wholesalers and the membership purchases from the cooperative. Members have loaned money to their cooperatives in 12 cases, and individuals outside the organization provided credit in 6 instances. Credit facilities have not been entirely satisfactory for a number of cooperatives as will be indicated in the sections dealing with interest rates and security, but the situation has improved rapidly with the spread of the cooperative movement.

SECURITY FOR LOANS. The frequency of use of the various forms of security for loans reported in 52 associations is set forth in Table 21. In 36 cases only an unsecured promissory note executed by the cooperative has

Table 21. Security for Loans of 52 Oregon Cooperatives Handling Farm Supplies, by Type of Association, 1938

Form of Security	All	Petro-leum	Feed	Unclassi-fied
Mortgage on Plant...........	15	3	5	7
Member Endorsement of Note..	8	7	1	-
Sales Contracts.............	1	-	1	-
Unsecured Promissory Note...	36	19	9	8
Warehouse Receipts..........	8	-	3	5
Endorsement by Manager......	1	1	-	-
Building Fund Certificate...	1	-	1	-

been required. Member endorsement, usually by directors, is in use in 8 cases, but this practice is not favored by most of the reporting organizations. Local banks have required the member endorsement in these instances although most bank loans to associations are made on the basis of an unsecured promissory note. Fifteen organizations, mostly of the feed and unclassified types, have given mortgages on their plants and equipment, and warehouse receipts have been used by the marketing units. The Bank for Cooperatives loans to these groups are usually secured by mortgage or warehouse receipts. Individuals hold a few mortgages on cooperative property, but the bulk of this indebtedness is the result of the purchase of facilities from the mortgage holder. Cooperatives are finding more and more credit facilities opened to their use on a reasonable basis without the pledge of specific security. In most localities the cooperatives are rapidly gaining the same sort of consideration in banking as has been given private business in the past.

RATE OF INTEREST. The rate of interest paid by some associations remains comparatively high, particularly in the cases of 10 petroleum cooperatives in the 7 to 8 per cent group in Table 22. The average rate paid is less

Table 22. Rates of Interest Paid on Funds Borrowed by 53 Oregon Cooperatives Handling Farm Supplies, by Type of Association, 1938

Interest Rate	All	Petroleum	Feed	Unclassified
None................	2	2	-	-
2 to 3 per cent....	9	-	3	6
3 to 4 per cent....	11	3	3	5
4 to 5 per cent....	11	5	2	4
5 to 6 per cent....	23	12	8	3
6 to 7 per cent....	4	2	2	-
7 to 8 per cent....	11	10	-	1

than 6 per cent, and this average is influenced considerably by the low rates of the Bank for Cooperatives loans. Several marketing associations reported that local bank funds are available at rates comparable to those of the Bank for Cooperatives. The low rates from 2 to 3 per cent were obtained through the use of warehouse receipts and the 3 to 5 per cent loans were mostly secured by mortgages, although two petroleum associations are paying no interest whatsoever on certain member loans. The bulk of the unsecured promissory note advances are bearing from 5 to 8 per cent, and there is little doubt that several associations could secure from 1 to 2 per cent reduction in their rates if they will call attention to the lower rates prevailing elsewhere. Particular attention should be directed toward reduction of these 7 and 8 per cent rates which appear too high for a business loan at this time. The current rates (March 1939) of the Bank for Cooperatives are $1\frac{1}{2}$ per cent on commodity advances, $2\frac{1}{2}$ per cent on operating capital loans and 4 per cent on facility loans. These rates will undoubtedly serve to influence reduction of the charges made by other agencies.

Operating Condition

The data contained in this section of the study is based upon material compiled from questionnaire forms returned by 55 of the 62 cooperatives included in the survey.1/ Sales figures were complete for the 55 associations reporting, but the balance sheet and operating statement forms were either incomplete or in a form not permitting comparison in approximately 20 of the 55 cases. For this reason the sample method has been utilized in arriving at the distribution of average balance sheet and operating statement items. In this sampling process the statements of 30 associations were analyzed and it is believed that the resulting averages are representative of the entire group.

DISTRIBUTION OF SALES. Total sales volume of the 55 reporting associations was $5,805,135, an average of $105,548 per unit. It appears that the total volume of the 62 associations included in the study plus the supply sales of a few marketing organizations not covered would

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1/ This questionnaire method was necessary because the personal canvass by the writer was conducted during the months of November and December, 1938, when the calendar year statistics were not available.

bring the total cooperative farm supply business in Oregon to over $6,000,000 for 1938. The average feed association had the largest volume of sales with a gross of $196,974, as compared to $59,278 for the petroleum units and $115,377 for the unclassified cooperatives. Approximately 48 per cent of the reported sales volume is listed by 14 feed cooperatives, 30 per cent by 30 petroleum associations and 22 per cent by 11 unclassified groups.

The Cooperative Division of the Farm Credit Administration conducted a study of the cooperative purchasing of farm supplies in Oregon for the year of 1933. The bulletin covering this study reports total sales for 30 of the 31 associations then handling supplies as $2,022,643 2/ Comparison of these data with the 1938 tabulation above indicates a 100 per cent increase in the number of associations handling supplies and almost 200 per cent gain in total sales during the five year period immediately following 1933.

The distribution of sales by products handled indicates that 45.5 per cent of all volume is found in feed, seed and fertilizer. Machinery, hardware, and other supplies constitute the second largest group in sales

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2/ Lister, John H.--"Cooperative Purchasing of Farm Supplies in Oregon - 1933," p. 2, Cooperative Division, Farm Credit Administration, 1935.

Table 23. Sales Volume and Distribution by Groups of Supplies of 55 Oregon Cooperatives Handling Farm Supplies by Type of Association, 1938

Groups of Supplies	All		Petroleum		Feed		Unclassified	
	Dollars	Per Cent	Dollars	Per Cent	Dollars	Per Cent	Dollars	Per Cent
Petroleum Products and Auto Supplies...	1,488,742	25.6	1,342,649	75.5	49,638	1.8	96,455	7.6
Feed, Seed and Fertilizer..............	2,639,110	45.5	60,464	3.4	2,517,727	91.3	60,919	4.8
Machinery, Hardware and Other Supplies	1,677,283	28.9	375,230	21.1	190,277	6.9	1,111,776	87.6
Total Sales Reported..................	5,805,135	100.0	1,778,543	100.0	2,757,642	100.0	1,269,150	100.0
Associations Reporting................	55		30		14		11	
Average Sales per Association..........	105,548		59,278		196,974		115,377	

volume with 28.9 per cent of the total and is followed by petroleum products and auto supplies in third place with 25.6 per cent. Table 23 indicates that feed associations tend to concentrate their business in one group of supplies to a greater extent than the organizations of other classifications and report 91.3 per cent of sales as feed, seed and fertilizer. Orchard supplies account for almost $750,000 of the sales volume reported by the 11 unclassified associations and are outranked in sales volume of individual supplies by feed and petroleum products only.

AVERAGE BALANCE SHEETS. As previously explained, the average balance sheets in Table 24 are based upon a representative sampling of 30 statements. The balance sheet for "All" associations is the result of weighting the average balance sheets of the three classifications according to the numerical frequency of each type. The total assets per unit range from $15,220 for the petroleum associations to $232,535 for the unclassified associations, and the average assets per unit for all associations are $73,924. The principal reason for the extremely large total assets of the average unclassified association is the inclusion of several extensive marketing organizations, and these large associations tend also to increase the assets of the average association listed under the

"All" associations heading.

