

THE ROLE OF COOPERATIVES IN THE U.S. ECONOMY

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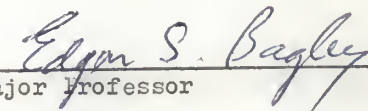
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INTRODUCTION

The word cooperation is used in a variety of meanings. It is a Latin word (co means with and operate means to work) and means literally to work together. Webster (New International Dictionary) defines the verb cooperate as 'to act or to operate jointly with another or other'.

Perhaps the broad usage of cooperation includes working together in which the individual works not for self alone but also for the good of the social body of which he forms a part. The motto 'each for all and all for each' may be accepted as characteristic of cooperation.¹

'Economics' says Professor Marshall in the opening words of his 'Principles', is a study of mankind in the ordinary business of life', and cooperation is one way of conducting certain parts of this business.²

Like all human impulses cooperation has been institutionalized in many ways. In the family first, then the clan, the tribe, the city state, the nation. The cooperative business of present times represents the institutionalization of the principle and impulse of mutual aid in the day-to-day economic activities of the man.³

Owners of cooperative business are rendering all sorts of services to themselves and to their communities in the U.S. to-day. They bring babies into the world, they bury people, light up farm houses, spread fertilizer, service automobiles, market farm crops. They also run super markets owned by consumers, conduct wholesaling of groceries for independent grocers, drill oil wells, mine phosphate

¹ Filley, H.C., Cooperation in Agriculture, 1929, p.1.

² Fay C.R., Cooperation at Home and Abroad, 1920, p.1.

³ Voorhis J., American Cooperatives, 1961, p.14.

rock, grow seeds, grind coffee and manufacture machinery. They pool people's savings in credit unions, cooperative insurance companies and cooperative farm credit institutions. They conduct health plans of every shape and size in an effort to make the marvels of modern medicine available to people generally.⁴

Cooperatives are a legally recognized form of private enterprise, some being established as long ago as 1810. Membership in cooperatives is entirely voluntary and open to any one who can use their services. Cooperatives are not incompatible with free enterprise but a force strengthening free enterprise. They promote more wide-spread ownership of business and help to boost the real income of the people, thereby increasing consumer demand and stimulating employment. Cooperatives lead away from regimentation and make for the exercise of individual initiative and responsibility. They are a pure form of democracy in the economic field. Cooperatives are a potent factor in retarding the march of this country toward a government-manipulated economy.⁵

Statement of the Problem

The purpose of the report is to examine the role of cooperatives in Agriculture, Rural electrification, housing, credit, health and other fields of American life and economy. The discussion will be limited to the above fields in examining the basic principles and

⁴Ibid, p.14.

⁵Rural Electrification News, June-July 1950. p.5.

issues involved in cooperatives and in appraising their role in the economy of the U.S.

Methods and Materials

The method followed in preparing this report is to study the published material available at the Kansas State University Library, the material obtained through the Department of Economics and Sociology and from other sources and to select information pertinent to the subject; and then to analyse it seeking to arrive at an evaluation of the role of cooperatives in the U.S. economy.

DEFINITION OF COOPERATIVES

When people join in a mutually helpful undertaking, that is cooperation. Cooperatives are business organizations formed by people to serve their own needs. A technical definition of cooperatives is expressed as follows: 'A cooperative enterprise is one which belongs to the people who use its services, the control of which rests equally with all the members, and the gains of which are distributed to the members in proportion to the use they make of its services'.⁶

A cooperative society is a voluntary association in which the people organise democratically to supply their needs through mutual action, and in which the motive of production and distribution is primarily service profit a secondary one.⁷

A cooperative is an association for the purpose of joint trading, originating among the weak and conducted always in an unselfish spirit,

⁶Wieting C.M, The Progress of Cooperatives, 1952, p;3.

⁷Fay C.R, Cooperatives at Home and Abroad, 1920,p.7.

on such terms that all who are prepared to assume the duties of membership share in its rewards in proportion to the degree in which they make use of their association.⁸

Federal and State statutes consider cooperation to exist only in organizations which meet the particular criteria for cooperatives as set up in such statutes. These statutes have tended to complicate the definition of the term. A simple and proper definition of a cooperative under the decisions of American courts may be the following.⁹

"A cooperative is a legal entity organised and operated for the purpose of furnishing at cost goods or services to its patrons or its patron-members".¹⁰

WHY COOPERATIVES CAME INTO THE AMERICAN ECONOMIC SCENE

Americans have long resisted monopoly. Yet there have been forces operating that have been conducive to its development such as technological improvements leading to mass production. Government has endeavoured to curb monopolies where possible and has regulated public utilities, but government regulation in a democracy may not be as effective as an action springing directly from the people. Consumers and producers have taken the initiative themselves and are responsible for one of the most vital curbs to monopoly - the cooperative associations.¹¹

⁸ Ibid, p.5.

⁹ John C. Satterfield, Cooperatives in our free enterprise system, an address on March 9, 1961, pp.5-6.

¹⁰ Ibid, p.6.

¹¹ Daggar I.W, Cooperation as a Bulwark of Private Enterprise, American Cooperation, 1947, pp.362-363.

In agriculture, cooperatives were formed because they were needed to provide goods and services not available otherwise or not available on satisfactory terms. Some times farmers for example, sent cream to market by selling to a cream station which shipped to a large creamery. When the dairy industry increased in the area and there was enough cream to make it possible for a creamery to operate, businessmen with capital did not always recognise the opportunity to make a profit and therefore did not start a plant. If farmers wanted the service, they provided the capital to establish a cooperative creamery.

Another example might be that of a town with only one creamery. With no competition farmers might not be getting the services expected. The cooperative could put into operation the necessary competition.¹²

HISTORICAL OUTLINE

The actual practice of cooperative enterprise by agricultural and industrial workers goes back for many centuries. This type of enterprise originated with guilds of the Middle Ages which were cooperative efforts of the early industrial employees to alleviate the conditions under which they worked. Thereafter, cooperative enterprise continued on the continent and in Great Britain in many forms until the birth of the modern cooperative business organization through the Rochdale Equitable Pioneers' Society in Rochdale, England in 1844. In the meanwhile, there was a parallel but entirely

¹²Ibid, p.363.

separate development of cooperative enterprise in America dating back to the earliest colonial days. Pioneers cooperated in clearing land, building homes and constructing roads. There were community husking bees, log rollings, threshing rings, beef and cheese rings, and many other cooperative activities. These were informal, but gradually definite organizations developed. As early as 1780 farmers organized societies to purchase pure bred cattle and to make community drives of live stock to distant markets.¹³

Gradually as the farmers' production expanded and the farmers markets increased and became more distant, cooperative techniques were developed both in the marketing of agricultural products and the purchase of supplies. Formal organizations developed, one of the first being the "Associated or Cooperative dairying" at Goshen, Connecticut, about 1810. These gradually spread to the Midwest as illustrated by the organization of dairy cooperatives by Wisconsin farmers in 1841. During the next fifty years various types of cooperative enterprises spread throughout the entire United States, the principles of cooperative organizations and operation gradually emerging by trial and error. By 1860, cooperative organizations existed in most of the agricultural areas of the country, and in 1865 Michigan passed what is regarded as the first statute recognizing the cooperative method of selling farm products and purchasing farm supplies.¹⁴

¹³John C. Satterfield, The Cooperatives in our free Enterprise System, p.2.

¹⁴Ibid, p.3.

