Financing
Oregon Cooperative Associations
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Foreword

Farmer marketing cooperatives are an integral part of the overall processing, storage, and handling of agricultural products in Oregon. Also, cooperative purchasing associations have developed during the past 25 years to provide another medium through which farmers may obtain supplies essential to efficient production. Efficient production of agricultural products serves the interest of both farmers and the general public.

This study deals with the important aspects of financing marketing and purchasing cooperative associations. When a group of farmers decide a cooperative is needed for their mutual benefit, they must be prepared to provide much of the total capital requirements. Like any other business, cooperative associations need capital for site, plant equipment, inventory, supplies, and to meet day-to-day operating expenses. Successful business enterprises do not operate on a shoestring. Credit institutions lend capital funds to cooperatives only after the farmer members themselves have provided a substantial part of total capital needs.

Financing of farmer cooperatives is an increasingly important problem because these organizations are becoming fewer in number but larger in size. This is a trend that is occurring in most cooperative business enterprises.

ACKNOWLEDGMENTS: The author greatly appreciates the cooperation of all the marketing and supply cooperatives who provided the information needed to make the analysis contained in this bulletin. Also, the Agricultural Cooperative Council of Oregon through its Secretary, Paul Carpenter, gave encouragement and valuable counsel during the study.

H. Prentiss Gazaway, Graduate Research Assistant, Oregon Agricultural Experiment Station, performed much of the field work and assisted in the tabulation of some of the data.
Summary

Records dealing with the important aspects of financial organization and capital structure were obtained from 119 marketing and farm supply cooperatives in Oregon for a 12-month period ending sometime in 1951 (in some cases it was 1950 or 1952). These associations did a total annual dollar volume of business in marketing of 144.1 million and a supply volume of 39.6 million, making a total of 183.7 million dollars. It is estimated that this was at least 90 per cent of all the cooperative marketing and farm supply business in Oregon during the period covered by the study. On the average, each association had slightly more than 500 active members, had 26 employees the year around, and total assets of 600 thousand dollars.

The average ratio of net worth to total assets of all associations was 53 per cent. This means that members provided 53 per cent of total capital employed and the remainder was borrowed or from other sources.

Fruit and vegetable associations had the largest capital requirements, each one on the average needing a little over a million dollars. On the average, dairy, and grain and seed associations had capital requirements between 600 and 700 thousand dollars and did the largest dollar volume of business. Supply associations had the lowest capital requirements with an average of 276 thousand dollars. Fruit
and vegetable associations had relatively heavy capital requirements because they needed expensive plants and equipment for processing. In addition, several of these associations carried large inventories of canned and frozen fruits and vegetables during much of the year.

By far the most important source of member capital was the revolving capital fund. On authorization of members, capital for the revolving fund was obtained through either the retention of net margin or by retaining part of the proceeds due patrons, or both. The average length of the revolving period for all of the associations was 9 years. Retains were still made after 9 years, but the oldest retains were being retired thereby giving the oldest members a cash payment. Only one in five of the associations with revolving capital funds paid any interest. Some of the advantages of the revolving capital fund plan are that funds are obtained proportional to patronage, capital is provided on an installment basis, and invested capital can be repaid on retirement or death of the member. In most instances, the revolving capital fund plan provided the only practicable means whereby relatively large amounts of capital could be obtained from the members over a period of years.

The Spokane Bank for Cooperatives was the most important source of borrowed funds from the point of view of total dollars. More than four-fifths of all loans, however, were obtained from commercial banks, private lenders, other cooperatives, and equipment manufacturers. The loans made by the bank for cooperatives were on the average much larger than those made by other lenders.

The weighted average interest rate for loans from individuals was 4.43 per cent whereas the average for commercial banks and the bank for cooperatives was 3.72 and 3.25 per cent respectively. The differences in these interest rates were sufficiently large to warrant careful consideration by cooperatives when it is necessary to borrow funds.

Associations 25 or more years of age were able to borrow operating and commodity funds at a much lower rate of interest than those under 25 years old. Also, associations doing more than a one million dollar business annually were able to borrow funds for all purposes at lower rates of interest than those doing less than a million dollar business.

The ratio of funds borrowed to total assets shows clearly that most associations 25 or more years old needed to borrow less than the newer organizations. On the average, associations 15 years of age or less had to borrow twice as much in proportion to total assets as those 25 or more years old. It can be seen, therefore, that the proportion of equity capital in most cooperatives is related directly to length of life of the organizations.
Financing
Oregon Cooperative Associations

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One of the most important problems facing Oregon cooperative associations is that of obtaining adequate capital. Much of the capital required by cooperatives needs to come from the membership. It often has been possible for cooperatives to borrow substantial funds for capital purposes, but it would have been better if farmer members could have provided larger amounts of capital. In some cases, however, cooperatives were not able to borrow because financial participation of the membership was inadequate. Commercial banks, banks for cooperatives, and others cannot be expected to finance entirely cooperative associations in which many of the members show little or no interest.

There are several methods of obtaining capital from the membership. A major purpose of this study is to show the relative importance of these methods together with an analysis of each. Also, sources of borrowed capital are indicated and appraised. An understanding of all important sources of capital is essential to successful cooperative enterprises. This study is aimed at improving such understanding so that cooperative associations may move closer toward rendering maximum service for their members.

In the first section of this report some basic facts are presented. These include volume of business, age of associations, number of members, number of employees, total assets, net worth, and requirements for membership. This is followed by a listing and appraisal of sources of capital employed by cooperative associations. The next section deals with the sources and analysis of member or equity capital. The report is concluded with an appraisal of borrowed capital.

Procedure

A total of 119 records was obtained by personal interview with managers of Oregon cooperative marketing and purchasing associations. Records were obtained from nearly every important association in the state. It is estimated that at least 90 per cent of the dollar volume of all marketing and supply cooperative business in Oregon
was done by these 119 associations. There were at least 20 other marketing and purchasing associations in the state but in most cases their volume of business was small. Most of these associations were not included because they required little capital or their records were inadequate. Every dairy and grain marketing association in the state is included in this study. Most of the very small associations were either marketing fruits or handling supplies.