Considerable variation in the composition of assets and liabilities exists among associations, both within classifications and among classifications. No attempt is made to discuss the balance sheet differences within classifications and the average is considered as representative of the group as a whole. Feed and petroleum associations are very similar in the percentage of current assets to total assets with either group listing over 59 per cent current. Petroleum and unclassified associations have 17 per cent of their assets in the form of accounts receivable, and the petroleum associations lead in cash position with 13.2 per cent of their total assets in the form of cash. The largest percentage of inventory is carried by the feed associations which have 42 per cent of their total assets in merchandise. Unclassified associations have the smallest percentage of inventory, principally because of handling seasonal goods which are moved before the close of the calendar year. Investment in fixed assets ranges from 24.7 per cent for petroleum associations to 50.1 per cent for unclassified associations. In this connection it must be remembered that the majority of the unclassified cooperatives are marketing organizations with a relatively heavy investment in facilities. Miscellaneous assets amounting to 15.7 per cent of the

Table 24. Average Balance Sheets of Oregon Cooperatives Handling Farm Supplies, by Type of Association, 1938

	All		Petroleum		Feed		Unclassified	
	Dollars	Per Cent	Dollars	Per Cent	Dollars	Per Cent	Dollars	Per Cent
Assets								
Current:								
Cash	2,124	2.9	2,013	13.2	2,300	3.7	2,225	1.0
Accounts Receivable	11,888	16.1	2,582	17.0	6,794	11.0	40,248	17.3
Notes Receivable	5,959	8.1			1,880	3.0	24,938	10.7
Inventories	15,999	21.6	4,404	28.9	26,165	42.1	34,821	15.0
Total Current	35,970	48.7	8,999	59.1	37,139	59.8	102,232	44.0
Fixed:								
Land and Buildings	19,814	26.8	1,955	12.8	19,393	31.2	64,884	27.9
Machinery and Equipment	23,528	31.8	2,616	17.2	15,896	25.6	83,444	35.9
Reserve for Depreciation	(10,382)	(14.0)	(809)	(5.3)	(12,845)	(20.6)	(31,854)	(13.7)
Total Fixed	32,960	44.6	3,762	24.7	22,444	36.2	116,474	50.1
Other:								
Prepaid Items	674	.9	76	.5	868	1.4	1,975	.8
Miscellaneous	4,320	5.8	2,383	15.7	1,639	2.6	11,854	5.1
Total Other	4,994	6.7	2,459	16.2	2,507	4.0	13,829	5.9
TOTAL ASSETS	73,924	100.0	15,220	100.0	62,090	100.0	232,535	100.0
Liabilities and Net Worth								
Current:								
Accounts Payable	5,757	7.8	2,138	14.0	6,922	11.2	13,643	5.9
Notes Payable	16,750	22.7	1,598	10.5	12,449	20.0	58,935	25.3
Accrued Items	975	1.3	80	.5	1,478	2.4	2,710	1.2
Miscellaneous	577	.8	1,039	6.8				
Total Current	24,059	32.6	4,855	31.8	20,849	33.6	75,288	32.4
Non-current:								
Mortgages or Contracts	13,470	18.2	283	1.9	5,773	9.3	54,136	23.3
Miscellaneous	1,516	2.0	513	3.4	2,509	4.0	3,031	1.3
Total Non-current	14,986	20.2	796	5.3	8,282	13.3	57,167	24.6
TOTAL LIABILITIES	39,045	52.8	5,651	37.1	29,131	46.9	132,455	57.0
Capital:								
Stock, Memberships and Certificates	19,829	26.8	3,474	22.8	14,703	23.7	65,844	28.3
Reserves:								
Working Capital, Contingencies and Undivided Earnings	15,050	20.4	6,095	40.1	18,256	29.4	34,236	14.7
TOTAL NET WORTH	34,879	47.2	9,569	62.9	32,959	53.1	100,080	43.0
TOTAL LIABILITIES AND NET WORTH	73,924	100.0	15,220	100.0	62,090	100.0	232,535	100.0

total are noted in the petroleum associations. This item is composed almost entirely of stock in other cooperatives, mostly regional wholesale organizations, and of unpaid subscriptions to the capital of the local units.

Little variation between groups is to be found in the percentage of current liabilities to total liabilities, the range being from 31.8 per cent for petroleum associations to 33.6 per cent for feed associations. Unclassified cooperatives have the smallest percentage of liabilities in the form of accounts payable and the largest percentage in notes payable, while the reverse situation is noted in the petroleum group. Non-current liabilities are greatest in the feed and unclassified associations where the investment in facilities is most extensive.

Membership capital investment in the form of stock and memberships varies from 22.8 per cent and 23.7 per cent in the petroleum and feed associations, respectively, to 28.3 in the unclassified group. Net worth in the form of reserves and undivided earnings varies in the opposite direction, the percentage being 40.1 per cent for petroleum associations, 29.4 per cent for feed associations, and 14.7 per cent for unclassified associations. In relation to membership capital investment it is of interest to note that feed associations report 89.2 per cent of capital subscriptions paid. This same relationship is 83 per cent for the petroleum group and 73.5 per cent for the unclassified organizations.

AVERAGE OPERATING STATEMENTS. The range of gross sales per unit as between groups of associations ran from $59,278 for petroleum cooperatives to $194,974 for feed associations. Little difference is to be found in the percentage of gross margin as indicated in Table 25. The total variation in percentage of gross margin is only 1.55 per cent, petroleum associations being high with 14.62 per cent and unclassified groups low with 13.07 per cent. Total expenses amounted to 12.72 per cent of sales in the feed cooperatives in contrast to 8.84 per cent in the unclassified group and 9.36 per cent in the petroleum classification. This higher percentage of expense in the feed associations appears to be the result of greater costs in connection with salaries and wages, maintenance of facilities, and bad accounts. Miscellaneous or other income reached 2.28 per cent of sales in the petroleum associations, this item being composed principally of dividends declared by regional wholesale cooperatives.

Net operating income was 5.26 per cent of sales in the petroleum group, 4.23 per cent in the unclassified cooperatives, and 1.67 per cent in the feed associations. Similar relationship existed between classifications in

Table 25. Average Operating Statements of Oregon Cooperatives Handling Farm Supplies, by Type of Association, 1938

	All		Petroleum		Feed		Unclassified	
	Dollars	Per Cent	Dollars	Per Cent	Dollars	Per Cent	Dollars	Per Cent
Gross Sales	105,548	100.00	59,278	100.00	196,974	100.00	115,377	100.00
Cost of Goods Sold	90,539	85.78	50,612	85.38	168,629	85.61	100,297	86.93
GROSS PROFIT	15,009	14.22	8,666	14.62	28,345	14.39	15,080	13.07
Expenses:								
Salaries and Wages	4,908	4.65	2,395	4.04	13,197	6.70	4,753	4.12
Interest	760	.72	101	.17	1,655	.84	2,284	1.98
Taxes	338	.32	113	.19	1,458	.74	277	.24
Insurance	285	.27	113	.19	847	.43	346	.30
Depreciation	538	.51	273	.46	1,142	.58	635	.55
Repairs	158	.15	53	.09	591	.30	162	.14
Rent	243	.23	53	.09	1,005	.51	346	.30
Advertising	84	.08	36	.06	374	.19	46	.04
Light, Water and Fuel	253	.24	1 24	.21	906	.46	115	.10
Office and Misc. Supplies	211	.20	130	.22	492	.25	92	.08
Auditing	127	.12	95	.16	118	.06	81	.07
Telephone and Telegraph	116	.11	71	.12	197	.10	104	.09
Bad Accounts	338	.32	113	.19	1,398	.71	312	.27
Travel and Director Expense	137	.13	65	.11	551	.28	69	.06
Truck and Delivery Expense	1,678	1.59	1,529	2.58	768	.39	358	.31
Other Expenses	369	.35	284	.48	354	.18	219	.19
Total Expense	10,543	9.99	5,548	9.36	25,053	12.72	10,199	8.84
NET OPERATING INCOME	4,466	4.23	3,118	5.26	3,292	1.67	4,881	4.23
Other Income	1,604	1.52	1,351	2.28	906	.46	785	.68
TOTAL NET INCOME	6,070	5.75	4,469	7.54	4,198	2.13	5,666	4.91

regard to total net income; the percentages being 7.54 per cent for petroleum, 4.91 per cent for unclassified, and 2.13 per cent for feed.