The modern cooperative had its origin in the group of twenty eight weavers who banded together in Rochdale, England, in 1844, to overcome the desperate straits they were in as a result of combination of high prices of goods they needed and low wages in their industry. It is said that these weavers pooled about \$140 as their initial capital and formed the first consumer cooperative. When the Rochdale weavers formed the Rochdale Equitable Pioneers' Society, they formulated seven basic principles of cooperative endeavour: (1) open membership, (2) democratic control, on the principle of "one member one vote", (3) limited interest on capital, (4) trading on the basis of cash, (5) patronage refunds, (6) political and religious neutrality and (7) promotion of education. These have come to be the generally accepted principles of cooperatives. However, it has long been recognized that all seven of the Rochdale principles need not be present for an organization to be properly considered a cooperative.

The national Grange, officially known as "The order of Patrons of Husbandry" was founded in 1867, and in 1874 the Grange sent one of its officers to Europe to study the cooperative enterprises which had developed there. An early writer on cooperation says "The great contribution of the National Grange was the formulation and distribution in 1875 of a set of rules for the organization of cooperative stores".

These rules were based on those of the twenty eight weavers of Rochdale. By 1876 the National Grange had established more than 20,000 local Granges and in twenty six states local granges

participated in selling and buying for members on a cooperative basis.¹⁵

The federal government and all of the states have repeatedly recognized the value of farmer cooperatives. Basic federal legislative recognition of the desirability of encouraging farmer cooperatives includes the exemption from federal income tax in 1913, the protection of such cooperatives from the provisions of the Clayton Act in 1914, the authorization of organization of cooperatives as against certain provisions of anti-trust laws by Capper-Volstead Act in 1922, and the creation of the Federal Farm Board in 1929. Each of fifty states in the U.S. has authorized the organization of cooperatives under special statutes, most of which contain features designed to encourage agricultural producers to form cooperatives.¹⁶

Since the turn of the century the importance of farmer cooperatives to the agricultural economy of the United States has rapidly increased. The number of farmer cooperatives has increased from 3,099 in 1915 to the all time high of 12,000 in 1930 with a gradual decline, following the reduction in the number of farms and farmers, to 9,731 in 1957-58. The number of membership in farmer cooperatives has increased from 651,186 in 1915 to 7,485,779 in 1957-58. In the year 1915 the business done by farmer cooperatives amounted to

¹⁵Ibid, p.4.

¹⁶Loc.cit.

\$310,313,000. During the 1957-58 season, the gross value of farm products marketed, farm supplies handled and receipts for services performed by cooperatives amounted to approximately fourteen billion dollars, and the total net volume, after eliminating duplication resulting from inter-association business, amounted to almost 10.7 billion dollars.¹⁷

ROLE OF COOPERATIVES

To many, cooperation has appealed as a means of solving some of the difficult economic problems which confront the U.S. National economy. More enthusiastic exponents of cooperation hope for the day when cooperation will dominate economic activities. Others look upon the movement as antagonistic to the present economic order and would relegate it to a subordinate role.

Among the essential elements in the system are its economic institutions including, among others, the institution of private property. Private property rights both in producers and consumer goods are basic features of the capitalistic economy. Over long history, Americans have accepted the doctrine that the property which an individual creates or acquires belongs to him. The right to private property is a means of compensating the individual for activities he has undertaken and is an incentive to the full use of his productive ability.¹⁸

The profit motive is another generally recognized feature of the system. Economic activity in the capitalistic system is actuated by the quest for private gain. It is on this motive that the capitalistic economy depends to stimulate individuals to put forth their greatest productive effort. Production and distribution of goods and services are characteristically organized and performed by private individuals

¹⁷Ibid, p.5.

¹⁸Koller E. Fred, Cooperative in a Capitalistic Economy, J.F.E., 1947, p.1133.

or privately owned organization. In the cooperative plan of organization similar stress is placed on the individual initiative and control. It is in this setting of economic doctrines and economic institutions that American cooperation is being developed.¹⁹

The cooperative may be viewed as a form of business organization owned and controlled by its member patrons for the rendering of services for their mutual benefit as patrons. Basically cooperatives seek economic gains for their members and patrons. The basic aim of every business undertaking, regardless of its form is gain for some individual or individuals.

If cooperative business is examined for the similarities it bears to capitalistic enterprise, a predominance of likeness may be seen. Cooperative business accepts the fundamental institutions of capitalism including the right of private property, the right of contract, inheritance, and the right of private enterprise with its emphasis on the dignity and importance of the individual. Even in the matter of motivation the differences are a matter of form rather than basic principles.

Cooperatives are like ordinary business organizations with respect to many aspects in their daily business operations. They pay interest on the capital, at the going rate of interest, that is used in carrying the business activities. Regarding the hiring of labor, cooperatives adopt usually the same ways and means as the ordinary firms.

¹⁹Ibid, p.1134.

Cooperatives employ managers and compensate them on the quality of service they render. Ordinary business firms depend for their success on efficient business methods and the cooperatives follow the same.²⁰

Cooperatives differ from ordinary business or corporations in the following way: A corporation serves the people - generally the non-owner customers by providing goods and services which they need. A cooperative on the other hand serves only its members at cost. The policy of a corporation is decided by the board of directors who are elected by the stockholders at the annual meeting, whereas the basic policy questions of a cooperative are decided at general meetings of members, who also elect the board of directors. The business of the corporation is managed by its president, secretary, treasurer and other officers employed by the board of directors to carry out its decisions. The judgment of the management is not subject to control by stockholders. In a cooperative the board of directors is responsible for efficient management and employs necessary personnel to carry out adopted policies. In a corporation each stockholder has as many votes as the number of voting shares of stock he owns. Voting "by proxy" is permitted. In a cooperative each member generally has one vote in meetings of members, irrespective of the number of shares of stock he owns. The stock holders are the owners of the corporation whereas member patrons are the sole owners of the cooperative business. In a corporation the stock holders supply the

²⁰ Ibid, p.1136.

needed capital by subscribing for the corporation's stock, divided into shares but in a cooperative the member patrons supply needed capital. Part of the money needed may also be borrowed from members or others. The returns on capital investment by share holders in a corporation, in common stock, are not limited but in a cooperative invested capital gets only fixed interest. In a corporation dividends are paid to stock holders in proportion to the number of shares held by each whereas in a cooperative net margins are returned to the members in the form of patronage refunds paid in the proportion to the amount of business transacted by each member.²¹

It has been charged by some that cooperation is socialistic and that extension of the movement is a step toward the creation of socialistic state. A brief examination of the doctrines of socialism reveals some fundamental differences. Socialism represents ownership and control of the basic means of production and distribution by the state and for the benefit of society as a whole. A feature of socialist doctrine is its emphasis upon a more equitable distribution of income and wealth. Socialism implies subordinate of individual to the state, and places the interest of the general public above private interest. It would replace competition as the regulative force in economic society and substitute control by government.²²

In contrast with the doctrine of socialism, cooperatives oppose ownership and control of the means of production by the state. Cooperatives favor and improve distribution of income. However, cooperative distribution according to patronage rests on the principle of productive contribution which is in accord with the principle of

²¹ Abrahamsen and Scroggs, Agricultural Cooperation, 1957, pp. 79-81.

²² Koller E. Fred, Cooperative in a Capitalistic Economy, J.F.E., 1947, p. 1138.

distribution commonly accepted in capitalistic society. It is in contrast with the socialist goal of equal distribution or on the basis of need. In general cooperatives recognize, along with capitalistic business, that expansion of the business functions of the political state creates an instrument which in the end would destroy cooperatives or would allow them to exist only as an aim of the state and under its control. Thus a maximum of agreement may be found in their underlying principle and foundations and it may be said that cooperatives are an integral part of the capitalistic economy just as are ordinary corporations, partnerships, and individual proprietorships. Cooperation is a phase of capitalistic free enterprise system. A better understanding of these concepts by both cooperators and ordinary business men should serve to lessen the bitter controversies which often develop between these groups and should promote a greater tolerance.²³

The primary role of cooperatives in a free enterprise economy is to overcome some of the defects and limitations of that economy. Important among these are imperfections in the competitive process which interfere with the allocation of resources, in accordance with consumer preferences. A fundamental objective of the cooperative plan of business is to improve competition and to enlarge the area in which the competitive pricing mechanism is effective.