Most of the records pertain to the year 1951 or part of 1951 if on a fiscal year basis. However, a few of the records obtained cover the fiscal year 1950 or 1952.

Some General Facts

Type of associations and volume of business

Although fourth in importance in number, grain and seed associations were largest in total dollar volume of business. (See Table 1.) The farm supply associations were the most numerous but did much less business than most of the marketing associations. It should be noted that many of the marketing associations did some farm supply business. Likewise, nearly one-fourth of the farm supply associations also did some marketing for their members.

Table 1. Volume of Business, by Type of Cooperative, Oregon 1951.

<table>
<thead>
<tr>
<th>Type</th>
<th>Number</th>
<th>Marketing volume</th>
<th>Supply volume</th>
<th>Total volume</th>
</tr>
</thead>
<tbody>
<tr>
<td></td>
<td></td>
<td>Million dollars</td>
<td>Million dollars</td>
<td>Million dollars</td>
</tr>
<tr>
<td>Farm supply</td>
<td>35</td>
<td>2.7</td>
<td>17.0</td>
<td>19.7</td>
</tr>
<tr>
<td>Dairy</td>
<td>28</td>
<td>45.6</td>
<td>6.4</td>
<td>52.0</td>
</tr>
<tr>
<td>Fruit and vegetable</td>
<td>23</td>
<td>35.6</td>
<td>2.8</td>
<td>38.4</td>
</tr>
<tr>
<td>Grain and seed</td>
<td>18</td>
<td>48.5</td>
<td>7.5</td>
<td>56.0</td>
</tr>
<tr>
<td>Nut</td>
<td>6</td>
<td>4.3</td>
<td>...</td>
<td>4.3</td>
</tr>
<tr>
<td>Miscellaneous¹</td>
<td>9</td>
<td>7.4</td>
<td>5.9</td>
<td>13.3</td>
</tr>
<tr>
<td><strong>Total</strong></td>
<td>119</td>
<td><strong>144.1</strong></td>
<td><strong>39.6</strong></td>
<td><strong>183.7</strong></td>
</tr>
</tbody>
</table>

¹ In subsequent sections of this report the miscellaneous category usually will not be included in the analysis except when seeking statistical relationships between two or more factors.

Age

About 71 per cent or 84 of the cooperatives included in this study were less than 25 years old (See Figure 1). Only 12 associations now in business were organized before 1920.

The many new cooperatives established in the 1930's consisted largely of farm supply, dairy, and grain associations. Several of
the fruit and vegetable, and nut associations were established prior to the 1930's. Few farm supply associations were established until the 1930's and 1940's. In most cases, the oldest organizations in the state are dairy, and fruit and vegetable associations.

**Number of members**

The 119 cooperatives included in this study had 59,258 active members or an average of slightly more than 500 in each association. According to the 1950 U. S. Census, there were 59,827 farms in Oregon. This does not mean that nearly every farmer belonged to a marketing or farm supply cooperative. Many farmers were members of more than one cooperative while others belonged to none. It was estimated that three out of every five farmers in the United States in 1949-50 belonged to either a marketing or purchasing association.¹ There are indications that Oregon farmers may hold membership in similar associations in about the same proportion.

**Number of employees**

Oregon marketing and supply cooperatives employed 3,100 people the year round or an average of 26 per association. An addi-

tional 8,600 people were employed during peak season. Most of the seasonal workers were employed by the fruit and vegetable associations. Dairy cooperatives also used some additional personnel during the spring and summer months. Of course, all types of associations employed some additional personnel during their peak season. Most farm supply associations, however, employed less seasonal labor than any of the other types.

**Total assets**

The total assets of the associations in this study were 71.2 million dollars or an average of 600 thousand dollars. Total assets averaged $1,200 per active member, with $636 of these assets financed per member. It can be seen that farmers have acquired considerable physical plant, equipment, inventory, and supplies to help them market and process their products and to obtain supplies needed for production.

**Net worth**

The net worth of Oregon marketing and purchasing associations was 38.0 million dollars. In other words, farmer members have provided 38.0 million dollars of the capital employed in the conduct of their respective cooperatives. The rest of their capital, amounting to 32.4 million dollars was borrowed or from other sources. The ratio of net worth to total assets was:

\[
\frac{38.0 \text{ million dollars}}{71.2 \text{ million dollars}} = 53 \text{ per cent}
\]

This means that 53 per cent of the total assets were financed by the owners—the farmer members. There was considerable variation in the ratio of net worth to total assets among associations. The reasons for these variations are given in another section of this bulletin.

**Capital stock**

Slightly more than one-half of the associations sold common stock to their members. Preferred stock was sold by one-half of the associations using common stock. A membership fee was collected from the members of associations who did not issue common stock.

Nearly one-half of the associations selling common stock had a par value of $10 a share. Several had common stock with a par value of either $25 or $50. Common stock with par values of less than $10 or more than $50 was not very common in Oregon. However one association had its common stock valued at $250 a share and five associations at $1 a share.
Nearly one-half of the associations authorized the payment of dividends on common stock, but only 33 per cent actually paid any in the year of this study. The dividend rate paid ranged from 2 to 8 per cent.

With reference to preferred stock, two-thirds of the associations had established a par value of either $10 or $25 a share. Several associations had their stock valued at $1, $50, or $100 a share.

Nearly all associations with preferred stock authorized the payment of dividends. Dividend payments ranged from 2 to 8 per cent with the most common dividend rate being 4 per cent, but a number of associations paid either 5 or 6 per cent. Most of the preferred stock sold was cumulative as to payment of dividends.

Whenever an issue of stock is contemplated, the par value per share needs to be established at a level that will raise the required amount of capital. Obviously, if the par value is high some small investors will not be able to participate. If the par value is $10 or $25 a share, people with only a small amount to invest may be inclined to purchase some of the issue. The large investors can, of course, buy several shares.

Requirements for membership

In the case of most capital stock associations, members were required to purchase at least one share of common stock. As already indicated, the par value of nearly all common stock was less than $100 a share. In practically all cases, it was not necessary to pay cash for membership stock. Patronage dividends could be applied on the purchase of a share of common stock.