AVERAGE OPERATING RATIOS. The average ratios tabulated in Table 26 are based upon the statements in Tables 24 and 25. These ratios are obtained in the usual manner of dividing the first item listed by the second item and expressing the result as a decimal. The purpose of computing ratios is to provide means for analyzing the position of the business at any given time and of comparing the resulting ratios with certain standards.

Petroleum associations have the most favorable current ratio with 1.85, which means that the average petroleum cooperative has $1.85 of current assets for each dollar of current liabilities. The current ratio of feed associations is 1.78, and of unclassified cooperatives is 1.36. The often accepted standard of 2.00 for mercantile establishments is most nearly approached by the petroleum and feed associations.

Only 4 per cent of annual sales are represented by the accounts and notes receivable of feed and petroleum cooperatives. This ratio would indicate a comparatively rapid turnover of accounts and strict control of credit, but any conclusion in this respect must take into consideration the bad debt losses of each classification.

Table 26. Average Operating Ratios of Oregon Cooperatives Handling Farm Supplies, by Type of Association, 1938.*

Ratio	All	Petroleum	Feed	Unclassified
Current Assets to Current Liabilities........	1.49 to 1	1.85 to 1	1.78 to 1	1.36 to 1
Accounts and Notes Receivable to Sales.......	.17 "	.04 "	.04 "	.56 " **
Net Worth to Total Liabilities...............	.89 "	1.69 "	1.13 "	.76 "
Net Worth to Fixed Assets....................	1.06 "	2.54 "	1.47 "	.86 "
Net Worth to Total Assets....................	.47 "	.63 "	.53 "	.43 "
Sales to Total Assets........................	1.43 "	3.89 "	3.17 "	.50 " **
Net Income to Total Assets...................	.08 "	.29 "	.07 "	.02 " ***
Net Income to Net Worth......................	.17 "	.47 "	.13 "	.06 " ***

* Ratios are based upon the statements in Tables 24 and 25.
** Sales of supply department only are considered in relation to total sales and assets.
*** Income of supply department only is considered in relation to total assets and net worth.

The ratio of .56 listed for unclassified associations is not representative of their entire business since only supply sales are considered in relation to total receivables, whether arising from supply sales or marketing operations.

The net worth ratios indicate that the members of the petroleum and feed cooperatives own a larger equity in their organizations than do the members of the unclassified groups. Petroleum associations show the highest net worth ratios, varying from 2.54 in net worth to fixed assets, to .63 in net worth to total assets; and feed associations are next with a range from 1.47 to .53 in the same ratios. The high ratio of net worth to fixed assets in the petroleum classification reflects the lower percentage investment in facilities among these units. Creditor equity is in excess of membership equity only in the unclassified group where the net worth is 76 per cent of the total amount owed by the association to creditors. The ratio of net worth to total assets indicates that the members of the average petroleum cooperative own 63 per cent of their business, the feed association members own 53 per cent, and the cooperators in the unclassified group own 43 per cent.

Both petroleum and feed associations had gross sales in excess of three times their total assets. The ratio listed for the unclassified associations is unduly low because only supply sales are considered although the bulk of the volume in this classification is of a marketing nature. This same explanation applies to the unclassified associations in the ratios of net income to total assets, and of net income to net worth where the petroleum and feed units again rank higher. Net income represented 29 per cent of the total assets in the case of petroleum co-operatives and 7 per cent in the feed organizations. The average petroleum association had net earnings equal to 47 per cent of its net worth and this same ratio for feed units was 13 per cent. From their supply business alone, unclassified associations received net earnings which amounted to 2 per cent of their total assets and 6 per cent of their net worth.

The Marketing-Purchasing Combination

The present status of the supply departments being conducted by 21 Oregon marketing associations is of interest as an indicator of the future trends in cooperative purchasing. The advisability of combining the two functions, marketing and purchasing, in one organization is a point debated in the ranks of the marketing cooperatives of the state. Regardless of arguments pro and con, the fact remains that a very considerable volume of the farm supply business is being handled by these 21 organizations. Some discussion of the types of products being stocked by these supply departments serves to clarify the position of the marketing associations as regards the farm supply business. The consensus among the managers of these units and their reports of the value of the supply department are of interest in this consideration.

The frequency of handling the various classes of farm supplies in the 21 marketing associations reporting is tabulated in Table 27. From this table we note that the tendency is for the supply department to handle goods involved in the production of the product marketed by the association. Thus, we find that the dairy associations concentrate their efforts on feed, dairy supplies, seed, and related lines; and the grain associations, while handling a wider variety of goods, devote most of their attention to feed, petroleum, auto supplies, harvest supplies and insurance. The majority of the supply departments of grain associations are of the petroleum type and handle practically the same merchandise as the strictly supply cooperatives in the same classification. Fertilizer and orchard supplies are the most frequently handled merchandise in the fruit and vegetable group, although two of these associations are

Table 27. Frequency of Handling Farm Supplies in 21 Oregon Marketing Cooperatives, by Type of Association, 1933

Product	Seven Dairy	Seven Grain	Five Fruit and Veg.	One Poultry	One Wool
Petroleum	1	6	2	-	-
Feed................	6	7	1	1	-
Seed................	4	3	3	-	-
Fertilizer...........	4	2	5	-	-
Auto Supplies........	-	6	2	-	-
Machinery............	2	3	2	-	-
Hardware.............	1	3	2	-	-
Groceries, Dry Goods.	-	-	2	-	-
Orchard Supplies.....	-	1	5	-	-
Harvest Supplies.....	-	6	-	-	-
Dairy Supplies.......	7	1	1	-	-
Poultry Supplies.....	3	1	1	1	-
Electrical Appliances	-	3	2	-	-
Insurance............	-	5	-	-	-
Fuel.................	-	2	-	-	-
Building Material....	-	1	-	-	-
Bee Supplies.........	-	-	1	-	-
Wool Supplies........	-	-	-	-	1

conducting a complete farm supply and general store business. The poultry association has confined itself to feed and poultry supplies and the wool association carries only wool supplies. This clearly illustrates the tendency of the marketing association to handle supplies related to production of the product marketed.

The major point of the above discussion is emphasized in Table 28 which lists the principal lines of supplies handled by the 21 associations. The principal lines sold

Table 28. Principal Supplies Handled by 21 Oregon Marketing Cooperatives, by Type of Association, 1938

Product	Dairy	Grain	Fruit and Veg.	Poultry	Wool
Petroleum...........	-	3	1	-	-
Feed................	6	1	-	1	-
Machinery...........	-	1	-	-	-
Groceries, Dry Goods	-	-	1	-	-
Orchard Supplies....	-	-	3	-	-
Harvest Supplies....	-	2	-	-	-
Dairy Supplies......	1	-	-	-	-
Wool Supplies.......	-	-	-	-	1
Associations Reporting.......	7	7	5	1	1

by the 7 dairy associations are feed and dairy supplies, feed being predominant in 6 cases. The greatest supply volume of the 7 grain associations is found to be petroleum, feed, machinery and harvest supplies. Feed predominates in only one of these units and is the only case in this group where the largest volume of supplies is not directly related to the production of grain. In the fruit and vegetable section we find 3 associations with orchard supplies as the most important line and one association with each of petroleum and groceries and dry goods. The poultry and wool cooperatives handle only supplies used in the production of their respective products, feed in the former case and wool supplies in the latter. These facts bear out the contention of most marketing associations that they are interested in the supply business only as a means of reducing the cost of production, as it relates to the products marketed.