In performing their important role in the economic system, successful cooperatives provide leadership in supplying their

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Ibid, p.1138.

patrons with goods and services on a more efficient and economical basis than they have been provided by non-cooperative business.²⁴ Cooperatives have taken the lead in the introduction of improved techniques of production and distribution which have served to reduce costs and improve the returns of their members. Among these techniques are standardization of production of various commodities produced on farms and standardization of packages and grades. Quality improvement programs and improved methods of handling often have been sponsored by cooperatives. Efforts to standardize market quotations and terms, of sales and activities designed to widen market information available to producers have been accomplished where cooperatives have taken the lead. In many cases these and other improvements gradually were adopted by competing firms and thus the benefits also have been available to others than members of cooperatives.²⁵

Consumer and supplying cooperatives have been always making an effort to improve the quality of merchandise by certain techniques such as testing of the products in laboratories, putting a descriptive labelling on the products and providing useful information to the patrons about the use of merchandise. They have aimed to reduce selling costs by substituting consumer education in place of advertising and salesmanship.²⁶

By bringing about the horizontal combination of producers, cooperatives have played a distinctive role in achieving important economies. Horizontal combination has been a means of effecting an optimum scale of enterprise including optimum scale of plant, optimum scale of management and other services. In this way small scale farmers who could not perform certain marketing and purchasing activities efficiently on an individual basis have been brought together to obtain the advantages of size. Horizontal combination has been instrumental in reducing irrational competition characterized by excessive duplication of services and

²⁴Ibid, p.1138.

²⁵Ibid, pp.1138-39.

²⁶Ibid, p.1139.

facilities in many local and terminal markets.²⁷ Cooperatives, by entering these situations, have contributed, significantly in improving the allocation of resources in the American economy.²⁸

Another important role which cooperatives have played in the U.S. economy is that of counteracting and breaking down the elements of monopoly which have developed in business. One of the important reasons why a free market economy fails to function optimally is the prevalence of monopolistic pricing. The capitalistic system depends on the price mechanism to direct the activity of individuals into the productive channels. Cooperatives may exert an influence in breaking down monopolistic pricing and thus help maintain competition in the free enterprise economic system of the U.S.²⁹

From early history cooperatives have taken a stand against monopolistic practices in private business. In the Granges period of 1870's cooperatives were formed and directed toward breaking up monopolistic conditions of that period. Contemporary cooperatives likewise have been established with the avowed purpose of providing competition in fields in which protection against monopolistic conditions has been deemed desirable. The entry of cooperatives into the petroleum business, into manufacture of fertilizers and farm machinery are illustrations of efforts to provide competitive safeguards against monopolistic elements.³⁰

From time to time some cooperatives have deviated from the traditional stand on monopoly and have resorted to monopolistic methods themselves. One may sympathize with this point of view of cooperators

²⁷ Loc.cit., . . .

²⁸ Loc.cit.

²⁹ Ibid., p.1141.

³⁰ Loc.cit.

who desire to use the size and power of their organization to achieve monopoly gains, since they have suffered serious abuses in some markets in the past. Some have concluded that it is either too slow, or next to impossible, to break down the monopoly position of certain buyers in the market by normal competitive method, and hence have turned to build up their own monopoly power to challenge the opposing forces in the market. The reaction is to meet power with power. But public resentment to such an economic structure is growing and cooperatives face the prospect of reactions.³¹ Cooperatives have not developed organizations with the size and power of many large national corporations and labor unions. Furthermore, since these organizations do not ordinarily control supplies in their respective fields, they are not in a position to manipulate price by withholding supplies.

The preponderant majority of cooperatives over the country recognize that the sound, constructive role of cooperatives in the capitalistic economy is that of competitive pace maker and not monopolistic manipulation. The more progressive cooperatives recognize that it is their function in the economy to stimulate competition by maintaining high standards of efficiency and service. Even a small but efficient cooperative occupying a strategic spot in the market may be highly influential as a competitive pace-maker. To perform their role in the economy most effectively, cooperatives themselves

³¹Ibid, p.1142.

need the stimulation of private business competition. Successful cooperatives owe a great deal to their competitors.³² Efficient competitors present a continuous challenge to cooperative management to try to render better service at lower costs. The reciprocal competitive action of efficient cooperatives and efficient private business firms is a most desirable goal for the economy. It is a means of assuring a more effective and productive economic system than one in which government regulation plays a larger part.³³

Thus cooperatives provide a means of complementing and strengthening the capitalistic economy at its weakest points. While the cooperative is clearly not a panacea for all the ills of capitalism, it does perform a positive role in the free enterprise economy by aiding it to achieve a better allocation of resources, higher total production, and a wider distribution of income.

Cooperation is the antithesis of communism because the collective action involved is for individual gain. This is in sharp contrast to the communistic system, in which the goods produced are owned collectively or by the state. The desire for individual gain or profit motive makes one to join cooperative.

Through its executive committee the National Association of Manufacturers recognized cooperatives as a part of the U.S. system of

³²Ibid, p.1143.

³³Ibid, p.1144.

private enterprise. It said in a generalized statement that the cooperative is a form of business enterprise that enables a group of individuals, partnerships or corporations to combine together for purposes of producing or buying or selling a commodity or service. Individuals join together to buy life insurance through a mutual insurance company. People who have money put their funds in a mutual savingsbank. Farmers join together to buy the goods they use in production or to sell the things they grow. All of these are cooperatives and are legitimate forms of private enterprise. The cooperative form of doing business has been used by many groups. As a result there are many kinds of cooperatives, both farm and non-farm, and these do business in several ways. Some carry on at actual cost with no funds left for building reserves or for distributing the patronage dividends.³⁴

Cooperation is a bulwark to all private enterprise. Every farmer is a capitalist and, like other capitalists, he is seeking to increase the returns from his business by reducing the costs and expenses incidental to the operation of his farm, and by marketing his agricultural commodities so as to receive maximum returns. The farmers of America believe in the individual ownership of farms and in the individual ownership of commodities produced on the farms. The farmers of the U.S. constitute still the largest single class of capitalists in the country. Even tenant farmers are capitalists through the ownership by them of machinery tools and live stock.³⁵

³⁴Duggan I.W., Cooperative as a Bulwark of Private Enterprise, American Cooperation, 1947, pp.358-360.

³⁵Ibid, p.358.

Any business in a competitive economy can survive only so long as it is filling a need. If the records of failures and discontinuance of businesses are reviewed, it may be seen that these occur both in cooperative and other business. This too, is a part of the workings of the capitalistic system which tends to weed out inefficiency. A business must succeed in meeting the interests of the public; otherwise it will not survive, be it cooperative or non-cooperative. In the American system of private enterprise if a job is not being done well by a cooperative or any other type of business, competition forces it to the wall.

The two types of private business have existed side by side practically since the beginning of large scale business in this country. Cooperatives handle a small portion of agricultural products but the proportion that they handle is sufficient to exert a considerable influence on the economy.³⁶

CLASSIFICATION OF COOPERATIVES

With reference to the nature or type of services or goods furnished, cooperatives may be classified as follows:

1. Cooperatives organized for the purpose of providing financial aid to their members at cost, such as credit unions, mutual building and loan associations, health, accident, medical care and compensation companies, and mutual life insurance companies.
2. Cooperatives organized for the purpose of furnishing services at cost, such as the marketing and processing of agricultural products, the rendition of public utility functions

³⁶Ibid, p.364.

such as electric, water and telephone service, and the rendition of various types of service to members such as the services furnished to about one thousand news papers by the Associated Press and to seventy four rail roads by the Railway Express Agency; services to trade associations and the like.

