



Grower Cooperatives (Co-ops)

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Introduction

Cooperatives have historically been utilized to market wholesale quantities of produce in Kentucky. In the early 2000s, as many as four grower co-ops in Kentucky were actively marketing tomatoes, melons, sweet corn, cabbage, bell peppers, pumpkins and other crops to wholesale buyers. By 2006, however, produce marketing by grower co-ops had largely disappeared from Kentucky's produce industry, with only one co-op still operating as growers found other ways to market produce. The involvement of co-ops in marketing produce from Kentucky has since been limited.

Cooperatives remain a potential form of business organization for specialty crop growers located in a similar geographic area. Producers interested in exploring the cooperative business structure can investigate resources available from the Kentucky Center for Agriculture and Rural Development (KCARD), which is recognized by USDA Rural Development as a cooperative development center.

This publication will highlight the general principles behind a co-op and identify potential benefits for produce growers.

WHAT IS A COOPERATIVE?

A cooperative is a business owned and controlled by the people that patronize and use its services. Unlike other businesses, a cooperative is not profit-driven. The purpose of a cooperative is to meet a common need among its members and to provide greater benefits to its members such as increasing income levels for members or providing access to markets that they cannot access individually. *The goal of the cooperative is to provide its members with services and goods that would be economically impossible for members to obtain individually.*



However, just because a cooperative is not profit driven does not mean that it is a non-profit or exists to lose money. In fact, cooperatives operate in a manner to earn a profit, but co-ops strive to keep net income low by providing products and services at or near cost. The profits generated by the co-op are allocated to its members based upon their patronage or use of the co-op's services; i.e., the farmer who markets the most produce through a produce co-op is allocated the largest share of the profits.

This is the first of three USDA "principles of cooperatives" and is referred to as the **user-benefits** principle.² The purpose of a cooperative is to provide and distribute benefits to members on the basis of their use of the services of the co-op. Cooperatives depend on a group of producers joining forces and, in return, obtaining bargaining power. Additional benefits include cost savings associated with producing and/or processing larger quantities. For example, in Kentucky, cooperatives have not only existed to market members' products, but also to purchase packaging and other inputs in bulk quantities, allowing substantial discounts to members.



The second principle is the **user-owner** principle. This means that the coopera-

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tive's members actually own the co-op. If a cooperative owns a building, for example, that building's ownership is spread across the entire co-op membership. Because the members are actually the owners of the co-op's assets, co-ops do not exist to give their members "something for nothing." Members are responsible for providing some of the start-up funding and providing working capital by using its services. This means that, if expansion is being considered, the co-op and its owner-members are to be the first source of potential funds.

There is much evidence that the most successful cooperatives begun in the past 30 years have involved substantial personal financial commitment by their members. A group operating a co-op that is unwilling to fully dedicate their financial and production resources to this enterprise should reconsider structuring as a cooperative. Lack of member commitment to this enterprise's business operations frequently results in undercapitalization of the business and is one frequent reason for failure.

Finally, co-ops are **user-controlled**. This means that cooperatives are democratically controlled businesses where each member-owner has an equal vote in how the operation is run. Voting rights are tied to membership status (one member, one vote) and not based on the level of investment. Most often, the members elect a board of directors from among themselves to oversee the operation of the co-op. By selecting leaders who are committed to the original goals and ideals, members exercise the power to dictate how their cooperative is run.

Members of all cooperatives should be careful to monitor and take interest in how their co-op is doing business. Serving the needs of its user-owners, after all, is the primary reason that a co-op exists.

CONSIDERING COOPERATIVES

A cooperative is not the only way for farmers to create new market opportunities or to meet a mutually shared unfilled need or solve a problem shared among a group of producers. Still, interest in co-ops continues to be strong in American agriculture. This is especially true among producers exploring new and alternative enterprises for their farms. In Kentucky, the Lexington Farmers Market is organized as a co-op; cooperatives can be of benefit where there is no established common market for certain products or where a task is too daunting for an individual producer. Co-ops can also be helpful when marketing meats, cheese and other products processed from raw farm commodities. A co-op can help the farmer retain ownership and earn revenue beyond just selling a commodity like milk, livestock or grain.

Business Planning

The success of new cooperative ventures will depend heavily on careful study of the activities pursued prior to making major investments into operations and facilities. Before an actual business plan is written, a feasibility study will need to be conducted. This tool can then be used to determine whether the business is feasible, and whether or not a business plan should be prepared. A thoughtful, forward-looking business plan is a key success factor for which there is little substitute.

For further information on conducting a feasibility study, please refer to *The Farmer's Cooperative Yardstick: Conducting a Feasibility Study for Marketing Cooperatives*. Business planning assistance for producer groups is available through KCARD. This center is staffed by people experienced in co-op development. KCARD can help make financial projections and ask the hard questions that can contribute to the business' success.