The greatest objection voiced by marketing associations in regard to expanding the lines of supplies handled is based upon the credit problem involved. The two associations operating general stores as a part of their supply activity report that credit is a major difficulty. The tendency is for the member to expect the cooperative to carry him and his family for all necessary supplies, particularly so long as any part of his products delivered are not settled for. The broader the lines handled, the more credit is expected and demanded by the membership. Even after final disposition of the delivered products, the association must often carry the member until the next harvest period. A county agent serving in the territory of one of the above cooperatives states that the association has been the only thing between many small growers and relief, but this fact does not serve to alter the very real credit problem of such an organization. The least credit difficulty is found where the supplies handled form a comparatively small part of the total cost of production, as in the case of orchard supplies or wool supplies. Contrasted to this situation are the dairy and poultry associations which supply feed to their producers. In other words, the potential credit problem of the marketing association handling supplies hinges to a considerable extent upon the relative position of these supplies in the cost of producing the product marketed and the number and class of lines handled.

One of the most effective arguments for the addition of a supply department to a marketing organization has been to the effect that such addition would lead to more efficient use of facilities and personnel. Also, the marketing association already has an active clientele to which it may look for its prospective patronage. The majority of these supply departments are not housed in separate buildings and the bulk of their office work is handled through the central office of the association. Usually some one person is directly responsible for the operation of the supply department, but personnel may be shifted from one division to another as necessity demands. There is considerable justification for the above contention of greater efficiency and practically all managers of these 21 associations report that their supply departments are operating at a relatively low cost. Part of this low operating cost is undoubtedly the result of considering the supply department as a service unit, and as such, this unit often does not carry its portion of the overhead and indirect expenses. However, even in those cases where the accounting for the supply department is complete, the operating costs of most supply departments are relatively moderate and little criticism appears appropriate relative to the combination in this respect.

In addition to the credit angle, another reported obstacle to the expansion of the supply business in the marketing organization lies in antagonism of private trade interests through which most of the association products must be marketed. This side of the problem was mentioned most frequently by the fruit and vegetable, and dairy associations which depend upon retail channels for their ultimate outlet to the consumer trade. So long as the association holds its supply business to products essential to the actual production of the products marketed, there is not a noticeable amount of organized criticism from the private business interests.

A more abstract, but nevertheless real, point in this discussion is the view of certain cooperative leaders that, fundamentally, the marketing and purchasing movements may be pointing in opposite directions. It is the function of the marketing cooperative to secure as much as possible for the producer's product, while the supply cooperative is trying to furnish the needs of the consumer and producer at as low a net cost as possible. This conflict of interests does not appear in the bulk of these 21 marketing associations included in the study. The only cases where the problem appears at all are the grain associations manufacturing feed and the fruit and vegetable units selling canned goods through their stores. Where the marketing association restricts itself to supplies used directly in the production of the product marketed, this conflict of interests does not appear and it is to this end that most Oregon marketing cooperatives with supply departments are aiming.

A few marketing organizations have added unrelated lines to their supply departments, and in so doing they have made profitable operation for supply cooperatives in the same territory very difficult. Several cooperative leaders expressed the view that a marketing organization should not add an unrelated line of supplies when such action jeopardizes the existence of another cooperative handling a full line of supplies. Marketing and purchasing cooperatives have much in common and should cooperate for their mutual benefit. Several marketing associations are themselves patronizing the supply organizations and are working with the supply group in the matter of credit arrangements for supply purchases by their membership.

Accounting and Internal Control

The value of an efficient accounting system has been overlooked or underestimated by many cooperative organizations. This tendency to minimize the importance of accounts and records has been a leading factor among the causes contributing to the failure of a number of associations. The majority of managers and directors are now recognizing the advantage of adequate records and a number of units have installed very efficient systems. While the value of a plan adapted to the cooperative unit is realized and such a plan is desired by most groups, the cost of installation by public accounting firms has been regarded as prohibitive by the smaller units. There are very few books available on the subject of cooperative accounting and the majority of associations have been forced to develop their own systems, each adopting its own plan in light of its needs. Certain of these self-developed systems are very effective and are worthy of being passed on to other units doing a similar business. An effort is being made by one regional cooperative to maintain uniform accounts in all affiliated units and with this uniform system a central auditing service is provided the members. The following discussion of cooperative accounting is based upon observations of the plans now in use in the various Oregon cooperatives. Due credit must be given the managers, accountants, and office employees who have been instrumental in the introduction of these methods.

ADVANTAGES OF A COMPLETE ACCOUNTING SYSTEM. A well-adapted accounting plan involving the use of standard double entry bookkeeping consisting of the journals, general ledger and such subsidiary ledgers and other records as may be necessary, provides a number of advantages to any cooperative organization. Among the more important of these advantages are:

1. The manager and directors may base their operating policies upon the information to be gained from study of the financial records of the organization.

2. The buying and selling plans of the manager are more accurately formulated when adequate operating statements are available.

3. It enables the directors and membership to judge more accurately the efficiency of the management and the relative position of the business unit at any given time.

4. Where essentially similar systems are being used, valuable comparisons as between associations may be made for the purpose of determining relative efficiency of operations and policies.

5. Adequate accounts are necessary if an association

is to secure and retain its exemption from the payment of federal and state income taxes.

6. Annual reports prepared for various governmental and credit agencies are more easily compiled.

7. Efficient accounting provides a source of valuable training and insight of business operation to those who are performing the work.

OFFICE EQUIPMENT AND METHODS. The office equipment of an association should include an adding machine, a typewriter, proper filing devices and, in most supply cooperatives, a cash register and sales ticket register. This equipment should be provided in order that the bookkeeping and office work may be handled with speed and accuracy. It is very important that a good safe be available for safekeeping of all association records. The preservation of all records is especially necessary in the case of a cooperative organization because the member equities in the reserves are based upon patronage, and this patronage record must be available at all times.

> The Oregon Cooperative Association Laws as amended in 1937, provide that, "any association established under this act shall once each year, upon request of any member, render a statement to that member, showing or representing the proportionate interest of that member as such, in the assets or capital of that association, or in any particular reserve fund or any other specific portion of such assets or capital." (Chap. VIII, Sec. 25-811)

For this reason it is imperative that the association safeguard all records and that these records be complete.

The computation of dividends is a detailed task and is a long, tedious job without an adding machine. Filing devices are very desirable in order that correspondence and invoices may be easily available for future reference. The filing system need not be elaborate or costly, but should include a metal filing cabinet equipped with alphabetical index and filing folders for each class of material to be filed. The use of a sales register on which all sales are recorded in duplicate or triplicate is a material improvement over the duplicating sales books, and such a register could be used to advantage by a number of associations. The sales register tickets are not so easily lost or misplaced and are usually more convenient for filing purposes. Where a considerable amount of cash business is transacted, the association should own and use a cash register because it provides a more effective means of controlling receipts and disbursements. The majority of the organizations included in this study meet the minimum requirements for office equipment, but there are a number of units without filing cabinets and fireproof safes.

HANDLING THE CASH. From the standpoint of accounting procedure and ease of auditing the association records, all cash receipts should be deposited intact at regular intervals and the proper entries made daily in the cash journal. All disbursements should be made by check in order that the cancelled checks may be used as a permanent record of expenditures and receipts therefor.

