



## **What are Cooperatives?**

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There are many structures today that individuals can use to operate a business to provide a product or service to others. A sole proprietorship is formed by an individual who serves as the sole business owner. The business owner is responsible for the liability and earns the profits from the business. Partnerships are formed by more than two people whom share the liability of the business or the liability is placed on one person within the partnership. Corporations are another business structure usually formed by a group of people with a specific interest or focus. There are four types of corporations: non-profit, subchapter C, subchapter S and subchapter T (cooperatives). Four characteristics that make business structures differ include: who owns, who controls, who uses and who profits.

Cooperatives are unique to other corporations because they have three distinguishing principles: user-owned, user-controlled and user-benefited. The user-owned principle signifies that the users are the ones who are financing the cooperative by transacting business. User-controlled relates to the Board of Directors of the cooperative that makes the decisions. The Board of Directors is elected by the members of the cooperative and serve as the link between the membership and the manager. User-benefited indicates that the members are the ones profiting from the cooperative because patronage refunds are returned to the members based on the amount of business they conducted with the cooperative. The uniqueness of cooperatives is that the customers, owners, patrons and members could be the same person. Customers buy and sell, owners are providing capital and wanting returns, patrons are getting patronage refunds distributed from the cooperative's profits and members maintain the democratic control of the cooperative and its operations. The fact that one person can play these four roles simultaneously makes defining these roles important to the cooperative's success. The manager and the Board of Directors must be aware that there are different needs among the individuals within the cooperative. Education becomes a big part of making sure the manager, Board of Directors and members understand the operations and functions of the cooperative structure.

### **Why start a cooperative?**

A group of individuals must see a benefit that a cooperative can provide to put in the effort and time commitment that it takes to establish a cooperative. Some of the objectives that the cooperative must provide prospective members are:

- *Improved bargaining power* - the cooperative can leverage its position more than individual producers could do alone to obtain contracts and penetrate markets.

- *Reduced costs* – volume purchase of products/services can reduce the cost to the individual producer and increase their profit margins. The cooperative can take advantage of bulk purchasing and pricing strategies.
- *Obtain products/services that otherwise would be unavailable* – the cooperative provides a product/service that producers could not get by themselves. The collaborative effort of producers to gain access to a product/service that is not currently available makes a cooperative more viable and successful.
- *Obtain market power or broaden market channels* – the cooperative pools resources and provides more marketing power because of the large quantity of product that can be provided. The cooperative can also establish marketing channels to be utilized by its members.
- *Improve product/service quality* – the cooperative members might have been using a product/service, but were not happy with the quality. The cooperative can also provide an opportunity to increase the value of the products being sold by the members through value-added processing efforts.
- *Increase income* – the cooperative eliminates some of the middlemen in the marketing process by using the cooperative. The cooperative gives back patronage refunds to increase the profits or reduce the costs that the member incurs.

### **Steps to forming a Cooperative**

The formation process of incorporating a cooperative takes a strong group of focused people that are outgoing and motivated. Most groups have a leader or person that assumes the lead role in the group and coordinates the other members to keep the ball rolling. The Ohio Cooperative Development Center (OCDC) personnel are contacted to meet with the group and explore the alternative business structures at the initial meeting. OCDC has developed relationships with other organizations like the USDA Rural Development and the Ohio Council of Cooperatives. These relationships provide access to legal, tax and finance professionals that can help the group proceed in the cooperative development process. There is a simple outline that walks the groups through the cooperative development process, but the group can use cooperative development professionals to assist them as they proceed towards incorporation.

1. *Steering Committee* - the Steering Committee members are usually elected from the initial group of potential members and provide the coordination for the rest of the group. The Steering Committee meets frequently and serves as a communication channel back to the group to report findings and progress.
2. *Survey* – the Steering Committee conducts a survey of the group to determine interest, need and use of the proposed cooperative. This shows what industries the business might enter and the volume of business the cooperative can expect to conduct. The survey also indicates the willingness of individuals to join the cooperative and provide financing for its operations. Members must be willing to invest in the business because they provide a large source of financing for the cooperative.

3. *Analyze the markets* – conducting an analysis of the markets is important to gain the members’ support to continue the process towards incorporation. The members are interested in the potential markets and the possibility of the cooperative entering those markets.
4. *Business Plan* – the business plan is a step that some cooperatives tend to skip or overlook. The business plan goes into detail explaining the cooperative’s focus and operational practices, including a financial analysis. This document is essential to get support of the existing group and necessary to attract new members.
5. *Commitment* – the group of prospective members must now vote to confirm their commitment to the cooperative and their approval that they are comfortable with the process and analyses so far. Changes in the Steering Committee can be made at this time if the group feels a need to replace someone on the existing committee.
6. *Legal Documents* – the incorporation of the cooperative is confirmed by filing Articles of Incorporation with the Secretary of State. The Articles outline the purpose of establishing the cooperative. The By-Laws are also composed and show how the cooperative intends to carry out the purpose outlined in the Articles. The By-Laws are an internal document for the cooperative, but provide the necessary direction for the Board of Directors and manager. Any other legal documents that the cooperative desires can be written at this time, including marketing or membership agreements.
7. *Approve documents and elect Board of Directors* – the membership must approve the legal documents and are responsible for electing the Board of Directors for the cooperative. The Board handles the accounting, expending, bonding and insuring issues facing the cooperative as it begins operation.
8. *Implement Business Plan* – the Board elects officers from within and establishes committees for the cooperative. Committees are established to address certain sections or processes outlined in the business plan. Other committees are established as the needs are identified that necessitate committee work. The business plan is now used to secure financing for the cooperative.
9. *Hire Manager* – the Board hires a manager for the cooperative that makes the day-to-day decisions for the cooperative and its members. It’s important that the manager has the skills and abilities to run a successful cooperative and understands the cooperative business structure.
10. *Board of Directors acquires facilities* – the Board must acquire facilities for the operation of the cooperative, if needed. Depending on the scope or focus of the cooperative, facilities might not be a need for the cooperative at this time.

A cooperative is a business that is formed by dedication and commitment from a core group of individuals who have a common need. The cooperative provides a mutual benefit to the members that could not have been provided individually. Identifying that common need is an

important part in creating cohesion among the members of the cooperative and making it successful.