In the case of most nonstock associations it was very easy to become a member. More than one-half of these associations had a membership fee of $5 or less. Only one association had a membership fee of as much as $50. Here again, patronage dividends could be applied to pay the membership fee.

Most farmer cooperatives have been careful to restrict membership to farmer growers in order that they might satisfy the provisions of the Capper-Volstead Act of 1922, the Act authorizing the association of farmers, and other legislation affecting their welfare.

Voting

All but eight of the associations allowed one vote per member irrespective of the number of shares owned and amount of business done during the year. Three associations had the provision in their by-laws that members could have additional votes if they owned more than a specified amount of stock. For example, one association
authorized an additional vote for every $200 of additional stock purchased but not to exceed 10 votes for any one member. Two associations had one vote for every share of stock owned. Two others had members voting on the basis of tonnage or patronage. In one association, members voted both on the basis of one-member-one-vote and tonnage.

Oregon laws relating to cooperative associations provide that voting shall be on the basis of one vote per member, or members may vote in proportion to patronage, or a combination of these two plans may be used. The law specifically provides that shares of stock as such shall not be given voting power in any case. The few associations in Oregon that authorize voting based on number of shares owned are incorporated under the general business statutes.

Affiliations with other organizations

At least three out of four Oregon cooperatives held membership in one or more regional marketing or supply cooperatives to assist them in the sale of their products or purchase of supplies. All of the farm supply, and grain and seed associations held membership in some large marketing and/or purchasing association. Most of the small fruit and vegetable, and livestock shipping organizations were independent.

There are six federated supply and marketing cooperatives located in Oregon. They are Pacific Supply Cooperative, Oregon Grange Wholesale; North Pacific Canners and Packers Co., North Pacific Grain Growers, Inc., Northwest Nut Growers, and Tillamook County Creamery Association. Many Oregon associations hold membership in the above-mentioned organizations. Still other important federated organizations in which several Oregon associations hold membership are Challenge Cream and Butter Association, Los Angeles; and United Dairymen’s Association, Seattle.

Net Margins of Associations

An analysis of net margins of cooperative associations does not produce any really conclusive results and this is particularly the case when data for only one year are available. Large net margins do not necessarily mean that the associations are meeting the expectations of their farmer members. Net margins may be high but the advance(s) made to patrons (if a marketing association) may have been low and the service may have been poor. In the case of a farm supply association the original sale price might have been relatively high, thus resulting in a high net margin. On the other
hand, an association with a low net margin may be rendering excellent service to its membership.

It is important, however, that cooperative associations do not suffer net losses year after year because it is a common practice to retain net margins in order to accumulate capital. At the time of this study, 10 associations showed a net loss at the end of the fiscal year and 25 others had a net margin ratio of less than 2 per cent. When all of the associations in the study (except those operating on a pool basis) are included the net margin ratio was:

\[
\frac{3.7 \text{ million dollars net margin}}{150.3 \text{ million dollars volume}} = 2.47 \text{ per cent}
\]

This means that for every dollar of business done by these associations, about 2½ cents was available for allocation to patrons as patronage refunds.

**Capital Employed and Volume of Business**

Cooperative associations, like other business organizations, require capital for site, plant, equipment, supplies, inventory, and working capital. Some types of cooperatives require more capital than others. Capital requirements depend largely on size and type of business, and services rendered to patrons.

**Average capital employed**

Fruit and vegetable associations employed the most capital but considerable capital was used by all types of associations (See Table 2). Most of the large fruit and vegetable associations needed large amounts of capital for plant and equipment for their canning and freezing operations. In addition, large inventories of canned and/or frozen products were maintained through most of the year.

Dairy and grain and seed associations also employed considerable capital. Much of their capital was needed for buildings and equipment. Those dairy associations manufacturing cheese, or acting as sales agent for manufacturing plants, needed large amounts of capital. Cheese was often held from six months to a year in the curing and storage rooms.

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2 When pooling organizations are referred to in this report it includes those associations that retain from each pool an amount sufficient to cover all expenses. Also, most associations made retains for capital. Each grower then received his pro rata share of the net proceeds according to the grade of product contributed to the pool. The financial statement at the end of the fiscal year shows no net margin for these pooling associations. It needs to be recognized that unless the product is sold on individual account, all marketing cooperatives operate on a pool basis. More than one-half of the marketing associations in Oregon make only one advance (the original price), and the financial statement at the close of the fiscal year shows a net margin or loss. Associations of this kind, however, are not referred to as pooling organizations in this bulletin.
Grain and seed associations had large inventories in the fall of the year. By the end of the fiscal year, however, usually April, May, or June, inventories were low. The same was true of cooperative nut associations.

Table 2. Average Capital Employed and Volume of Business for 109 Associations, by Type of Business, Oregon 1951.

<table>
<thead>
<tr>
<th>Type of cooperative</th>
<th>Number</th>
<th>Average capital employed</th>
<th>Average annual volume of business</th>
</tr>
</thead>
<tbody>
<tr>
<td></td>
<td></td>
<td>Thousand dollars</td>
<td>Thousand dollars</td>
</tr>
<tr>
<td>Fruit and vegetable</td>
<td>23</td>
<td>1,111</td>
<td>1,546</td>
</tr>
<tr>
<td>Dairy</td>
<td>27</td>
<td>692</td>
<td>1,627</td>
</tr>
<tr>
<td>Grain and seed</td>
<td>18</td>
<td>618</td>
<td>2,692</td>
</tr>
<tr>
<td>Nut</td>
<td>6</td>
<td>388</td>
<td>717</td>
</tr>
<tr>
<td>Farm supply</td>
<td>35</td>
<td>276</td>
<td>78</td>
</tr>
</tbody>
</table>

Farm supply associations, on the other hand, maintained a fairly even inventory of supplies during the year. On the average, Oregon farm supply associations still used about a quarter of a million dollars in capital to maintain their operations.