To eliminate the need for issuing checks to cover small items of expense, most associations have set up a petty cash fund of from $25.00 to $50.00 When the petty cash fund is established, an initial check is drawn in the amount of the fund and is made payable to and charged to "Petty Cash" in the journal. Hereafter, this item will be carried as an asset in the general ledger and is always carried to the trial balance intact. Payments from this cash fund are always to be covered by a receipt showing the payee, the amount, and the purpose of the disbursement. Every month, or more often if necessary, a check is drawn to the order of Petty Cash to cover the expenditures from the fund. This check is cashed and the money placed in the fund, and the petty cash is restored to the original amount each time this action is taken. When the petty cash check is entered in the journal, it is charged out to the expense accounts to which the petty cash receipts are related. The advantage of the petty cash fund is that it allows for minor payments covering office supplies, postage, express, contributions and other small items without drawing a check to cover each disbursement; while at the same time the replenishing of the petty cash by check complies with the general rule that all payments be by check.

THE JOURNAL - CASH, SALES, AND PURCHASES. In most cooperative purchasing associations of average size, all journal entries may be combined into one book of original entry. The usual method is to use standard columnar forms in a sectional post binder, and to head up the columns in such a manner that there is a place for both debit and credit sides of every transaction. Each page may be cross-footed and checked for balance prior to carrying the totals forward to the next page. The column totals are posted to the general ledger at the close of each month in most cases, although some associations prefer to post to the general ledger daily or weekly. This posting to the general ledger is not to be confused with entries in the accounts receivable or customer's ledger. In this latter subsidiary ledger, posting to the individual accounts of patrons is a daily routine and such entries are usually made from sales tickets or receipts for payments on account.

The headings of the journal will usually include the following debits:

1. Purchases. Where the organization has several departments, this heading will include several columns such as feed, gasoline, hardware, etc. The headings are made to suit the particular type of business involved.

2. Accounts Receivable. In this column are listed the charges to the accounts of patrons. Usually the total charges for one day are listed in a single item and the individual charges are posted to the accounts receivable ledger from the sales tickets.

3. Expenses. A number of associations are using a "fly leaf" in their journal in order that the "Expenses" item may be broken down into its component parts. Where the single column is used, each entry must be initialed in order that segregation of the total may be simplified at the close of the accounting period. It appears that the fly leaf should be installed where the association has any material volume of individual expense items to put through the journal. All payments or obligations incurred in connection with the operation of the business other than merchandise purchases and capital investment, are charged out through the expense headings.

4. Cash. All cash receipts from whatever source are entered in this column.

5. Bank Deposits. The amount of each bank deposit is entered in this column on the day of deposit.

6. General Ledger. Any debit entries for which no separate heading is provided are placed in the general ledger column. Each entry is to be initialed or otherwise identified with the account to which it is charged, and each item is ordinarily posted individually to the account involved; although some associations post only once a month and group the general ledger items according to accounts involved. This column is not to be used where there are a number of frequently recurring transactions involving one account. In such cases a separate heading should be established for the account in order that posting may be simplified.

7. Accounts Payable. All payments to creditors or allowances to the association on trade accounts are entered in this column. These items are then posted individually to the accounts payable ledger and the total carried to the general ledger.

The credit side of the combined journal should include these headings in the average case:

1. Checks Issued. The amounts of all disbursements by bank check are entered here, and in connection with this heading, a smaller column should be provided in which the check number may be recorded. This column combined with the "Bank Deposits" listing is used in preparing the

monthly reconciliation of the bank account.

2. Accounts Receivable. All payments on account and any other credits to patron accounts are listed in this category. It is customary to group the credits for one day in a single entry covering the lot. As in the case of charges to customer accounts, posting to the subsidiary accounts receivable ledger is from individual tickets or receipts.

3. Sales. This heading is broken into departments to correspond with the divisions of "Purchases" on the debit side. This departmentalization is of importance in dividend determination and in aiding the management to determine the relative operating efficiency in the handling of the various classes of merchandise.

4. General Ledger. This column on the credit side serves the same purpose as the "General Ledger" column on the debit side, and must be provided to care for miscellaneous entries for which no separate heading is provided.

5. Accounts Payable. This column is provided where an association purchases on a credit basis and the entries under this heading consist of the individual purchases, as indicated in the invoices received from the creditor firms. It is convenient to provide a space for listing

the invoice numbers when the purchases are entered in the journal.

In addition to the headings mentioned above, the journal always provides the customary date, explanation, and folio columns. These columns are often conveniently located between the debit and credit sides of the journal. While this type of journal will serve the needs of the average purchasing association, it cannot be expected to suffice in the larger organizations where the books must often provide for the recording of marketing transactions in addition to the supply business. These larger and more diversified units have usually found it necessary to set up several journals and these specialized journals may include a cash journal and check register, a general journal, an accounts payable journal or invoice register, and a sales journal.

A number of associations have developed a daily "recap" form which serves to summarize the transactions for each day, and this summary is then used to check the balance of the cash and to serve as the basis of entries into the journal. This daily summary lists the sales by department and according to cash and credit classifications, and sometimes lists the quantity of goods sold in order that the book inventory may be kept in operation. A simple recap form will serve to prevent many errors in journal entries and the organizations making use of this plan are well satisfied with its operation.

GENERAL LEDGER. The ordinary general ledger is a standard loose leaf form to be used in a sectional post binder and this ledger form is of the three column type with debit, credit, and balance headings. The various divisions of the accounts, such as assets, liabilities, capital, etc., are separated by dividers and each group of accounts should have its own series of numbers in order that posting may be facilitated. The account headings now in use among the various associations vary in name and number but, in general, an essentially similar basic pattern is noted and this similarity allows for some comparison among units. No single classification of accounts can be formulated to fit the needs of all cooperatives handling different classes of supplies and operating under varying conditions, but the following classification may serve as a guide to certain associations desiring to follow a standardized plan of naming and numbering accounts. Account numbers fulfill a useful purpose in that they serve as identification in making journal entries and in posting to the ledger.

ACCOUNT CLASSIFICATION FOR A PURCHASING COOPERATIVE

1. Current Assets

111 Cash on Hand
112 Cash in Bank
12 Accounts Receivable
13 Notes Receivable
14 Merchandise Inventory

2. Fixed Assets

21 Land
22 Buildings
23 Machinery and Equipment
24 Trucks
25 Office Equipment

3. Other Assets

31 Supplies Inventory (Operating supplies only)
32 Prepaid Expenses
33 Investments
34 Stock Subscriptions Receivable

4. Current Liabilities

41 Accounts Payable
42 Notes Payable
43 Accrued Expenses
- 431 Accrued Interest
- 432 Accrued Salaries and Wages
- 433 Accrued Taxes

5. Non-current Liabilities

51 Mortgage Payable (or Long Term Notes)
52 Certificates of Indebtedness

6. Net Worth and Reserves

61 Capital Stock (or Membership Certificates) Issued
62 Capital Stock (or Membership Certificates) Subscribed
63 Working Capital Reserve evidenced by Credits to Individual Patrons
64 Undivided Earnings
65 Valuation Reserves
- 651 Reserve for Depreciation of Buildings
- 652 Reserve for Depreciation of Machinery and Equipment
- 653 Reserve for Depreciation of Trucks
- 654 Reserve for Depreciation of Office Equipment
- 655 Reserve for Bad Debts

7. Purchases

71 ____________________ Purchased
72 ____________________ Purchased
73 ____________________ Purchased
74 ____________________ Purchased

8. Sales

81 Sales of ____________________
82 Sales of ____________________
83 Sales of ____________________
84 Sales of ____________________

9. Expenses

911 Salaries and Wages
912 Commissions
913 Delivery Expense
914 Miscellaneous Expense
915 Light, Heat, Water and Power
916 Communications
917 Office Supplies
918 Interest
919 Taxes
920 Insurance
921 Plant Maintenance
922 Rent
923 Advertising and Donations
924 Auditing and Legal Fees
925 Bad Debts
926 Depreciation
927 Directors Fees and Expenses
928 Travel Expense

10. Other Income and Expense

1011 Interest Received
1012 Discounts Received
1013 Dividends Received
1014 Miscellaneous Income
1021 Discounts Allowed

This system of general ledger accounts is presented only as a guide and may be rearranged or revised to fit the needs of any particular cooperative.