3. Cooperatives organized for the furnishing of goods at cost, such as manufacturing, purchasing and consumer cooperatives and wholesale buying groups.³⁷

SOME SPECIFIC EXAMPLES OF COOPERATIVES

Rural Electric Cooperative

Rural Electric cooperation is a community enterprise through which the farmers provide electric services to themselves with the help of the Rural Electrification Administration. A Rural electric cooperative is an incorporated association of neighboring farmers and other rural residents, organized democratically for the purpose of supplying electricity to its members at the lowest cost made possible through mutual self help.³⁸ It is a private non-profit enterprise, locally owned and managed, and incorporated under state law. It is owned by the members it serves and each member has one vote in the affairs of the cooperative regardless of the amount of electricity he uses.³⁹

In 1911 the National Electric Light Association submitted a

³⁷Salterfield J.C., The Cooperative in our Free Enterprise System, p.6.

³⁸Rural Electrification News, February, 1947, p.8.

³⁹The Story of the REA's first 25 years, U.S.D.A. Miscellaneous Publication No.811, p.14.

report on rural electrification at its annual convention. This report revealed that few farmers outside irrigation districts were using electricity. The utility executives who heard the report were impressed but they were not sold on the idea that line extensions to farmers would pay. In the early 1920's a growing number of farm leaders and others were starting to insist on rural electrification. But the price of electricity was very high and hence the chief problem was how to get electricity at a reasonable price so that most farmers could afford to get it.⁴⁰

One man deeply concerned about the high cost of rural electric service was an electrical engineer named Morris L. Cooke. He assembled his data to prove that rural electrification was practical. In 1934, Cooke reported that the achievement of widespread rural electrification would depend on the federal governments' assuming active leadership.

In response to these findings and pressure from farm leaders the Rural Electrification Administration was created by an executive order of the President on May 11, 1935. Cooke was appointed as the first Administrator of R.E.A. He thought that the large power companies would carry the rural electrification work with financial aid of government but he was disappointed with the poor response from power companies. In 1936 the Rural Electrification Act was passed. This act clearly stated that R.E.A. loans should be given to non-profit

⁴⁰Ibid, p.5.

organizations like cooperatives.⁴¹

In 1937 the R.E.A. drafted a model law for states called Electric Corporation Act. This uniform act gave the cooperatives ample powers to organize and build cooperatives. By 1940 a total of twenty three states had given the green light to rural electric cooperatives. The hard work of organizing the rural electric cooperatives generally fell to a handful of local farm leaders. In the beginning farmers were not universal in their demand for electricity. R.E.A.'s staff played a great role in convincing the farmer and getting him to establish rural electrification cooperatives.⁴²

As rural line construction proceeded at a faster pace private utility companies were spurred by the competition to build their own lines in rural areas. In some cases this new building led to bitter feelings between cooperatives and commercial companies. Frequently commercial construction took the form of spite lines.⁴³

Rural electric cooperatives were organized and functioned according to the general pattern of consumer cooperatives; follow the Rochdale principles and have been accepted by the cooperative movement, but they have a number of distinguishing characteristics. Many cooperatives were brought into existence by R.E.A., all have been guided and supervised by it. They are often thought and spoken as R.E.A.

⁴¹Ibid, p.10.

⁴²Ibid, p.15.

⁴³Spite lines are lines built almost overnight after cooperative was organized and which paralleled the proposed cooperative lines.

cooperatives.⁴⁴ Their lines are called R.E.A. Lines. R.E.A.'s influence pervaded all of them. The interesting thing about the R.E.A. movement was the way in which the initial stimulus came from government to be followed later by the development of local interest and activity.⁴⁵

The people who were called upon for leadership were pretty much the same, no matter how the cooperative was organized. Where the organized farm groups were strong, they took a leading part, especially the farm bureaus. When the agricultural extension program was well developed, county agents were generally active, in some cases serving as directors. In general it has been the middle income progressive farmers who have taken the lead. About 80 per cent of the membership of a typical cooperative consists of farm consumers. The remainder is made up of stores, gas stations, summer hotels, schools and churches, government camps, small extracting manufacturing or processing industries and their workers.

People form cooperatives for their own protection as consumers of essential goods or users of essential services. In the case of R.E.A. cooperatives rural people originally joined them as the only means available of obtaining electric service at the rates they could afford. At the start of 1960, R.E.A. had approved loans to 1053 electric systems in forty six states, Puerto Rico and the Virgin Islands. Of

⁴⁴The standard sign for example reads "REA Coop".

⁴⁵The story of the R.E.A.'s first twenty five years, U.S.D.A. Miscellaneous Publication, no.811, p.72.

these 952 were cooperatives. The balance consists of fifty public power districts, twenty seven other public bodies and twenty four commercial electric companies. During R.E.A.'s first twenty four years there were only two foreclosures and ninety six systems retired their indebtedness to R.E.A.⁴⁶

At the start of the fiscal year 1960, ninety eight per cent of the farms in U.S.A. had electricity.⁴⁷ Electric cooperatives range in size from a twenty four member system in Arizona to one in Louisiana with more than 28,000 members. These cooperatives have revolutionized the whole American farming and eased the drudgery and monotonous life of the American Farmer.⁴⁸

Rural Telephone Cooperatives

In many areas of the country rural telephone service has been very poor. Commercial companies in this field have had so many other expansion opportunities which would increase their profits that they showed little interest in the rural problem. Congress passed legislation which made rural telephone cooperatives feasible. In some instances rural communities had been poorly serviced with small, independent, inadequate exchanges. These exchanges had been unsuccessful in persuading larger commercial companies to take them over.

⁴⁶Ibid, p.22.

⁴⁷Statistical Abstracts of U.S., 1961, p.634.

⁴⁸U.S.D.A. The Story of R.E.A.'s first twenty five years, Miscellaneous Publication, no.811, p.23.

However, groups armed with the new legislation began making plans to form cooperatives and take these exchanges over. Almost immediately existing firms voiced their opposition to the cooperatives and stepped forward to buy and improve the rural exchanges. Here, we see the stimulating and prodding function in action. In these situations the cooperative was never actually formed. Its purpose was accomplished. Duplication of facilities for duplication's sake alone is not a justifiable role for cooperation.⁴⁹

Supply Cooperatives

Farmers have been using cooperatives for more than a hundred years to help them with the purchase of their farm supplies. Pooling of orders for coal, salt, twine, seed, fertilizer and feed has long been practised by farmers. The Grange and Farmers Alliance had as one of their major aims the establishment of cooperative purchasing agencies.⁵⁰

The growth of purchasing cooperatives came rather late in the United States.⁵¹ In 1913 only two per cent of the business of cooperatives was in purchasing. Yet in 1950 it accounted for twenty five per cent of all the business done by farmer marketing and purchasing cooperatives. World War I marks the time when farmers were faced with economic conditions which made it necessary for them to pool their buying power in purchasing cooperatives. Large scale regional cooperatives began to spring up during the early twenties with the aid of

⁴⁹ Cooperation as a part of Private Enterprise System, a paper by Kohls R.L., American Cooperation, 1955, p.698.

⁵⁰ Wieting C.M., The Progress of Cooperatives, 1952, p.17.

⁵¹ Ibid, pp.21-22.

the Farm Bureau, the Grange and the Farmers' Union. Today Farm Purchasing Cooperatives are major suppliers of petroleum, fertilizer, feed and seed. Mixed feeds in 1950 accounted for more than forty five per cent of the total value of supplies handled by cooperatives for farmers.

Fertilizer was one of the early products handled by cooperatives. Today many regional associations have their own fertilizer plants and distribution systems. Farmer education on the use of high analysis fertilizer has been carried on by cooperatives. Seed is a necessity for good farming. It is the aim of the cooperatives to secure for farmers high quality seed at reasonable cost. Farm supplies of all kinds are now sold by many cooperatives. These include farm machinery and equipment, steel products, electrical farm appliances, paint, insecticides and sprays. Many of these regional supply cooperatives have joined in national associations to help them in the manufacture and purchase of supplies.