Average volume of business

Although employing the most capital, fruit and vegetable associations did not do the largest volume of business. Fruit and vegetable associations averaged about 1.7 million dollars a year whereas the volume of grain and seed associations was slightly more than 3 million dollars (See Table 2). It is important to note that grain and seed associations did almost as much supply business as those organizations classified as farm supply cooperatives. The supply volume done by grain and seed associations was important, but secondary when compared to the grain and seed part of the business.

Sources of Capital

Sources of capital were divided into three general categories of (1) member capital, (2) borrowed capital, and (3) other capital (See Figure 2).

Member capital

Member capital, the capital supplied by members of the associations, was the most important single source. Member capital, in
Member capital
Borrowed capital
Other capital

Fruit and vegetable
Farm supply
Dairy
Grain and seed
Nut

Figure 2. Important sources of capital by type of cooperative, Oregon 1951.

proportion to total capital, was a particularly important source of capital for the farm supply, dairy, nut, and grain and seed associations. It was of less importance among fruit and vegetable associations.

When the fruit and vegetable associations are excluded the ratio of net worth to total assets was:

\[
\frac{28.0 \text{ million dollars}}{45.7 \text{ million dollars}} = 61 \text{ per cent}
\]

Whenever an association is able to obtain 61 per cent of its capital from the owners it is usually considered to be in a fairly sound capital position. This is particularly true of most Oregon cooperatives because they have much of their capital in fixed assets. It is well to keep in mind, however, that the ratio is an average of 86 associations. Twenty-seven of this number were using no borrowed capital which gave them the very high ratio of net worth to total assets of 82 per cent. On the other hand, 19 associations had a ratio of net worth to total assets of less than 50 per cent.

Borrowed capital

With the exception of fruit and vegetable associations, borrowed capital was the next most important source. Three out of four
associations had some borrowed capital at the end of the fiscal year. Some associations borrowed during the peak season of their operations but the loan was repaid before the close of the accounting period.

Oregon cooperatives borrowed capital (1) for facilities (site, plant, and equipment), (2) to maintain or build inventory, and (3) to cover current operating expenses.

**Other capital**

It can be seen that the “other capital” category was an important source of capital among Oregon associations and particularly those in the fruit and vegetable business. This miscellaneous source of capital requires some explanation as to what it includes and how it fits into the capital structure of cooperatives.

Other capital is composed of two general items. First, the item “due patrons” was important among associations that pooled growers’ products and made final settlements with their patrons after the products all were processed and sold. Even when substantial partial payments or advances were made from time to time, the total amount due growers was often large. Some fruit and vegetable pools were open for a year or more. Dairy associations that paid their patrons every two weeks or once a month also had large amounts due patrons much of the time.

The item “due patrons” can logically be considered a source of capital because the patrons are assisting in the financing of the association. If the products were purchased outright from the patrons, it would be necessary to either obtain more member capital and/or larger loans. Outright cash payments to producers in many cooperatives is not feasible. The product may be sold over a long period of time. Examples are canned and frozen fruits and vegetables. The total net returns due growers cannot be determined accurately until all the inventory is sold.

A large “due patrons” account does not necessarily mean a cooperative is in a poor capital position. Although shown as a liability on the balance sheet, money “due patrons” assumes the characteristics of member or equity capital for the time it is in the association. Fruit and vegetable associations had a ratio of net worth to total assets of only 39 per cent. If nearly seven million dollars in the “due patrons” account were considered as member capital, however, the ratio of net worth to total assets would be 66 per cent. It can

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1. Actually, the physical pooling or mingling of farm products has no significance in itself. It is the pooling or mingling of sales that is important. Sales or returns are averaged, expenses are deducted, and then each grower receives his pro rata share of the net returns.
be seen, therefore, that many fruit and vegetable cooperatives with a relatively low ratio of net worth to total assets were actually in excellent financial condition.

The second item under other capital was "accounts payable," which included a considerable number of current liabilities. Almost every association had some at the close of the accounting period. Items included under accounts payable were trade accounts, accrued taxes, interest, dividends, and miscellaneous expenses.

When payment of accounts was delayed, sellers of goods and services were compelled temporarily to finance part of the associations' operations. Consequently, it is appropriate to consider accounts payable as a source of capital. It is recognized, however, that it is not good business to permit accounts payable to become too large. Accounts need to be paid as promptly as possible. Frequently, discounts on accounts are given for prompt payment or payment within a specified period.

Sources of Member Capital

Revolving capital funds

A high proportion of member capital was obtained by a revolving capital plan of one kind or another. Consequently, it is felt desirable to indicate briefly how capital is raised by this method.

Capital for the revolving fund is obtained through either the retention of the net margin\(^1\) or by retaining part of the proceeds due the patrons, or both. Under these plans, funds are obtained proportional to patronage—that is, the patrons doing the most business with the association furnish the most capital. The retained funds are allocated or credited to the patrons at the time the retainers are made. This is done each year until adequate capital is obtained or it is felt that repayment should be started. In any event the revolving feature does not become operative until repayment of these retainers is started. The oldest capital retainers are returned each year (say those taken 10 years before) and new retainers are made so that the supply of capital from this source may be stabilized. Under the revolving plan, it is possible to repay invested funds. Farmers who have retired or have moved to another locality usually are glad to be able to recover their capital investment over a period of years.

Seventy-five per cent of all member capital was in revolving funds (See Table 3). Fruit and vegetable associations obtained 79

\(^1\)In some instances, only part of the net margin is retained; the remainder is paid in cash to the patrons in proportion to their patronage.
Table 3. **Relative Importance of Sources of Member Capital, by Type of Association, Oregon 1951.**