SUBSIDIARY LEDGERS. The three principal auxiliary ledger records which should be maintained by a cooperative association are:

1. Accounts Receivable Ledger
2. Accounts Payable Ledger
3. Reserve Equities Ledger

These subsidiary ledgers serve as a listing of the individual items which go to make up the balances of the related control accounts in the general ledger. For example, the accounts receivable ledger provides the amounts of the individual patron accounts, and the total of these individual items is equal to the balance of the "Accounts Receivable" account in the general ledger. This same principle holds in the cases of the accounts payable and reserve equities ledgers.

The accounts receivable ledger is an absolute necessity in any association doing a credit business. This type of record is doubly valuable to a cooperative organization because it can be made to serve as a complete record of all purchases by a patron, and several units are using this record in the dual capacity by carrying all sales, whether cash or credit, through the receivables ledger. Where the cash sales are routed through the accounts receivable ledger, a corresponding credit entry is made to offset the charge. The ledger sheet serving both of the above purposes is a loose leaf form with the usual debit, credit, and balance columns to provide the balance due the association at any given time. In addition to these three headings, the form has columns in which the purchases may be entered according to department or type of product. Thus, the single ledger serves as a record of a patron's total purchases as well as a statement of the patron's account. The record of purchases is of great value in the determination of dividends and in presenting evidence of the percentage of business conducted with non-members. The posting to this ledger is from sales or credit tickets and the total balances of the individual accounts must always equal the balance of the control account in the general ledger.

The accounts payable ledger, or creditors' ledger, is a record of the transactions with the individual firms from which the association purchases goods or services. This ledger is ordinarily made up of the conventional three column ledger sheets which are kept in a binder similar to that used for the accounts receivable. Many associations use parts of the same binder for accounts receivable and accounts payable, each division having its own alphabetical index. The posting to this ledger is from invoices and credit memos of the creditor firms and from the payments listed in the debit "Accounts Payable" column of the journal.

Only 8 associations of the 59 reporting on the question are making regular use of an accurate reserve equities ledger. Until recently, little attention was given the maintenance of such a record, but under present cooperative laws and tax exemption regulations, this type of record has assumed real importance. The Oregon Cooperative Association Laws provide that any member may ask for an annual statement of his equity in the net worth of the association. In addition to this provision, the State Tax Commission insists upon these specific credits to any non-members who may transact business with the cooperative as a condition precedent to exemption from the corporation excise tax. An accurate record of individual equities in the reserves of the association is of inestimable value in case of dissolution or reorganization. Associations which have operated over a period of years may have difficulty in establishing individual equities in their present reserves, but once this has been accomplished, it is a comparatively simple task to set up these equities each year thereafter. This record may be a regular sectional post binder with alphabetical index and the conventional three column ledger sheets. The entries to each account are based upon each patron's contribution to the total patronage and are ordinarily prorated in the same manner as any dividends which may be declared. Thus, if the association declares 80 per cent of its earnings as dividends, each member's equity in the "hold-back" will be 25 per cent of the amount of his dividend.

AUDITING AND SUPERVISION. Over 50 per cent of the 60 associations reporting in Table 29 are having their books audited by public accounting firms. This supervision ranges from an annual review requiring two or three days to complete charge of all association records throughout the year. Several cooperatives keep only sales records, accounts receivable ledger, and notation records

Table 29. Auditing of Accounts in 60 Oregon Cooperatives Handling Farm Supplies, by Type of Association, 1938

Auditing Agency	All	Petroleum	Feed	Unclassified
Public Accounting Firm...	31	11	10	10
Qualified Accountant.....	10	5	4	1
Regional Cooperative.....	15	14	-	1
Directors or Members.....	3	1	-	2
None.....................	1	1	-	-
Associations Reporting.	60	32	14	14

of receipts and disbursements at the association office; all entries in the journal and ledgers, except accounts receivable, being made by the accounting firm in its office. In these cases the monthly statements and annual reports are issued by the accounting firm as a part of its function as association accountant. This method is attractive to those associations who cannot hire regular and competent office help capable of keeping the accounts and preparing financial statements. Ten units report auditing by a qualified accountant, usually some accountant employed locally and who does some outside work on a part-time basis. Regional cooperatives are supplying auditing service to 15 associations and here the range of supervision runs from direct control of the association ledger, from which monthly statements are prepared, to an occasional check-up at the request of the local unit, usually once or twice a year. Only 4 groups do not have any outside person or agency to check upon and verify the accuracy of the association accounts. The fact that the books are audited does not mean that the accounting systems are all efficient and well-adapted. In fact, a number of associations have failed to carry out recommended changes in their systems and have continued from year to year using the same inadequate procedure. Most cooperatives are recognizing the value of some outside supervision and auditing, and more efficient accounting systems are being rapidly adopted as new methods are developed to fit the peculiar needs of the cooperatives.

STATE AND FEDERAL TAX EXEMPTION FOR COOPERATIVES. All cooperatives are interested in securing and retaining their exemptions from the state corporation excise tax and the federal corporation income tax. Of 59 associations reporting in Table 30, 48 organizations have secured exemption from both levies and 5 other groups are exempt from one or the other of the taxes. Only 6 associations are filing returns under both the federal and

Table 30. Federal Income Tax and State Excise Tax Status of 59 Oregon Cooperatives Handling Farm Supplies, by Type of Association, 1938

Status	All	Petroleum	Feed	Unclassified
Exempt State and Federal.......	48	25	12	11
Exempt Federal and not State...	4	3	-	1
Exempt State and not Federal...	1	1	-	-
Pay both State and Federal.....	6	3	1	2
Associations Reporting.......	59	32	13	14

state corporation income taxes. After obtaining its exemption an association should not consider the matter closed because this exemption may be cancelled through the violation of any of the provisions under which it was originally granted. For this reason, the more important points determining exemption under each tax are of interest to the management of any supply cooperative seeking the tax-exempt status.

The following principles are fundamental in the determination of exemption from the filing of the federal corporation income tax returns:

1. The association must be organized and operated on a cooperative basis. That is, a supply cooperative must have as its purpose the distribution of supplies at cost plus necessary expenses.

2. Members and non-member patrons must benefit from the operation of the association in exactly the same manner and upon the same basis, whether the entire savings of the association are returned as patronage dividends or a reasonable amount retained for necessary reserves.

3. Dividends on capital stock must not exceed 8 per cent per annum. This rate is also prescribed by the Oregon Cooperative Association Laws, and any cooperative operating in conformity with the provisions of this code is automatically eligible in this respect.

4. The value of supplies purchased for non-members shall not exceed in value the purchases for members, and purchases for non-members who are not agricultural producers must not exceed 15 per cent of the value of all purchases.

5. "Substantially all" of the voting capital stock must be owned by producers who patronize the association.

