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A PRIMER ON
COOPERATION



EXTENSION SERVICE
SOUTH DAKOTA STATE COLLEGE
BROOKINGS, SOUTH DAKOTA




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A PRIMER ON COOPERATION*

Cooperation has a variety of meanings. Broadly speaking, it means working together toward a common end. We will discuss, however, a specialized type of cooperation; one that deals with the working together in an organized way for carrying on a business for the benefit of its patrons.

History and Origin of Cooperation

HOME. Perhaps the first form of cooperation was found in the home. Members of the family worked together toward a common goal to supply the necessities of life.

COMMUNITY. Soon others than members of a family were working together—toward common ends in many different ways. In the country, neighbors cooperated by helping each other during the harvest season. Individuals cooperated by joining groups in order to maintain churches and employ ministers. Laborers, as a class, cooperated through unions to protect their interests. Our city, county, state, and national governments are huge cooperative undertakings within the general meaning of the term. In democratic governments, the people collectively work together for such purposes as maintaining schools and roads, furnishing protection to life and property, and administering justice. In fact, the advancement of civilization has been pretty much a cooperative undertaking.

FIRST ORGANIZED MOVEMENT—ROCHDALE PRINCIPLES. Cooperation in business came into being and has grown and developed because other recognized forms of business did not meet the needs of groups interested primarily in savings. In 1844, 28 flannel weavers of Rochdale, England, banded together to form a self-help organization, an organization which would meet their needs as consumers. To govern their business, these cooperative pioneers set up rules that are still fundamental. Naturally, the Rochdale principles of 1844 have been extended and modified to meet present conditions; but the concept remains essentially as formulated at that time.

What are these principles?¹

1. Membership fee, or value of stock—low in price and within the reach of all. No prospective member is debarred from participation because of his financial status.
2. Limitation of the number of shares of capital held by any one member. Capital shall be widely distributed among the members and not concentrated in the hands of a few.
3. One-man-one-vote regardless of the number of shares owned. This provision insures the equal rights and voting powers of members.

* The manuscript for this publication has been prepared by L. M. Brown and R. J. Penn, of the Agricultural Economics Department of South Dakota State College at the request of the South Dakota Agricultural Extension Service. The authors have written the circular to serve as a source of information on cooperatives for rural youth. The authors wish to thank the Agricultural Economics Department of the University of Wisconsin for permission to use the information in Wisconsin Special Circular, COOPERATION—PRINCIPLES AND PRACTICES, November, 1936.

1. Department of Agricultural Economics, University of Wisconsin, COOPERATION—PRINCIPLES AND PRACTICES, Special Circular, Nov. 1936. p. 4.

4. Sales at regular prices rather than at reduced rates. This practice does not invite ruinous price-cutting wars with competitors.
5. Sales for cash, thus eliminating inevitable losses connected with the granting of credit.
6. Payment of a low rate of dividend on capital stock and the distribution of savings on the basis of volume of patronage contributed by each member. Capital is hired. Patronage is rewarded.

It is evident that these principles were intended for consumers in the operation of a cooperative store. Not all of them apply with equal force to farmers' cooperative marketing associations. The foundation principles are equal voting power, limited returns on capital, the distribution of the earnings on a patronage basis, political and religious neutrality, cash trading, control or ownership of facilities, membership open to all agricultural producers in the trade area, and promotion of education.

Cooperation in Foreign Countries

DENMARK. The Danish system of rural education, particularly the adult rural Folk Schools, have contributed richly to Denmark's agricultural progress and the successful development of the cooperative movement. The Folk Schools have provided the background for an intelligent and enlightened farm population, opening the minds of the farmers to new worlds outside their experience, developing a mutual sentiment, which is nothing more nor less than a willingness to think together, work together, play together—in short, to cooperate. This philosophy toward rural life and the educational process has been the greatest single factor in the development of the cooperative movement in Denmark. In turn the organizational experience and leadership developed by the cooperative movement has given Danish agriculture an influential voice both in local and national governmental affairs.²