<table>
<thead>
<tr>
<th>Type of association</th>
<th>Revolving funds</th>
<th>Preferred stock</th>
<th>Common stock</th>
<th>Membership fees</th>
<th>Other permanent capital</th>
<th>Contingency reserve</th>
<th>Other reserves and miscellaneous</th>
<th>Total per cent</th>
</tr>
</thead>
<tbody>
<tr>
<td>Fruit and vegetable</td>
<td>79</td>
<td>8</td>
<td>4</td>
<td></td>
<td></td>
<td>7</td>
<td>2</td>
<td>100</td>
</tr>
<tr>
<td>Farm supply</td>
<td>60</td>
<td>15</td>
<td>8</td>
<td>3</td>
<td>1</td>
<td>2</td>
<td>11</td>
<td>100</td>
</tr>
<tr>
<td>Dairy</td>
<td>75</td>
<td>3</td>
<td>3</td>
<td></td>
<td></td>
<td>2</td>
<td>17</td>
<td>100</td>
</tr>
<tr>
<td>Grain and Seed</td>
<td>77</td>
<td>4</td>
<td>7</td>
<td></td>
<td></td>
<td>5</td>
<td>7</td>
<td>100</td>
</tr>
<tr>
<td>Nut</td>
<td>82</td>
<td></td>
<td></td>
<td>1</td>
<td>6</td>
<td>3</td>
<td>8</td>
<td>100</td>
</tr>
<tr>
<td>Average of all associations</td>
<td>75</td>
<td>6</td>
<td>4</td>
<td>1</td>
<td>...</td>
<td>5</td>
<td>9</td>
<td>100</td>
</tr>
</tbody>
</table>

1. Includes certificates of ownership, capital reserve certificates, and building fund certificates. All of these certificates were considered to be member equities because there was no due date as in the case of outright loans. What these equities were actually called is really of minor importance.

2. This category includes such things as undivided net margins, capital surplus accounts, educational reserves, and building and/or repair reserves.
per cent of their capital through the revolving fund method, whereas the farm supply associations obtained only 60 per cent in this way. It can be seen that revolving funds were by far the most important source of member capital in all types of Oregon associations. Nine out of ten associations had a revolving fund. Most of those with no revolving funds were small organizations requiring relatively little capital.

Capital for revolving funds was obtained in one of two ways or both. First, the net margin due members was retained. Only 13 associations paid part of their net margin in cash. None of them paid out all of the net margin in cash in the year it was earned.

Second, 3 out of 10 of the associations retained part of the proceeds due patrons in order to obtain capital. All but three of the fruit and vegetable associations and all of those handling nuts followed this practice. Cooperative associations that pooled the patrons' products, and hence receipts, made wide use of this method of raising capital. Most associations that operated on a pool basis found it necessary to make some kind of a product retain, because their accounts did not show a net margin at the end of the year. In other words, pooling associations as defined in this bulletin, pooled all sales receipts,\(^1\) allocated expenses to each type of product and grade, and then paid all of the remaining revenue to the patrons less a deduction to provide capital.

**Basis for making product retain**

More than one-half of the 36 associations resorting to a product retain, as authorized by the patrons, deducted a specified amount per dollar value. In some cases the deduction was some proportion of gross receipts while in others it was a percentage of net returns. The rest of the organizations made the deduction on the basis of a certain amount, per ton, bushel, pound, or box. Three associations called their deductions a tax, because they did not expect to turn these retains back to the members.

The actual amount deducted varied considerably from one association to the other depending on capital requirements. For example, fruit and vegetable associations doing considerable processing, storing, and handling require more capital than some other types of cooperatives. The most common deduction for these associations was from 3 to 5 per cent of gross sales. In some instances the amount was 5 per cent of net returns due the growers. Two or three associations had deductions amounting to 10 per cent and even more but

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\(^1\) In all cases but one, the receipts were pooled by kind of products and grade. Pools were closed and final settlement made when all of the products were sold.
some current expenses were paid out of the funds obtained in this way.

The amount deducted on a unit basis also varied from one association to another. One association retained 2½ cents per hundredweight of potatoes; another 1½ cents per pound of butterfat; and still another $1 per ton for all grain sold.

The above examples are given to indicate the amounts deducted or retained to provide capital for the associations included in this study. Each cooperative association must decide for itself how much needs to be deducted if this method of financing is used. Some factors determining the amount of the deduction are:

- Type of product(s) to be handled.
- Services to be performed.
- Length of revolving period.
- Attitude of the members toward the association.

**Length of revolving period**

The average length of the revolving period by type of association for those actually turning over their capital is shown below:

<table>
<thead>
<tr>
<th>Type of association</th>
<th>Average length of revolving period (Years)</th>
</tr>
</thead>
<tbody>
<tr>
<td>Fruit and vegetable</td>
<td>9.3</td>
</tr>
<tr>
<td>Farm supply</td>
<td>7.9</td>
</tr>
<tr>
<td>Dairy</td>
<td>7.8</td>
</tr>
<tr>
<td>Grain and seed</td>
<td>8.9</td>
</tr>
<tr>
<td>Nut</td>
<td>11.7</td>
</tr>
<tr>
<td>Average of all associations</td>
<td>8.7</td>
</tr>
</tbody>
</table>

The average length of the revolving period for all of the associations was nearly 9 years. About one in four of the associations had a revolving period of 5 years or less. On the other hand, one in seven had a revolving period of 15 or more years.

One in three of the associations with revolving funds had not turned over any of their capital at the time the records were obtained. These revolving capital plans, on the average, were in effect about 10 years. Six of these plans had been set up for 15 years or more, but still no turnover of capital. A number of the associations in this group, however, were in operation only a few years and will, no doubt, start to revolve the funds as soon as it is feasible to do so.

A few associations had two revolving funds. One association had a short-term revolving fund and a long-term revolving fund. They hope to turn the short-term fund over about every 3 years.
The long-term fund was being revolved on a 10-year basis. Another association was turning over its short-term revolving fund every 4 years. The long-term fund was on a 14-year revolving basis.

The principle reason some associations had two revolving funds was that they felt it improved membership understanding. Members were receiving repayment of some of their deferred credits in only a few years. Yet, because of heavy capital requirements it was necessary to revolve much of the retains at a slower rate. This method of handling revolving funds seems to have considerable merit. This is particularly the case when none of the net margin can be paid in cash.

Cooperative members probably have been more critical of the length of the revolving period than any other feature of the plan. It has been difficult for them to see why net margin and/or product retains need to be made year after year and it seems none are ever repaid. No matter how justified the board of directors may be in lengthening the revolving period or indefinitely deferring the revolving feature, serious consideration needs to be given to how the members will react to such proposals. If member attitudes will be so adversely affected by a lengthening of the revolving period that some members will reduce patronage it may be best to forgo raising additional capital by this method.