The above provisions are the most important points considered in the determination of federal income tax status and are more fully explained in a bulletin issued July 9, 1931 by the Treasury Department in elaboration of the Revenue Act of 1928. A reprint of this bulletin is presented as Appendix A of this report.3/ Exemption from the corporation income tax serves as the foundation for determining the status of a cooperative in regard to the capital stock, excess profits, and stamp taxes imposed by the federal government.

The State Tax Commission of Oregon has established certain principles for use in determining the status of a cooperative as regards the state corporation excise tax. Supply cooperatives are now mentioned specifically in the section of the present law which relates to the exemption of cooperatives.4/ To be eligible for this exemption a cooperative must meet these qualifications:

1. It must establish that for its own account it has no net income. In other words, all earnings must be

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3/ The Internal Revenue Service reports this bulletin the most recent Treasury Department statement providing comprehensive treatment of the conditions governing exemption of Farmers' Cooperative Associations.

4/ Specific treatment of supply cooperatives was added to the law dealing with corporation exemption by the 1939 apportioned to the patrons in proportion to individual patronage.

2. Non-members must receive exactly the same treatment as members in the declaration of dividends.

3. The association must maintain written records of the individual equities in any surplus accumulated for working capital purposes. This provision may be met through the use of the reserve equities ledger which facilitates the issuing of an annual "certificate of interest" by the cooperative.

4. The charter, articles of incorporation, or by-laws of the association must provide for equal participation of members and non-members in all savings, whether in the form of dividends or working capital reserves, and such participation must be based upon patronage. Thus, the membership cannot benefit at the expense of the non-member at any time or in any form.

Associations now exempt from either or both tax statutes should review their current operations from time to time in light of the technical exemption requirements, and make any necessary alterations in procedure before

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Legislature of the State of Oregon. See 1939 Session Laws, P. 991.

being subjected to investigation by federal or state agents. Several exemptions have been revoked during the past year and the operations of certain other cooperatives are now being scrutinized. These investigations have devoted particular attention to the treatment of non-members in the declaration of dividends and the building of working capital reserves.

APPENDIX A

TREASURY DEPARTMENT

Office of Comissioner of Internal Revenue

Washington, D. C.

IT-Mimeograph
COLL. No. 3886
R. A. No. 592

July 9, 1931

Exemption of Farmers' and Other Cooperative
Marketing and Purchasing Associations.

COLLECTORS OF INTERNAL REVENUE,
INTERNAL REVENUE AGENTS IN CHARGE,
AND OTHERS CONCERNED:

Under section 103 (12) of the Revenue Act of 1928 and section 231 (12) of the Revenue Act of 1926, and corresponding sections of prior revenue acts, cooperative associations engaged in the marketing of farm products for farmers, fruit-growers, live-stock growers, dairymen, etc., and turning back to the producers the proceeds of the sales of their products, less the necessary operating expenses, on the basis of the products furnished by them, are exempt from income tax and are not required to file returns.

The practice of the Treasury Department, under the revenue acts prior to the Revenue Act of 1926 has been at all times to extend the benefits of exemption from taxation to associations which operate for the benefit of their producer patrons, and to deny exemption in the cases of associations which operate so that their profits inure to the benefit of investors or others than the producer patrons equitably entitled to the profits. For example, these statutes have been construed in the cases of cooperative associations otherwise meeting the requirements of exemption, to include:

(1) Cooperative associations which buy and sell, and take title to, farm products in their own names and which strictly do not act as agents;

(2) Cooperative associations which deal with all producers, (whether or not they technically qualify as members) on a cooperative basis, the term "members" used in the exemption sections being construed to include all producer patrons in whose behalf the associations are operated;

(3) Cooperative associations which, in connection with their marketing functions, manufacture products and change the form of the raw materials furnished by the producers, such as cooperative creameries and fruit growers' cooperative cannery organizations; and

(4) Cooperative associations which issue capital stock provided the dividend rate is limited so as not to permit more than a fair return on the capital invested, and the ownership of any stock carrying the right to participate in the surplus of the association is restricted as far as possible to producer patrons.

The construction given by the Department to the pertinent provisions of the several revenue acts prior to the Revenue Act of 1926 was in substance approved by Congress and enacted into law as section 231 (12) of the latter Act. Speaking with respect to this section of the Revenue Act of 1926, the Senate Committee on Finance said:

> "Section 231 (12): The existing law, strictly construed, allows exemption only to those farmers', fruit-growers', or like associations which act as sales or purchasing agents for producer members and which return to such members the entire proceeds of their operations, except necessary sales or purchasing expenses. However, in order that any such association, not operated for profit, and which is a true cooperative association, shall get the benefit of this exemption, the Treasury Department in its regulations has construed the existing law with great liberality enlarging the term "member" to mean any producer whether or not a member, if treated by such an association on the same basis as a member; exempting such an association not acting as an agent, but taking title to products or supplies; allowing such associations to have outstanding capital stock and to pay dividends on such stock (subject to certain limitations); permitting such associations to build up reserves for State requirements or other necessary purposes; and allowing such associations to manufacture their products to change the form of raw materials, and in some cases to operate subsidiaries, so long as the operations are not conducted on an ordinary profit-making basis.
>
> "The committee amendment does not broaden the scope of nor even include all the provisions of the Treasury regulations but only incorporates certain provisions adopted by the department as fundamental in allowing exemptions to cooperative marketing and purchasing associations. The amendment will assure associations, now exempt, that the liberal construction, by the department, of existing law is sanctioned by Congress and if enacted will prevent a valid, but perhaps sudden or drastic, restriction upon exemptions, such as is now possible under existing law. It will also

permit a considerable number of cooperative agricultural associations, organized under general corporation laws, with capital stock, and not now exempt, to attempt to obtain exemption by changing their organization and operations to meet the requirements of permanent law rather than merely of impermanent regulations."

Section 103 (12) of the Revenue Act of 1928 follows verbatim section 231 (12) of the Revenue Act of 1926 and provides as follows:

"The following organizations shall be exempt from taxation under this title----

"(12) Farmers', fruit-growers', or like associations organized and operated on a cooperative basis (a) for the purpose of marketing the products of members or other producers, and turning back to them the proceeds of sales, less the necessary marketing expenses on the basis of either the quantity or the value of the products furnished by them, or (b) for the purpose of purchasing supplies and equipment for the use of members or other persons, and turning over such supplies and equipment to them at actual cost, plus necessary expenses. Exemption shall not be denied any such association because it has capital stock, if the dividend rate of such stock is fixed at not to exceed the legal rate of interest in the State of incorporation or 8 per centum per annum, whichever is greater, on the value of the consideration for which the stock was issued, and if substantially all such stock (other than nonvoting preferred stock, the owners of which are not entitled or permitted to participate, directly or indirectly, in the profits of the association, upon dissolution or otherwise, beyond the fixed dividends) is owned by producers who market their products or purchase their supplies and equipment through the association; nor shall exemption be denied any such association because there is accumulated and maintained by it a reserve required by State law or a reasonable reserve for any necessary purpose. Such an association may market the products of nonmembers in an amount the value of which does not exceed the value of the products marketed for members, and may purchase supplies and equipment for nonmembers in an

> amount the value of which does not exceed the value of the supplies and equipment purchased for members, provided the value of the purchases made for persons who are neither members nor producers does not exceed 15 per centum of the value of all its purchases."