Many of the larger cooperatives today provide a variety of services in both the marketing and purchasing field. The supply cooperatives make it possible for farmers to purchase their farm supplies at a better price.⁵² High quality is assured by the research and care which goes into the selection of the product to be sold.

⁵²Ibid, p.23.

Cooperatives in the Oil Business

Cooperatives dealing in petroleum provide an excellent example of the volume of business done and the extent to which farmers depend upon cooperatives. About a fourth of the dollar volume of supply cooperatives is in petroleum.⁵³ The first cooperative oil refinery arose in the late twenties on the plains of Kansas. It was followed by others in various parts of the country. Today cooperatives supply from oil well to bulk plant and filling station about eighteen per cent to twenty two per cent of the petroleum used on farms in the U.S. In the states of the upper Middle West the percentage is considerably higher.⁵⁴

Most of the products sold by the cooperatives to their members and customers at retail come from their refineries. In 1957 cooperatives sold 1,957,000,000 gallons of liquid petroleum fuels; cooperative refineries turned out 1,873,000,000 gallons. The product of some 2,000 cooperatively owned oil wells is ultimately sold to consumers through some 2,700 bulk plants and 2,000 filling stations.⁵⁵

Cooperatives distribute through their own pipe lines, trucks, wholesale and retail outlets 2.2 per cent of the nation's total supply of petroleum products. They refine about 1.6 per cent. Their weak link is that they supply less than fifteen per cent of their refinery capacity from their own wells. For balanced and reasonably secure operation they need about fifty per cent. Even with this small portion

⁵³Ibid., p.20.

⁵⁴Jerry Voorhis, American Cooperatives, 1961, p.104.

⁵⁵Ibid., p.105.

of the great industry's business, the cooperatives have accomplished much. They have returned in patronage refunds to farmers and to farm income and to rural towns and their income tens of millions of dollars.

The greatest benefits, however, have been indirect and intangible. By 1959 the index of prices paid by farmers for necessary supplies and inputs had risen to 275 from the base period of one hundred for 1910-1914. But for the two commodities where cooperatives are strongest--petroleum and fertilizer--the index was only 175 and 152 respectively.⁵⁶

Consumer Cooperatives

The average American knows little as yet about consumer cooperatives. The obvious reason is that there are not as yet enough cooperative stores and super-markets in the growing cities to draw the attention of many people. In rural areas the situation is different. Many kinds of cooperatives are known and recognized as integral parts of American Rural life.⁵⁷

Exactly when the first consumer cooperative grocery store was organized in the U.S. is not known. According to accepted cooperative history it could not have been before 1844, because in that year the "first" true consumers cooperative was born in Rochdale, England. But probably the first one in America was not many years after that.⁵⁸

In the years of self-sufficiency on the prairies in the 1870's and 1880's there came a wave of cooperative organizations, largely fostered by the Granges movement. Many of these were consumer-goods and farm supply cooperatives similar to the cooperative "general

⁵⁶Loc. cit.

⁵⁷Ibid, p.153.

⁵⁸Ibid, p.158.

store" operations of the present century. They aimed at giving the prairie farms family something to say about the cost of their necessities of daily living. At least one of these Granger founded cooperatives is still doing business at Cadmus, Kansas.⁵⁹

In the early years of the twentieth century attempts were made by some labor unions, notably the United Mine Workers, to set up consumer cooperative stores for their members but none of these was very successful.⁶⁰ The years of the Great Depression brought forth a new interest in consumer cooperation which expressed itself in many ways, but most of the consumer cooperatives started during this period lasted no more than a few years. There were however, exceptions to this pattern of failure. Where groups of people from Northern Europe had come to America and congregated in certain communities. They frequently brought with them a tradition of cooperative success in the "old country". Particularly this was true of Scandinavian and above all, of Finnish people. In some New England communities, in the Bay area of California, in the Head of the Lakes area around Lake Superior, and a few other places, strong, solid consumer cooperative stores were established early in the twentieth century and are growing steadily to this day. One of the oldest consumer goods cooperative in America is called The New Cooperative Company and was founded in 1908 in South-east

⁵⁹ Loc. cit.

⁶⁰ Ibid, pp.159-160.

Ohio largely by Czech farmers and Czech miners.⁶¹

Marketing Cooperatives

Primary producers have been exploited through much of the history of mankind because, largely, other people or firms with much bargaining power have done all the buying and selling, processing and manufacturing of primary products. The way to end such exploitation is for primary producers to organize their own agencies to do their own selling and buying and at least some of the processing and manufacturing of their crops.⁶² "In the latter half of the nineteenth century the Grangers spearheaded formation of both marketing and consumer cooperatives among distressed farmers".⁶³

There were in 1960 nearly 7,000 marketing cooperatives in the United States. These cooperatives market, annually, for their farmer members fourteen major categories of products. The annual value of these products, after allowing for duplication, is about ten billion dollars. Marketing cooperatives handle about a quarter of all U.S. farm products at one or more stages in their progress from farm to consumers table. These cooperatives are by far the largest single type of cooperative business in the United States if measured in the dollar volume of business.⁶⁴

⁶¹Ibid, pp.159-160.

⁶²Ibid, p.79.

⁶³Ibid, p.80.

⁶⁴Ibid, pp.82-83.

Cooperative Credit Unions

There were about 199 credit unions in the United States in 1921. In 1960 the number reached to about 20,000. The membership in these credit unions was more than eleven million with the assets reaching to five billion dollars mark. More than a thousand new credit unions are being organized in this country every year. Credit unions provide about eight per cent of all instalment credit in this country.

The origin of the credit union, like that of other cooperative institutions, is buried in the sands of very ancient times, for such institutions are as old as mutual aid among people. Probably, institutions similar to credit unions existed in India and some other countries for centuries, but Germany is the birth place of modern cooperative credit unions.⁶⁵

By the end of 1959 the United States had 19,800 credit unions with a membership of 11,300 and assets of \$4,382,000,000 (mostly members' shares), and outstanding loans to members of \$3,700,000,000.⁶⁶

The principle of a credit union is simple. In this a group of people having common ties and interests keep control of their own savings and their own credit and use them for mutual benefit of the group.⁶⁷

⁶⁵Ibid, p.114.

⁶⁶Ibid, p.117.

⁶⁷Loc.cit.

The largest credit union in the United States is that of Detroit teachers. A modest percentage of its \$20,000,000 of assets is being loaned to its members to enable them to build, as a cooperative, several beautiful apartment buildings in which they themselves will live. The majority of credit unions in the United States, however, are organized among the employees of industrial and commercial concerns and frequently with the benevolent sponsorship of the employing company.⁶⁸

Credit unions can be useful and constructive influences in any society but there are natural and unavoidable limits to the scope of their activities and effectiveness. People will probably never put the bulk of their savings into credit unions. Nor can credit unions provide the kind of large scale financing which modern industry, including cooperative industry, demands. All the assets of all credit unions in the United States amount to less than half the assets of any one of the largest New York or California banks. Less than three per cent of all personal savings are in credit unions, though this percentage is rising steadily.⁶⁹

Cooperative Farm Credit

In frontier days when land was cultivated extensively little capital was necessary for farming and the credit needs of farmers were on a short term basis. Such credit needs were met in large part by local merchants who sold to the farmers on open account and who themselves borrowed from local banks. This was one of the chief source of agricultural credit from earliest colonial times upto the last quarter of the nineteenth century. Meanwhile short term credit

⁶⁸ Ibid, pp.118-119.