Few of the Oregon associations established the revolving period of their capital funds according to any rigidly preconceived plan. Some flexibility is desirable but, of course, it should not be abused by boards of directors. The revolving period needs to be as short as possible but consistent with total capital requirements. A long revolving period is likely to have an adverse effect on member attitudes.

**Rate of interest**

Only one in five of the associations with revolving capital funds paid interest. For those paying interest, the rate was from 2 to 6 per cent. In most cases the rate was fixed by the by-laws of the association, or was the rate set when the plan was established.

An advantage of paying interest is that members are more likely to feel their investment in the association is worth something. It is common practice to receive interest on invested funds and to pay interest on borrowed funds. Therefore, by paying interest it may be easier to maintain favorable member attitudes. There is also an advantage in paying interest if all members do not furnish capital in proportion to patronage. In cases when some members may be required to provide more than their proportionate share of capital,
then it may be desirable to pay interest in order to bring about greater equity among the members.

In Oregon, the general practice has been to make retains in proportion to patronage. Consequently, there appears to be no reason why interest should be paid to adjust for inequities among patrons. The paying of a fixed rate of interest is an expense of the association that must be met every year. Some credit institutions in this area urge cooperatives not to pay interest on their revolving capital funds. The reason for this is that associations seeking credit can present a more favorable financial report if fixed charges such as interest can be held to a minimum.

**Issuance of certificates**

More than one-half of the Oregon associations issued certificates to members as evidence that certain deductions for capital purposes had been made. The others merely showed the deductions as book credits and notified the members accordingly.

The issuance of certificates serves little useful purpose. There is some expense connected with this procedure and all too often members lose the certificates before date of redemption. The mailing of a statement to the member at the end of each year is simple and helps to keep down expenses of administration.

The trend in Oregon in recent years has been toward the book credit method of accounting for member equities. This is a step in the right direction.

**Appraisal of revolving capital plans**

One of the best ways to obtain large amounts of capital from the members is through some kind of a revolving capital plan. Farmer members supply capital on an installment basis under this plan. This makes it easier than if the entire amount had to be paid in at one time. Another advantageous feature of revolving plans is that patrons finance the association in proportion to how extensively they use it. Also, currently active patrons carry much of the financial load in that the inactive, retired, or deceased members have their equities revoked out of the association over a period of years.

There are disadvantages to revolving capital plans. Perhaps the most important is that of membership understanding. As already indicated, if members do not understand the program they will be critical. Continuous work needs to be done to build and maintain member understanding.

Another problem is that of regularly revolving the capital. There are numerous examples of cooperatives in Oregon that have made relatively heavy retains during the last 8 to 10 years. There is already
some evidence to indicate that it will be difficult to pay off some of these heavy retainers according to any definite schedule. Once a revolving program is started, members expect to receive some return every year. A period of adversity may make it impossible to revolve the fund for one, two, or even several years. This may lengthen the revolving period to where some members become discouraged and drop out. This may have a "snowballing" effect causing still additional members to leave the association.

In the final analysis, the advantages of capital revolving plans far outweigh any disadvantages. Cooperatives have been turning more and more to this method because it is about the only practical way to raise large amounts of capital. It is important to keep in mind that the revolving capital fund plan is consistent with the basic principles of cooperation. True cooperatives are operated for the mutual benefit of their members. Therefore, it is reasonable to make retainers for capital purposes in proportion to patronage. A revolving capital fund is an almost automatic consequence because those individuals no longer patronizing the association (or who have changed their relative patronage) have their funds revolved out over a period of years.

It needs to be recognized, however, that under some circumstances the sale of common and preferred stock also has been used successfully to raise substantial amounts of capital.

**Stock**

Common and preferred stock are discussed together because of their relationship to each other in almost any logical plan to raise capital by this method. Oregon cooperatives that sold common or membership stock also frequently issued preferred stock.

In spite of the fact that one-half of the associations in this study sold common stock and nearly one-third sold preferred stock, only 10 per cent of total member capital was obtained in this way (see Table 3). In stock associations member patrons usually were required to purchase only one share to obtain voting privileges. Not much capital could be raised this way because the par value of a share of common stock in almost all cases was $100 or less.

In those cases where preferred stock was also issued, members and others were urged to purchase as many shares as possible. A substantial amount of capital was raised by a few associations through the sale of preferred stock. The preferred stock did not have voting privileges, and was issued by cooperative associations as a means of obtaining additional capital. The dividend rate on both preferred and common stock was between 2 and 8 per cent. Dividends per-
taining to preferred stock were cumulative in nearly all cases. Two-thirds of the associations with common stock paid no dividends at all.

Five cooperatives in this study issued stock as evidence of a product retain or retention of net margin. When stock thus issued is revolved, this financing plan assumes the characteristics of the revolving capital fund method as a means of raising capital.

The sale of common and preferred stock is an excellent method of raising capital if sufficient funds can be obtained. Farmers have demonstrated many times, however, that they are not inclined or able to provide large amounts of capital outright for their cooperative associations. Farmers have been turning more and more to providing capital on an installment basis by means of retains of one kind or another. These retains usually are revolved after a number of years, with the oldest retains being paid first.

It is important to keep in mind that members almost always need to furnish some capital outright when the association is first organized and established. Retains cannot be made until the association is in operation. Consequently, it is necessary at first to sell stock, collect membership fees, or sell some kind of certificates of ownership or equity. Once the association is operating, additional capital may be raised by the revolving capital fund plan. This has been the practice followed by most Oregon cooperatives.

Membership fees

About one-half of the Oregon associations were nonstock and consequently resorted to the collection of membership fees from their member patrons. Membership fees were an insignificant source of capital amounting to only 1 per cent of all member capital. Such fees were an unimportant source of capital because the amount of the fee was nominal in most cases. More than one-half of the Oregon associations had a membership fee of $5 and none was over $50.

It is recognized that a small membership fee makes becoming a member easy. However, consideration also needs to be given to raising some capital. Boards of directors and policymakers in cooperatives, therefore, may wish to give more emphasis to requiring a considerably higher membership fee as one of the requirements for becoming a member. Membership fees of $25 or $50 per member are reasonable and would provide some of the capital so essential to successful operation.