Danish farmers are undoubtedly the most highly organized group of agricultural producers in the world. In 1932, 42 per cent of Denmark's households were members of the cooperative consumers' societies, and 90 per cent of all the dairy farmers delivered their milk to cooperative creameries.³ A large part of the butter from these creameries is marketed cooperatively through federations owned and controlled by farmers. In 1933, there were 61 cooperative swine packing plants in Denmark, slaughtering annually between six and seven million hogs.⁴ On an average each cooperative swine packing plant had a membership of about 3,600 farmers, and slaughtered annually about 107,000 hogs. The purchasing of agricultural supplies, such as feeds, fertilizers and seeds, as well as household necessities, has been extensively developed in Denmark.

SWEDEN. Cooperation in Sweden developed from isolated associations, but since the World War it has become a great national movement. In Sweden, consumer cooperation is used to cut monopolistic tendencies; in the United States this is done by legislation. There is no friction between trusts and cooperatives unless the trusts are monopolistic and charge unfair prices. There is one central organization of the consumers'

2. Jensen, Einar, *DANISH AGRICULTURE, ITS ECONOMIC DEVELOPMENT*, J. H. Schultz Forlag, Copenhagen, 1937, p. 353.

3. Agricultural Economics Department, University of Wisconsin, *op. cit.*, p. 51.

4. *Ibid.*, p. 55.

cooperative movement—the Kooperativa Forbundet (Cooperative Union)—which combines wholesaling, retailing, manufacturing, insurance, education, and publishing. In order to break the monopolistic practices of the trusts, the Cooperative Union is now manufacturing margarine, flour, rubber overshoes, automobile tires, and light bulbs, in addition to other articles.

One-third of the Swedish population are members of the consumers' cooperatives; the consumers' cooperatives in turn made over 10 per cent of the national retail sales.⁵

The Swedish farmers also are organized cooperatively. Cooperative marketing organizations handling dairy products, livestock, grain, poultry and eggs, fruit, and forestry products are organized into local, regional and national cooperatives. Credit cooperatives are similarly organized. The six national commodity cooperatives together with the national organization of the credit cooperatives are affiliated in Sweden's general Agricultural Society (Sveriges Allmänna Lantbruksallskap) which protects the interests of Swedish agriculture in various ways. Friendly working relations exist between the producers' and the consumers' cooperatives.

NORWAY. Cooperation in Norway has progressed on about the same lines as in the other Scandinavian countries. They have developed some of the most efficient cooperatives for the handling of dairy products, especially fluid milk. The cooperatives dealing with fluid milk are operated on a plan similar to that used in the large fluid milk sheds of Austin and Chicago. In Norway eight milk sheds cover the whole nation.

GREAT BRITAIN. The Industrial Revolution was a primary cause for the development of cooperation in Great Britain. In the absence of adequate laws protecting the rights of the laboring people, able-bodied workmen were thrown out of employment by the same machines they had helped to create. In the economic reorganization, adjustments were required. One of the methods by which these adjustments were accomplished was the establishment of cooperatives by the low income laborers and the unemployed.

The expansion, beginning with one store on Toad Lane in Rochdale (1844) and growing to more than 1,200 retail distributive outlets and depots (1935), represents the phenomenal rise of the consumer movement throughout England, Wales and Scotland. The retail stores are federated into the Cooperative Wholesale Society of England and Wales and the Scottish Cooperative Wholesale Society of Scotland. These two great wholesale organizations had a total of more than seven million members, and their total retail sales amounted to nearly 500 million dollars.⁶

Cooperatively owned and operated industries had been the objective of the English workmen for a century before this goal was definitely achieved. About 150 cooperatively owned factories have been established throughout England, Scotland, and Wales. More than 70 thousand workers are engaged in manufacturing or providing services to the members of the two wholesale societies.⁷