⁶⁹ Ibid, p.122.

declined in relative importance as the farmers felt the necessity for more and more mortgage credit and intermediate credit. One of the chief early sources of mortgage credit was the life insurance companies, which were providing substantial portions of the farmer's mortgage credit by the end of the civil war. Another important source of farm mortgage credit was the commercial banks.⁷⁰

The first federal action in providing credit facilities for agricultural purposes was in 1916 through the Federal Farm Loan Act. The next federal action in providing permanent credit facilities for agricultural purposes was the establishment of the Federal Intermediate Credit banks. But for many years the facilities of the Federal Intermediate credit banks were utilized only to a very limited extent.

Banks for Cooperatives: Like many cooperatives, the banks for cooperatives, sprang from need. Farmers could not obtain needed credit for their cooperatives from commercial banks as the banks were having troubles in 1933. During 1932, five per cent of the cooperatives failed due to lack of capital and hence were in need of sound financing. Recognizing this need congress passed the Farm Credit Act of 1933. It included provisions for setting up the thirteen banks for cooperatives, as a method of making it possible for farmers to help themselves.⁷¹

⁷⁰ Seba Eldridge & Associates, Development of Collective Enterprise, 1943, pp.290-291.

⁷¹ Farm Credit Administration, Banks for Cooperatives, A Quarter Century of Progress, June 1960, p.2.

The banks for cooperatives were designed to supplant the work of the defunct Federal Farm Board which had been established by the agricultural Marketing Act of 1929 and were financed with what remained of a \$500 million revolving fund which had been established by the Act of 1929.⁷²

Although the thirteen banks were originally capitalized by the Federal government, it was not their intent or purpose, as agents of self help to farmers, to loan government money permanently. When it became feasible in 1950 they began obtaining much of their loanable funds through the sale of debentures. From the start the banks for cooperatives gained a reputation among borrowing cooperatives. These banks offer a complete loan service on a sound constructive business basis.⁷³

Production Credit System: The production credit system provides short term agricultural credit on a semi-cooperative basis in competition with commercial banks and cattle loan companies. They make short term loans to farmers with a maturity upto three years although most of the loans run for a year or less.

As early as 1923, congress attempted, by means of the federal intermediate credit banks, to make the borrowing power of the federal government available to farmers in the matter of intermediate term credit. That attempt was successful only to a limited extent. The production credit set-up was created as an addition to the intermediate

⁷²Seba Eldridge & Associates, Op.Cit.p.299.

⁷³Farm Credit Administration, Op.Cit.p.324.

credit banks by means of which farmers could tap the bank's funds through cooperative credit organization.⁷⁴

The Governor of the Farm Credit Administration was directed by congress to establish twelve production credit corporations, one to be located in each federal land bank city. Each corporation in its credit district was to assist farmers in organizing and then to supervise and direct, to the extent necessary, production credit associations composed of farmer borrowers. Each corporation divided the territory in its farm credit district into prospective production credit association districts and then proceeded to contact farm leaders in order to acquaint them with the new production credit set-up and assist in the formation of associations. At least ten farmer members eligible to borrow were required before an association could be chartered.⁷⁵

Production credit associations have been given a chance to become truly cooperative credit institutions. The association actually makes the production loans, and nearly all decisions regarding them must be made in the association office. Each association is allowed to accumulate its own surplus funds and in this way is given a strong incentive to build a sound financial structure. The production credit system seems adopted to a so-called middle class of borrowers.⁷⁶

⁷⁴Troelston, E.S., Principles of Farm Finance, 1951, p.169.

⁷⁵Ibid, p.170.

⁷⁶Ibid, p.175.

Federal Land Banks: The Federal Farm Loan Act provided that the U.S. should be divided along state lines into twelve districts by the Federal Farm Loan Board and a federal land bank established in each district. Each bank was to have a capital stock in the amount of \$750,000 and the secretary of the treasury was directed to subscribe for the government capital stock in the banks to the amount not taken by the private investors. Actually, the investing public bought little stock in the banks. The officers of a bank were to be elected by its board of directors, who are seven in number, and were to consist of a president, a vice president, a secretary and a treasurer.

The Federal Farm Loan Act authorized the establishment of a national farm loan associations through which a federal land bank could loan to farmers but left the initiative in forming the associations to farmers who wished to obtain funds from a federal land bank. These associations were formed rapidly.

No dividends have been paid to the government for stock it owned in the federal land banks. The Government has encouraged the banks to build up surplus and reserve funds. In fact when a bank had the funds the government insisted that some of its capital stock be retired. Thus by 1930, the government held very little stock in the federal land banks. However, it was forced to subscribe to additional stock during the depression, but now this has all been repaid.⁷⁷

⁷⁷ Troelston E.S., Principles of Farm Finance, 1951, pp.69-80.

The bank can make loans in cases in which first mortgages on farms are given as security. The banks can make loans upto sixty five per cent of the normal agricultural value of lands and buildings. The length of mortgage term may vary from five to forty years, but the policy of the banks is to make long term loans. Interest and principal payments are required to be made either annually or semi-annually. The usual practice seems to be for repayment to be made in semi-annual instalments.

A borrower is required to be a farm operator. The farm used as security for a loan is required to be an adequate-sized or economic unit. The purpose for which a loan is obtained is a matter of much concern to the banks. Loans may be made to purchase land, equipment, fertilizer or live-stock, to build buildings and construct other improvements, and to pay existing debts.⁷⁸

Cooperative Housing

Good homes in good neighborhoods are considered to be a need of middle and lower income families in the United States. Some fourteen million American families are living in sub-standard or slum homes today. And many families have escaped this by spending far more in purchasing their homes than they could safely afford. The houses that have been built have been mostly luxury housing. Few of them cost less than \$15,000 while it is a rule of thumb that a family should have an income of at least \$7,000 in order to safely afford a home of

⁷⁸Ibid, pp.81-83.

that expense. But only a minority of American families have income of \$7,000 a year. The construction industry is building the houses at prices at prices which are often out of the reach of an average income family. So some people had the idea of building the kind of homes at prices that the average income family could afford, by organizing a cooperative of the home needers to build homes and enable the members to own their own homes after they are built.⁷⁹

A whole section of New York's lower east side has been changed from a slum into a beautiful community of neighbors by this method. The cost of this housing is twenty five per cent to thirty per cent less than, comparable, commercially built housing. Families with incomes as low as \$4,000 can afford such costs for their homes without incurring burdensome debt.⁸⁰

Cooperative housing got its start in the United States in 1926. It began with a decision on the part of some members and officials of the Amalgamated clothing workers Union. The result of the pioneer effort was the Amalgamated Housing Corporation, builder and sponsor of an apartment building on the border of Van Cortlandt Park in New York City. The Amalgamated project turned out to be a brilliant success. Not only did it provide good housing at considerably reduced cost, but created a true neighborhood in the midst of America's largest city. The maintenance costs have been held to half what they are normally in rental housing or in publicly owned housing.⁸¹ "By 1959 there were some three hundred cooperative housing projects in the U.S.,

⁷⁹ Jerry Voorhis, American Cooperatives, 1961, p.43.

⁸⁰ Ibid, p.43.

⁸¹ Ibid, p.44.

Cooperation in Health Plans

In 1913 the International Ladies Garment Workers Union in New York City set up for its members the first union health center in U.S. History. It was a place where union members money was used to provide out-patient care for any ambulatory ailments any of them might suffer. It and scores of centers like it are in operation to-day.⁸³

Membership is open to any one who wants to join; control is by membership, each exercising one vote; and the plan is operated on a non-profit basis. No patronage refunds are paid to members when the year's operations show a surplus. This is a distinction between the health plans and all other types of cooperatives. But ethically, health plans cannot be operated for the financial gain of any one, not even their members. If there is a surplus, then either monthly subscription charges are reduced, or new services are added, or doctors and other staff people are better compensated or the money is put into a fund for a new wing on the clinic.⁸⁴

Besides these "pure" cooperative plans there are a wide variety of others. In all of them a group of people have decided to pool their need for health care, to pay for it as a group with sick and well paying the same amount, and to arrange with groups of doctors to provide the health care they need.