Other permanent capital

Cooperative associations with other permanent capital obtained funds from the members and issued capital certificates, certificates
of ownership, or building fund certificates. Irrespective of what the certificates were called, interest at the rate of between 4 and 5 per cent was paid and there was no due date as in the case of an outright loan.

This method was of minor importance as a source of capital for associations in this study. Less than 1 per cent of all member capital was obtained through the sale of these certificates. Six associations were able to raise some of their total capital requirements by this method.

**Contingency reserves**

Five per cent of all member capital consisted of contingency reserves. Two-thirds of the Oregon cooperatives had no contingency reserves at all.

In almost all associations the size of the contingency reserve was small in relation to total capital requirements. It has been difficult to build contingency reserves because capital has been needed to maintain or expand current operations. It may be increasingly difficult to build reserves in the future because all unallocated reserves are now taxable at prevailing corporation rates. Reserves allocated pursuant to a mandatory, legally binding obligation to accounts of patrons are not taxable.

**Other reserves and miscellaneous**

This final category includes building and/or repair reserves, educational reserves, capital surplus accounts, and undivided net margins. These miscellaneous sources of capital consisted of 9 per cent of total member capital (See Table 3). Dairy cooperatives had 17 per cent of their capital in this miscellaneous category because a number of these associations, as well as some of the others, show their net margin as being undivided at the end of the accounting period. While most of this undivided net margin was to be allocated and placed in the revolving capital fund there was no way to determine the exact amount. Consequently unless net margins for the current year were already allocated and precisely accounted for, they were placed in this miscellaneous category.

**Borrowed Capital**

Oregon marketing and supply cooperatives had borrowed 18.3 million dollars as of 1951,\(^1\) which amounted to 26 per cent of all capital employed. Nearly 42 per cent of all borrowed capital was

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\(^1\) As already indicated some of the records were taken in 1950 and 1952; in those cases the data pertain to the end of that fiscal year.
used by fruit and vegetable associations. The next largest users of borrowed capital were the dairy associations with 23 per cent. Although there were 35 farm supply associations included in this study, they used only 13 per cent of total borrowed capital. Farm supply associations borrowed less than some of the other types because their total capital needs were not as great. There are difficulties, however, in financing a rapidly moving inventory such as general farm supplies in contrast to grain, cheese, or packed fruit.

Thirty-eight associations out of the 119 included in this study were using no borrowed funds at the close of their accounting period.

**Source of loans**

The source of loans was divided into four categories: (1) bank for cooperatives, (2) commercial banks, (3) individuals, and (4) others. The Spokane Bank for Cooperatives provided Oregon marketing and farm supply associations with 48 per cent of all borrowed capital. Twenty-three associations had loans from the Spokane Bank for Cooperatives. Commercial banks were next in importance with 28 per cent, followed by loans from individuals with 18 per cent. Six per cent of all loan funds were obtained from other sources.1 (See Figure 3).

Source of loans has practical significance to cooperative associations only when some lenders supply adequate capital at more favorable terms and interest rate than some of the others. In Oregon, the weighted average interest rate for loans from individuals was 4.43 per cent; whereas, the average for commercial banks and the bank for cooperatives was 3.72 and 3.25 per cent respectively.2 The rate of interest charged by commercial banks compared favorably with that of the bank for cooperatives on relatively large loans. Commercial banks, however, charged a higher rate of interest on small loans than did the bank for cooperatives. The interest rate paid individuals was consistently higher than that of other sources of credit.

The average size of loan by source is shown below:

<table>
<thead>
<tr>
<th>Source</th>
<th>Amount</th>
</tr>
</thead>
<tbody>
<tr>
<td>Bank for cooperatives</td>
<td>$232,286</td>
</tr>
<tr>
<td>Commercial banks</td>
<td>102,982</td>
</tr>
<tr>
<td>Individuals</td>
<td>40,799</td>
</tr>
</tbody>
</table>

Commercial banks and individuals made more loans than the bank for cooperatives but the loans of the latter averaged much

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1 In almost all cases other sources of capital consisted of funds borrowed from other cooperatives, and purchase of machinery and equipment on contract from manufacturers or their representatives.

2 According to the t test, the differences between these means were all statistically significant.
larger. It is apparent that most cooperative associations requiring relatively large loans borrowed from either the bank for cooperatives or commercial banks. As a rule, cooperatives were not able to borrow relatively large amounts of capital from individuals even when the interest rate was between 4 and 5 per cent and in some cases more. A number of small and new cooperatives borrowed from their members simply because they could not borrow elsewhere.

**Term of loans**

With the exception of fruit and vegetable associations, all types of cooperatives found it necessary to borrow more long-term capital than either short or medium term (See Figure 4). Any capital borrowed for more than 3 years was classified as a long-term loan. Most long-term loans were for considerably more than 3 years; a large number made by the bank for cooperatives or commercial banks were for either 5 or 10 years. In no case did the bank for cooperatives or commercial banks loan funds for a period longer than 10 years. On the other hand, long-term loans from individuals ranged from 3 to 25 years.

All loans for 6 months to 3 years were classified as medium-term. Almost one-third of all borrowed funds were medium-term.
loans. The term of two-thirds of all funds borrowed by fruit and vegetable associations, however, was from 6 months to 3 years.

When the term of the loan was less than 6 months it was considered to be a short-term loan. Twenty-five per cent of all funds borrowed fell in this category. Most cooperatives required some short-term capital. With the exception of three cooperatives, all relatively large short-term loans were obtained from either the bank for cooperatives or commercial banks. It is difficult to borrow relatively large amounts of short or medium capital from individual members as the funds are needed. Commercial lending agencies are usually in a better position than private lenders to perform this service efficiently and promptly provided the association has established a satisfactory credit rating.