Member Commitment

A cooperative venture needs strong leadership and commitment from its members. This can be especially critical in the early stages of formation. The feasibility study and business planning process provides a design for how the cooperative should be run. They provide a guideline for the resources necessary to make the venture successful. Members need to commit to provide these resources on an ongoing basis or be prepared to struggle.

A group of CSA farms or a farmers market, for example, that identifies benefits of becoming a cooperative, must realize that co-ops take considerable time and effort to establish. Members will need to be as attentive to paperwork, accounting, administration, and legal issues as they are to facilities, advertising, and other items that have more visible — but not necessarily more important — benefits.

Market Research

Member education about the marketplace is another key success factor required both in the start-up phase and on an on-going basis. Board members need to be committed to keeping in touch with the changing customer, as well as with new technologies, since these can potentially impact the cooperative's way of doing business.

Many cooperatives are formed for the purpose of marketing members' goods. Since the co-op members own the business, they need to be actively interested in seeking out markets and shoring up existing ones. Capable employees and management personnel can help guarantee success, but in the end, it is the members-owners who need to be interested in the markets the co-op is entering.

Management

Strong management must be in place to oversee the day-to-day operations of any cooperative effort. Investment in capable people is every bit as critical as investing in equipment. Farmers considering a move into a cooperative effort should be prepared to pay for the right personnel to make their venture a success. Board members should monitor these costs carefully. Many co-ops are surprised by failure because they do not know their costs.

Labor and labor management are especially critical issues for agricultural cooperatives. Not only do they need managers with production and marketing expertise, but co-ops also need to identify and manage the labor needs. Labor is a major expense category for any business, and how it is managed can make or break a business' financial success. Board members should hire the best-trained manager they can find, and create the best possible working conditions for that manager. They should not interfere in the day-to-day operation of the co-op, but, in conjunction with the membership, board members should determine operating policies and ensure that these policies are carried out.

Cooperation can open many doors of opportunity for our farmers across Kentucky. The process of making cooperation work, however, should be carefully thought through. Demand for new products and for services that our farmers can provide is expanding all over the world. New market development partnerships with other farmers that secure access to special equipment and personnel will be one way for our farmers across the Commonwealth to play a role in the design of our future food and fiber system.

¹“Cooperative” defined in W. David Downey & Steven Erickson, *Agribusiness Management*, New York: McGraw Hill, 1987, p. 455.

²Further discussion of these principles may be found in the USDA Bulletin *Co-ops 101* (USDA Rural Business Cooperative Service, Cooperative Information Report 55, April 1997, Revised 2012 and 2016) <https://www.rd.usda.gov/files/publications/CIR55.pdf>

SELECTED RESOURCES

- Is A Cooperative the Right Choice? (Kentucky Center for Agriculture and Rural Development, 2018) <https://www.kcard.info/news/2018/10/5/is-a-cooperative-the-right-choice>

- The Farmer's Cooperative Yardstick (University of Kentucky, 1987 & 1998)
 - Agricultural Cooperatives – How They Fit in the American Free Enterprise System, AEC-42 <http://www.ca.uky.edu/agc/pubs/aec/aec42/aec42.pdf>
 - How to Start a Cooperative, AEC-43 <http://www.uky.edu/Ag/apes/materials/aec43.pdf>
 - Farmer and Consumer Cooperatives Structure and Classification, AEC-44 <http://www.ca.uky.edu/agc/pubs/aec/aec44/aec44.pdf>
 - Conducting a Feasibility Study for Marketing Cooperatives, AEC-45 <http://www.ca.uky.edu/agc/pubs/aec/aec45/aec45.pdf>
 - Understanding Cooperative Terminology, AEC-47 <http://www.ca.uky.edu/agc/pubs/aec/aec47/aec47.pdf>
 - Boards of Directors for Farm Cooperatives: Powers – Responsibilities – Liability, AEC-49 <http://www.ca.uky.edu/agc/pubs/aec/aec49/aec49.pdf>
 - Your Roles as a Co-op Member, AEC-50 <http://www.ca.uky.edu/agc/pubs/aec/aec50/aec50.pdf>
 - Role of the Co-op Manager, AEC-51 <http://www.ca.uky.edu/agc/pubs/aec/aec51/aec51.pdf>
 - Financing Agricultural Cooperatives, AEC-52 <http://www.ca.uky.edu/agc/pubs/aec/aec52/aec52.pdf>
- Kentucky Center for Agriculture and Rural Development <http://www.kcard.info/>
- Business and Cooperative Programs (USDA Rural Development) <https://www.rd.usda.gov/about-rd/agencies/rural-business-cooperative-service>
- Co-ops 101: An Introduction to Cooperatives (USDA, 2016) <https://www.rd.usda.gov/files/publications/CIR55.pdf>
- Cooperation Works (National Cooperative Business Association) <http://www.cooperationworks.coop>
- Rural Cooperatives Magazine (USDA Rural Development) <https://www.rd.usda.gov/publications/rural-cooperatives-magazine>

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