In its early years the medical society black-listed all the doctors who became associated with Group Health associations and

⁸³Ibid, p.28.

⁸⁴Ibid, p.29.

denied the use of hospitals to the doctors and their patients. A five year law suit, finally decided by the U.S. Supreme Court, held the medical society to be engaged in monopolistic practices, and required re-admission of Group Health Association doctors to the society and restoration of hospital privileges.⁸⁵

Practically all of the development of cooperative health plans have taken place since World War II. It is a young movement born out of an increasing health consciousness on the part of American people. In 1944, in the small town of Two Harbors, Minnesota, a cooperative plan was started largely by rail-road and steel workers. In 1945, the Labor Health Institute was organized in St. Louis. 1947 was an important year for in that year the Health Insurance plan of Greater New York began to provide services to subscribers. By 1960, five million people in the United States had eased the problem of medical economics for themselves by the application of the broad method of cooperation.⁸⁶

Cooperative health plans are not cooperatives in the full and strict sense of that word. Some at least violate the cooperative principles of open membership; some violate the principle of democratic control; and all of them fail the patronage refund test. But fundamentally they are cooperative in their essential nature, for they all have the one most essential characteristic of cooperation. They

⁸⁵Ibid, p.29.

⁸⁶Ibid, pp.32-35.

are enterprises whose owners are the same people who are the users of their services. They therefore exist not for financial gain of any individual or the enterprise itself.⁸⁷

CRITICISMS LEVIED AGAINST COOPERATIVES

When the attacks upon farmers cooperatives are analyzed, it is found in almost every instance that the actual reason motivating the attacker is the competition which is given to the business of such person by cooperatives. These attacks are concentrated upon what the attackers believe to be the 'Achilles heel' of cooperatives -- the payment of patronage refunds at the end of fiscal year as a means of adjusting to actual cost the consideration received for goods or services furnished by the cooperatives.⁸⁸

The tax advantage, by which cooperatives are excluded from paying tax on patronage refunds is available to every business man. Joseph G. Knapp pointed out this in the Harvard Business Review for January-February, 1959 under the caption "Are Cooperatives Good Business?", which is as follows:⁸⁹

The cooperative operation does not result in the formation of net income by the cooperatives subject to tax. Should any firm elect to forego the making of income and operate according to cooperative principles on a cost of service basis, it likewise would have little or no net income subject to tax. Any business can enter into contractual agreement with those that it serves to return to them savings resulting from their patronage and free itself from income-tax on those amounts. In other words, tax laws at the present time provide no general advantages to cooperatives that are not available to any other organization which elects to operate so as not to accumulate income.

⁸⁷Ibid, pp.35-36.

⁸⁸Satterfield C.J., The Cooperative in our Free Enterprise System, 1961, p.9.

⁸⁹Ibid, p.10.

The criticism of the taxation of cooperatives must be considered in the light of the recognized principles of law applicable to the payment of patronage refunds and the exclusion thereof from the income of non-exempt cooperatives legally obligated to pay them.⁹⁰

a) A tax payer is free to choose any form of business organization, may it be cooperative, partnership or any other form. The objective of the tax payer would be to achieve a desired business or tax result. It is not necessary for him to take that business form which results in the maximum tax on the business income.

b) Where there is legally enforceable obligation between the member patron and the cooperative, to refund to him the margin between the cost of the goods or services furnished and the amount actually received by the cooperative, it does not constitute income to the cooperative. Such margins paid to patrons are excludable from taxable income of cooperative if they are properly calculated and allocated. This is a matter of legal and constitutional right.

c) The court excludes the patronage refund from tax on five grounds.

i) The first one is that under the pre-existing legal obligation. The margins can never become the property of the cooperative and hence are not a part of its income.

ii) Money that is received by the cooperative in a business transaction and on which it has no right to retain can not be a gain or profit to cooperative.

⁹⁰ Loc.cit.

iii) Patronage refunds are distributions of money belonging to the patrons rather than distributions of income to the cooperative.

iv) Patronage refunds are held by the cooperative as an agent or trustee to the patrons and hence it is legally obliged to repay to the patrons.

v) In reality patronage refunds are discounts or rebates paid under pre-existing legal obligation and are allowable like other discount upon purchase price of any commodity.⁹¹

a) It is immaterial whether the cooperative is organized within a special cooperative statute or under the general corporation statutes; the test is the existence of a legally enforceable obligation to pay patronage refunds which existed during the period such refunds were earned. The obligation may be created by the charter, by-laws or separate contract.

e) If the board of directors of such a non-exempt cooperative has the discretion under contract to utilize a limited portion of such margins for the payment of common stock dividends, the amount which may be thus diverted within the fixed limits will not be excluded. It is held that the legally enforceable obligation to pay patronage refunds is destroyed to the extent that such discretion to divert exists.

⁹¹Ibid, pp10-11.

f) Such corporation is required to pay regular corporate income taxes upon net margins or profits derived from non-stockholder patrons when such persons are not entitled to patronage refunds upon their purchases.⁹²

The whole argument against cooperative overlooks the fact that under the American constitutional form of government the inalienable rights of life, liberty and the pursuit of happiness necessarily carry with them the right of individuals to do business as they see fit within the frame work of federal and state constitutions and statutes. An individual proprietorship, a partnership, a conventional corporation or a cooperative fits into the free enterprise system, one as well as another. The courts have repeatedly rejected the criticism of corporate contracts which minimize taxes. The burden of the argument is that cooperatives should be condemned because they chose to do business in a manner which prevents the patron's savings from becoming part of the corporate funds and corporate income so that such funds are not taxable to the corporation. One of the recent cases decided by the court of Appeals for the Fifth Circuit which reiterates this rule is that of *Friedlander Corporation V Commissioner*, 216 F 2d 75, (5th Cir.1954).⁹³

This and other decided cases reveal that tax favoritism, tax advantage, or tax discrimination in favor of cooperatives does not exist. Every individual proprietor, every partnership, every corporation in the U.S. may enter into patronage contracts under which

⁹²Ibid, pp.11-12.

⁹³Ibid, p.13.

patronage refunds are deductible or excludable from taxable income of business. It seems a weak argument to say that because there is "double taxation" of corporate income and corporate dividends, there should be double taxation of patronage refunds.⁹⁴

The attacks made upon the exclusion of patronage refunds from cooperative taxable income are actually a "tempest in a teapot". The reason is simply that, if congress should enact and the courts should uphold a statute preventing the exclusion of true patronage refunds from the income of cooperatives, all cooperatives would simply proceed to do business at cost by reduction of the original price charged for their services or goods.⁹⁵

SUMMARY AND CONCLUSIONS

The history or record of mutual aid and cooperation as the refuge of people from oppression, hunger and danger is long. Like all human impulses, mutual aid or cooperation has been institutionalized in many ways. In the family first, then the clan, the tribe, the city state and the nation. The purpose of this report is to see the role of different cooperatives in the American economic life and their contribution to the free enterprise economy.

A cooperative society is a voluntary association in which the

⁹⁴Ibid, p.19.

⁹⁵Loc.Cit.

people organize democratically to supply their needs through mutual action, and in which the motive of production and distribution is primarily service, and profit a secondary one. Cooperatives have appeared on the American economic scene because they were needed to curb monopoly and to stimulate competition and some times to provide needed services at reasonable costs which were not otherwise available.