**Purpose of loans**

Facility and commodity loans were of about equal importance (See Figure 5). Many cooperatives of all types found it necessary to borrow capital to build or purchase plant and to obtain equipment. The same was true also with respect to commodity loans for all except grain associations. Fruit and vegetable processing associations
with long pooling periods needed large amounts of capital to carry their inventory and make advances to the growers. Dairy associations manufacturing cheese often needed to borrow while the inventory was in the curing and storage rooms. Nut associations frequently have pooling periods of a year or more which means some inventory is carried for a long time. Farm supply cooperatives also used considerable borrowed capital to build and maintain inventory. This was particularly true of those supply associations in the farm machinery business.

Almost one-fifth of all borrowed funds was used to meet current operating expenses. Fruit and vegetable, dairy, and grain and seed associations used operating loans largely to meet seasonal expenses such as labor and supply costs. For example, fruit and vegetable associations needed much additional labor during the canning and freezing season. Funds were borrowed frequently to meet their payrolls and were repaid when part of the product was sold. During the flush season of the year, cheese factories added additional labor. The same was true also of grain and seed associations during the harvest season.
Age of association and rate of interest paid

Cooperatives less than 25 years old paid a much higher rate of interest for operating and commodity loans than that paid by associations 25 or more years old (see Table 4). Cooperatives that have survived for a quarter of a century usually have established a more satisfactory credit rating than the newer associations, which is evidenced by the important differences in interest rates paid by the two age groups for operating and commodity loans. There was no appreciable difference in rates paid by the two age groups for facility loans. Facility loans were nearly always secured by a mortgage covering all land and buildings. Unless members of both new

<table>
<thead>
<tr>
<th>Purpose of loan</th>
<th>Age of associations</th>
<th>Operating interest rate</th>
<th>Commodity interest rate</th>
<th>Facility interest rate</th>
</tr>
</thead>
<tbody>
<tr>
<td>Operating</td>
<td>25 or more years old</td>
<td>3.25</td>
<td>3.17</td>
<td>4.24</td>
</tr>
<tr>
<td></td>
<td>Less than 25 years old</td>
<td>4.64</td>
<td>4.52</td>
<td>4.42</td>
</tr>
</tbody>
</table>

1 The differences between these interest rates are statistically significant.

and old associations provide a reasonable part of the funds desired for facility modernization or expansion, they are not likely to be able to secure a loan for this purpose. This may account for the fact that the interest rate was about the same for facility loans in both age groups.

The relatively high interest rate that the newer associations must pay on operating and commodity loans has increased the cost of doing business during a period when it is extremely important to render good and efficient service in order to hold the membership and make some growth.

Size of association and rate of interest paid

Cooperatives doing less than a million dollar business annually paid interest on borrowed funds at a higher rate than those doing more than a million dollar business (see Table 5). Small associations must pay a relatively high rate of interest simply because they are small.
Table 5. AVERAGE RATE OF INTEREST PAID BY COOPERATIVES FOR BORROWED CAPITAL, BY SIZE OF BUSINESS, OREGON 1951.

<table>
<thead>
<tr>
<th>Annual volume of business</th>
<th>Purpose of loan</th>
<th>Interest rate</th>
<th>Interest rate</th>
<th>Interest rate</th>
</tr>
</thead>
<tbody>
<tr>
<td></td>
<td>Operating¹</td>
<td>Commodity¹</td>
<td>Facility¹</td>
<td></td>
</tr>
<tr>
<td>More than one million dollars</td>
<td>3.52</td>
<td>3.44</td>
<td>4.04</td>
<td></td>
</tr>
<tr>
<td>Less than one million dollars</td>
<td>4.80</td>
<td>4.56</td>
<td>4.56</td>
<td></td>
</tr>
</tbody>
</table>

¹The differences between these interest rates are all statistically significant.

Also, many of these small associations were relatively new. Unless they are the result of merger or consolidation, most cooperative associations start small. It usually takes a number of years to achieve some growth and become a stable business institution in the community.

**Age of association and need for borrowed capital**

The ratio of funds borrowed to total assets for 33 associations in operation 25 years or more was 14 per cent, whereas the ratio was 22 per cent for 85 associations less than 25 years old. The ratio of funds borrowed to total assets for the 35 associations 15 years of age or less was 30 per cent.¹

The above data show that as cooperatives grow older there is less necessity to resort to borrowed funds as a source of capital. There are exceptions, however. Some cooperative associations, irrespective of age, always seem to need a relatively high proportion of borrowed capital. This may be the result of poor membership understanding, lack of vision on the part of the directors, and/or poor management. The relationship between age and ratio of funds borrowed to total assets in this study was quite clear—the majority of the older associations needed to borrow less than the newer associations.

**The Ideal Capital Structure**

The problem of obtaining capital would be reduced to a minimum if members were able to provide all of the funds needed for site, facilities, equipment, and normal operating needs. It is assumed that this member capital would be either interest-free or furnished the associations at nominal cost as is now the case in most instances. It is also assumed that all member capital would be of a permanent nature—that is, the associations would not have to refinance from

¹When the average ratio of funds borrowed to total assets for the associations 15 years of age or less was compared with the average ratio of those 25 years or older the difference between these two means was significant.
time to time to stabilize their capital needs. Revolving capital funds logically can be considered as permanent capital if a long-range, consistent management policy of these funds is established.

Under an ideal capital structure, it usually is desirable to borrow seasonal capital requirements even though the members are in a position also to provide this capital.¹ There are a few cooperatives in Oregon in such excellent financial condition that they hardly ever borrow any funds. During several months of the years, however, they carry excessive cash bank balances. In most cases it would be better to distribute some of these funds to the patrons and borrow during the peak season. The patrons probably would be able to employ this additional capital productively on the farm. Associations that are able to obtain all of their facilities, equipment, and normal operating capital from the members will not encounter any difficulty in borrowing for seasonal needs at a reasonable rate of interest.

¹There are a number of small cooperatives in Oregon that operate exclusively as fresh fruit shipping organizations. The picking and shipping operation takes only a few weeks each year, which means the associations are inactive the rest of the year except for possibly overhauling facilities and assembling packing supplies inventory. In these cases it is desirable to borrow nearly all operating capital. Otherwise, relatively large cash bank balances would be carried for 9 or 10 months each year. This capital management policy applies, of course, to other types of cooperatives that also are active only a few months each year.