5. Minnesota Department of Education, COURSE OF STUDY ON CONSUMERS' COOPERATION, 1938. p. 52.

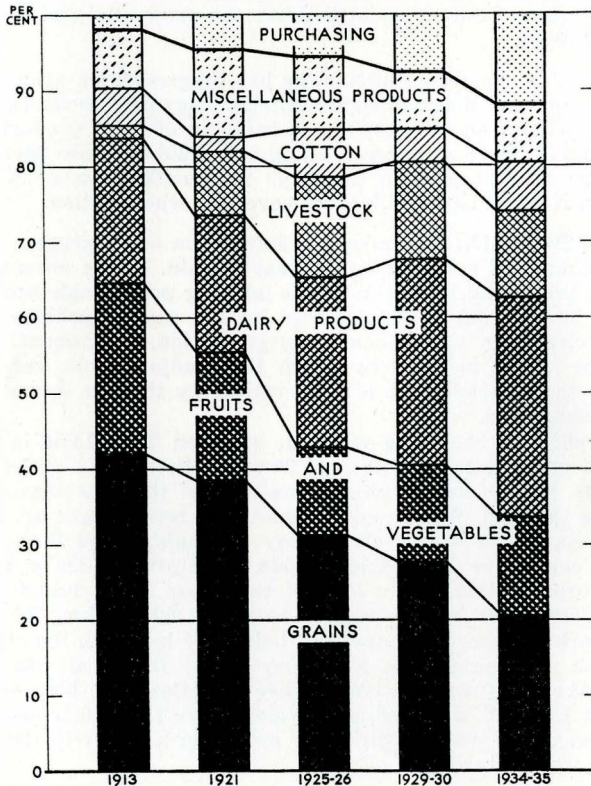
6. Agricultural Economics Department, University of Wisconsin, op. cit., p. 44.

7. Ibid., p. 44.

SWITZERLAND. Switzerland can be considered the cradle of cooperation. Here in the Alps, farmers found it expedient to cooperate in almost every line of farm business endeavor. Today there are more than 12,000 local organizations in this small country. The Swiss farmer is a cooperater. Few nations, except Denmark, have produced his equal in that respect. There are, on the average, slightly more than nine memberships in agricultural business cooperatives and farmers' organizations for every farm in Switzerland.⁸

The dairy organizations make up the largest and most influential group in the cooperative field. The hub of the cooperative dairy wheel is the Central Union of Swiss Milk Producers. In 1931 this organization was composed of 20 member federations, representing 3,339 local societies with a membership of 102,423 dairy farmers. Its members controlled in that year the product of 68 per cent of all cows in the country.⁹

Fig. 1.—Business of Farmers' Cooperatives by Commodities*
United States



* Elsworth, op. cit., p. 15.

8. Ibid., p. 60.

9. Ibid., p. 62.

The Extent of Cooperation in the United States and South Dakota

Cooperative buying and selling is carried on extensively throughout the United States. According to data published by the Farm Credit Administration, there were around 10,700 farmers' cooperative buying and selling associations in the United States in 1935; these reported approximately 3,280,000 members. Hence, there was about one cooperative membership for every two farms in the United States.¹⁰ South Dakota had 354 associations with 71,809 cooperative memberships in 1937. The proportion of cooperative memberships for South Dakota, nearly one (.86) cooperative membership per farm, is about double that for the United States as a whole.¹¹

On an average, every farm in the United States did \$225 worth of business with a cooperative; while in South Dakota the average was \$324 per farm.

NUMBER AND VOLUME OF BUSINESS. The figures in Table 1 compare the South Dakota cooperative associations with those in the United States. The averages are especially significant: Average membership and volume indicate that South Dakota is low, while the average volume of business per farm in the state is in a favorable position as compared with the United States.

TABLE 1.—Number, Membership, and Volume of Business of Cooperative Associations, United States and South Dakota

	Membership			Volume of Business		
	Number of Assns.	Total No.	Av. per Assn. No.	Total	Av. per Assn.	Av. per Farm
United States, 1935*	10,700	3,280,000	306	\$1,530,000,000	\$143,000	225
South Dakota, 1936	354	71,809	205	26,980,070	79,353**	324

In comparing the leading states as to the extent of cooperation, Minnesota had the greatest number of associations and the largest number of members, while California had the greatest volume of business (Table 2).