Historical Outline

In America cooperative enterprise dates back to the earliest colonial days. Pioneers cooperated in clearing land, building homes and constructing roads. As early as 1780 farmers organized societies to purchase pure-bred cattle and to make community drives of livestock to distant markets. By 1860, cooperative organizations existed in most of the agricultural areas of the country, and in 1865 Michigan passed the first statute recognizing marketing and supply farm cooperatives. Since the turn of the century the importance of farmer cooperatives has rapidly increased. The number of farmer cooperatives has increased from 3099 in 1915 to the all time high of 12,000 in 1930 with a gradual decline to 9731 in 1957-58.

Role of Cooperatives

More enthusiastic exponents of cooperation hope for the day when cooperation will dominate economic activities. Others look upon the movement as antagonistic to the present economic order and would relegate it to a subordinate role. However, cooperative business accepts the

fundamental institutions of capitalism including the right of private property, the right of contract, inheritance and the right of private enterprise with its emphasis on the dignity and importance of the individual. With respect to many aspects of their daily business operations, cooperatives, also are like the ordinary enterprise. Cooperatives are in full accord with the doctrines of private enterprise and oppose the encroachment of government in business.

The primary role of cooperatives in free enterprise economy is to overcome some of the defects and limitations of capitalistic economy. A fundamental objective of the cooperative plan of business is to improve competition and to enlarge the area in which the competitive pricing mechanism is effective. Cooperatives enable the free enterprise economic system to more nearly approximate the conditions of perfect competition. Another important role which cooperatives have performed is that of counteracting and breaking down the monopolistic elements which develop in private business. The more progressive cooperatives recognize that it is their function in the economy to stimulate competition by maintaining high standards of efficiency and service. Even a small but efficient cooperative occupying a strategic spot in the market may be highly influential as a competitive pace-maker. The reciprocal competitive action of efficient cooperatives and efficient private business firms is a most desirable goal for the free enterprise economy. It is a means of assuring a more effective and productive economic system than one in which government regulation plays a larger part. Thus cooperatives provide a means of complementing and strengthening the capitalistic economy at its weakest points.

The cooperative is a bulwark to all private enterprise. The American farmer believes in the individual ownership of farms and the commodities produced on it. Farmers join together to buy the goods they use in production or to sell the things they grow. Cooperatives have been a major factor in maintaining the family farm. The continued operation of cooperatives is an assurance of the continuance of private enterprise agriculture.

Classification and Specific Examples of Cooperatives

According to the nature of services or type of goods furnished cooperatives may be divided into many forms. For example, rural electric cooperative provides electric service at the lowest possible cost to its member patrons with the help of the Rural Electrification Administration. These cooperatives are organized and function according to the general pattern of consumer cooperatives but have a number of distinguishing characteristics. These cooperatives revolutionized the American farming and eased the drudgery and monotonous life of the American farmer. When plans were made to form rural telephone cooperatives, immediately existing private firms voiced their opposition to cooperatives and stepped forward to buy and improve the rural exchanges. Here the stimulating function in action can be seen. In these situations the cooperative was never actually formed but its purpose was accomplished.

Supply Cooperatives: The growth of supply cooperatives came late in the United States. Today farm purchasing cooperatives are major suppliers of petroleum, fertilizer, feed and seed. The supply

cooperatives make it possible for farmers to purchase their farm supplies at a lower price. Today cooperatives supply about twenty per cent of the petroleum used on farms in the United States. By 1959 the index of prices paid by farmers for necessary supplies and inputs had risen to 275 from the base period 100 for 1910 and 1914. But for the two commodities where cooperatives are strongest petroleum and fertilizer--the index was only 175 and 152 respectively.

Marketing Cooperatives: In the latter half of the nineteenth century the Grangers spearheaded formation of both marketing and consumer cooperatives among distressed farmers. Today about a quarter of all U.S. farm products are handled by marketing cooperatives.

Credit Cooperatives: By 1960 credit unions in the United States numbered almost twenty thousand, with a membership of more than eleven million and assets close to five billion dollars. Credit unions can be useful and constructive influences in any society but there are natural and unavoidable limits to the scope of their activities and effectiveness. In the cooperative farm credits field, banks for cooperatives and federal land banks provide credit facilities. The banks for cooperatives offer a complete loan service on a sound constructive business basis. The federal land banks make loans to farmers on a long term basis for purchase of land, equipment etc. In addition to these banks the production credit system also provides short term agricultural credit on semi-cooperative basis, in competition with commercial banks, through production credit associations.

Cooperative Housing: Because the construction industry tends to build small numbers of homes within the reach of an average income family, people have come together and organized cooperatives to build apartment houses that are within their financial capacity. By 1959 there were about three hundred cooperative housing projects in the United States.

Cooperative Health Plans: The cooperative health movement was born out of an increasing health consciousness on the part of the American people. The cooperative health organizations are not strictly cooperative but have the one most essential characteristics of cooperation, i.e. they are enterprises whose owners are the same people who are the users of their services.

Criticisms

The main criticism levelled against cooperatives is that they do not pay tax on patronage refunds. But this advantage is available to every business that operates in a cooperative way. When a legally enforceable obligation exists to refund to stock-holder patrons the margin between the cost of the goods or services furnished and the amount received by the cooperative it does not constitute income to the cooperative and should not be taxed as income. Many decided cases reveal that alleged tax favouritism, tax advantage or tax discrimination in favour of cooperatives is grossly exaggerated.

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THE ROLE OF COOPERATIVES IN THE U.S. ECONOMY

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The purpose of this report is to examine the role of cooperatives in agriculture, rural electrification, credit, housing, oil business, health and other fields of American life and economy. The discussion emphasizes the basic principles and issues involved in the relationship of cooperatives to other forms of business and their quantitative role in the economy of the U.S.

The method followed in preparing this report is to study published material available at the Kansas State University library, the material obtained through the Department of Economics and Sociology and other sources and to select information pertinent to the subject and then to analyse it seeking to arrive at an evaluation of the role of cooperatives in the U.S. Economy.

Cooperatives have appeared on the American Economic scene because they were needed to curb monopoly, to stimulate competition, and sometimes to provide needed services at reasonable costs which are not otherwise available.

In America, cooperative enterprise dates back to the earliest colonial days. By 1860, cooperative organization existed in most of the agricultural areas of the country.

Cooperatives may be divided into many forms according to the nature of services or types of goods purchased, such as rural electrification cooperatives, supply cooperatives, marketing cooperatives, credit cooperatives, cooperative housing, cooperative health plans etc.

During the 1957-58 season the gross value of farm products marketed, farm supplies handled and receipts for services performed by cooperatives amounted to approximately 14 billion. About twenty per cent of the petroleum used on farms in the U.S. is supplied by cooperatives. By 1959 there were some three hundred cooperative housing projects in the U.S., 150 of them being in New York state alone. By 1960 five million people in the U.S. had eased the problem of medical economics for themselves by the application of the broad method of cooperation.

Cooperative business accepts the fundamental institutions of capitalism like ownership of property, freedom of enterprise, competition, etc. With respect to many aspects of their daily business operation, cooperatives are also like ordinary enterprises.

The primary role of cooperatives in the free enterprise economy is to overcome some of the defects and limitations of capitalistic economy. Cooperatives enable the free enterprise economic system to more nearly approximate the conditions of perfect competition. Even a small but efficient cooperative occupying a strategic spot in the market may be highly influential as a competitive peacemaker. More progressive cooperatives recognize that it is their function in the economy to stimulate competition by maintaining high standards of efficiency and service. Cooperatives provide a means of complementing and strengthening the capitalistic economy at its weakest points.

Cooperatives are criticized mainly on the basis that they do not pay the corporation income tax on patronage refunds. But this

criticism is not reasonable because the so called tax advantage is available to any business that operates in a cooperative way. Many decided cases reveal that alleged tax favouritism, tax advantage, or tax discrimination in favour of cooperatives is grossly exaggerated.