It will be observed that this section exempts farmers' and other cooperative marketing associations organized and operated "for the purpose of marketing the products of members or other producers, and turning back to them the proceeds of sales, less the necessary marketing expenses on the basis of either the quantity or the value of the products furnished by them, * * *." (Underscoring supplied). The clear intent of this provision of the statute is that nonmember patrons, if dealt with at all, will be treated the same as members in so far as the distribution of patronage dividends is concerned. In other words, if products are marketed for nonmember producers the proceeds of the sales, less necessary operating expenses, must be returned to the patrons from the sale of whose goods such proceeds result, whether or not such patrons are members of the association. Therefore, a cooperative marketing association may not, without losing its exempt status, make a profit on the business transacted with nonmember patrons and divert the proceeds of such business from the patrons entitled thereto. However, where a cooperative marketing association has otherwise complied with the provisions of the statute respected exemption, but defers the payment of patronage dividends to nonmembers, exemption will not be denied---

1. Where the by-laws of the association provide that patronage dividends, by whatever name known, are payable to the members and nonmembers alike, and a general reserve is set up for the payment of patronage dividends to nonmembers.

2. Where the by-laws provide for the payment of patronage dividends to members, but are silent as to the payment of patronage dividends to nonmembers, but a specific credit to the individual account of each nonmember is set up on the books of the association.

3. Where the by-laws are silent as to the payment of patronage dividends to either members and / or nonmembers, but the evidence submitted shows that it has been the consistent practice of the association to make payment in cash or its equivalent of patronage dividends to members and nonmembers alike within a reasonable period after the expiration of the particular year involved.

4. Where, under the circumstances stated in 1, 2, and 3, above, patronage dividends are not payable until the nonmember becomes a member of the association either through the payment of the required amount in cash or the accumulation of dividends in an amount equal to the purchase

price of a share of stock or membership.

Under the regulations of the Department prior to their amendment by T. D. 3511, (C. B. II-2, 201) promulgated under the Revenue Act of 1921 and Treasury Decisions 3658 (C. B. III-2, 242) and 3709 (C. B. IV-1, 51) promulgated under the Revenue Act of 1924, a farmers' cooperative association was denied exemption if any of the stock of the association was held by nonproducers. By express provision of the Revenue Acts of 1926 and 1928 (and by the Departmental construction of prior revenue acts), farmers' cooperative marketing associations are exempt only if "substantially all" of the capital stock "(other than nonvoting preferred stock, the owners of which are not entitled or permitted to participate, directly or indirectly, in the profits of the association, upon dissolution or otherwise, beyond the fixed dividends) is owned by producers who market their products * * * through the association; * * *."

If an association is permitted to have nonproducers as stockholders and accumulate a surplus at the same time, the principle that a producer shall have returned to him the proceeds of the sale of his products less only necessary operating expenses is violated. This follows as a result of the established principle of law that the surplus of a stock corporation inures to the benefit of its stockholders. In recognition of this principle of law, the statutes of a number of states provide that cooperative associations must be organized without capital stock. In this connection, reference is made to the Civil Code of California (1929), Title XXII, Non-Profit Cooperative Corporation; Acts and Resolves of Mass. (1923), Chap. 438; and Pennsylvania Statutes (1920), Sec. 155, Incorporation of Cooperative Agricultural Associations. Therefore, where associations are permitted by law to organize with capital stock, it is essential to exemption that the ownership of capital stock which carries the right to participate in the surplus and reserves of the association be restricted, as far as possible, to actual producers.

It is impracticable to attempt to define the term "substantially all" as used in the statutes under discussion for the reason that what constitutes substantially all of the capital stock of a cooperative marketing association is a question of fact, which must be decided in the light of the circumstances surrounding each particular case. Any ownership of stock by other than actual producers must be explained by the association. The association will be required to show that the ownership of its capital stock has been restricted as far as possible to actual producers who market their products through the association. However, if by statutory requirement the officers of an association must be shareholders, the ownership of a share of stock by a nonproducer to qualify him as an officer will not destroy the association's exemption; or if a shareholder for any reason ceases to be a producer and the association is unable, because of a constitutional inhibition, or other reason beyond the control of the association, to purchase or retire the stock of such nonproducer, the fact that under such circumstances a small amount of the outstanding capital stock is owned by shareholders who are no longer producers will not destroy the exemption. On the other hand, where a substantial part of the stock was voluntarily sold to nonproducers, exemption must, under the statute, be denied as long as such stock is so held.

The statute recognizes that in order to operate a farmers' marketing association additional capital is frequently required. However, if it is necessary for such associations to be financed by investors, that situation must be taken care of by the issuance of preferred stock or bonds or other evidence of indebtedness for the purpose of providing necessary working capital, or acquiring property which is required for the conduct of the association's business. The holders of such securities may not be entitled or permitted to participate directly or indirectly in the profits of the association upon dissolution or otherwise beyond the regular fixed dividends or interest payments and voting control of the association must be retained by shareholders who are actual producers.

It is recognized in the law that cooperative associations have a need for accumulating and maintaining reserves for certain purposes, namely, "a reserve required by State law or a reasonable reserve for any necessary purpose." A reserve of the first class requires little discussion except to state that it must be a reserve required by a state law; a reserve permitted but not required does not meet this test of exemption. The necessity for the existence of any reserve or reserves, other than those reserves required by a state law, must be shown. The phrase, "reasonable reserve for any necessary purpose" has been construed to include reserves accumulated or maintained to meet capital expenditures of such associations. Where such an association has investments in buildings, machinery, and other property which, due to depreciation through use in the operations of the association, eventually reach a point where their usefulness is exhausted, such depreciation in a given year is properly chargeable against the patrons of the association as a part of the "necessary marketing expenses" of that year, and a reserve for the replacement of such property set up ratably over the period of the useful life of the property will be recognized as a necessary purpose within the meaning of the statute and the Departmental regulations.

Under the revenue acts prior to the Revenue Act of 1926, the extent of the business done by a farmers' cooperative marketing association with nonmenbers is immaterial, provided nonmembers are dealt with on the same basis as members, in so far as the payment of patronage dividends is concerned. However, under the Revenue Acts of 1926 and 1928, farmers' cooperative marketing associations may market the products of nonmembers only in "an amount the value of which does not exceed the value of the products marketed for members, * * *."

Membership in a cooperative association is, generally speaking, acquired in the same manner as membership in any other stock corporation--through the ownership of one or more shares of stock. However, as heretofore stated, the statutes of a number of states provide that farmers' cooperative associations must be organized without capital stock. Therefore, as the exemption statute is silent as to the qualifications of members in farmers' cooperative marketing associations, it follows that anyone who shares in the profits of such an association, and is entitled to participate in the management of the association, must be regarded as a member within the meaning of that statute.

In order to be exempt under the Revenue Act of 1921, and subsequent revenue acts, cooperative associations, engaged in the purchasing of supplies and equipment for farmers, fruit-growers, livestock-growers, dairymen, etc., and turning over such supplies and equipment to them at actual cost, plus the necessary operating expenses, must meet the forgoing conditions. An association which purchases supplies and equipment for non-members will not for such reason be denied exemption, provided the value of the purchases for nonmembers does not exceed the value of the supplies and equipment purchased for members, and provided the value of the purchases made for non-members who are not producers does not exceed 15 per cent of the value of all its purchases.

An association engaged both in marketing farm products and in purchasing supplies and equipment is exempt if, as to each of its functions, it meets the requirements set forth herein.

Associations claiming exemption as a farmers' cooperative marketing and / or purchasing association shall submit the information required by Questionnaire, Form 1028 (copies of which may be obtained from any collector) together with a copy of the articles of incorporation and the constitution and by-laws of the association. The latest financial statement shall also be submitted, showing the assets, liabilities, receipts, and disbursements of the association. When such an association has established its right to exemption it need not thereafter make a return of income, or any further showing with respect to its status under the law, unless it changes the character of its organization or operations or the purpose for which it was originally created.

Correspondence and inquiries regarding this mimeograph should refer to the number and symbols IT:E:RR.

H. F. Mires,
Acting Commissioner.