TABLE 2.—Number of Cooperative Associations, Membership and Estimated Business for the Leading States, 1934-35*

State	Associations No.	Membership No.	Estimated Business (\$1000)
Minnesota	1,416	332,100	122,450
Illinois	761	269,630	141,700
Iowa	1,000	259,480	106,830
Wisconsin	1,118	192,500	73,490
California	425	77,380	180,910
New York	255	124,200	124,520
Missouri	479	174,150	61,930
Nebraska	534	150,770	46,100
Ohio	335	167,600	63,980
Indiana	265	160,100	40,000
Michigan	320	129,610	42,050
North Dakota	513	87,630	25,640
All others	3,279	1,154,850	500,400
Total	10,700	3,280,000	1,530,000

10. 1935 Federal Census—6,812,099 farms in the United States.

11. 1935 Federal Census—83,000 farms in South Dakota.

* Elsworth, E. H., STATISTICS OF FARMERS' COOPERATIVE BUSINESS ORGANIZATIONS, Farm Credit Administration, Bul. No. 6. May 1936, p. 17.

** Only 340 reported.

* Elsworth, op. cit., p. 17.

COMMODITY GROUPS. Historical changes in the relative importance of commodity groups are pictured in Figure 1, showing the trend in the cooperative marketing of commodities for five periods. The cooperative marketing of grain, fruits, and vegetables has decreased in relative importance since 1913, while cooperative dealing in other commodities has increased. Commodity groups are ranked according to their importance in volume of cooperative sales, Table 3.

TABLE 3.—Volume of Sales of Cooperative Associations by Commodities, United States, Marketing Season, 1934-35¹²

Commodity Group	Associations No.	Membership No.	Estimated Business (\$1000)
Dairy products	2,300	750,000	440,000
Grain	3,125	580,000	315,000
Livestock	1,197	410,000	175,000
Fruits and vegetables	1,082	158,000	200,000
Cotton and products	305	255,000	100,000
Poultry and products	164	85,000	53,000
Wool and mohair	119	71,000	15,700
Tobacco	16	50,000	7,500
Nuts	53	14,800	11,300
Forage crops	29	6,900	1,830
Miscellaneous selling	404	109,300	23,670
Purchasing	1,906	790,000	187,000
Total	10,700	3,280,000	1,530,000

For South Dakota, the three most important groups of commodities ranked in order of their volume of cooperative sales are: Grain, dairy products, livestock.

Types of Cooperatives

Cooperative associations are of many different types and kinds. Some are marketing associations; others are purchasing associations; still others are laborers' cooperatives, mutual insurance companies and credit unions. Associations can be classified according to the commodities handled and the character of services rendered, the territory served, and the type of financing.

During 1934-35, farmers in the United States marketed cooperatively about seven times as much as they bought cooperatively, measured in terms of value. In 1935-36, the farmers in South Dakota marketed cooperatively only a little over twice as much as they bought cooperatively.

CONSUMER TYPE. "Consumer cooperation" to many includes only the activities of the city consumer. Yet fully three-fourths of all cooperative purchasing in the United States is done by farmers as consumers.¹² The farmer is not attempting by this means to gain control of the processes of production: His aim is directed toward exercising a voice in controlling, or at least influencing, the process of market distribution, in the hope of reducing marketing costs.

The earliest consumer cooperative development in the agricultural areas of this country was sponsored by the Grange in the 1870's. The movement was taken up next by the Farmers' Alliance, then by the Knights of Labor, Farmers' Union, Farm Bureau, and Equity locals. The recent developments in consumer cooperation among farmers have been growing out of: First, marketing cooperatives—purchasing activities of farmers' elevators and supply departments in some of the large organi-

12. Agri. Econ. Dept., University of Wisconsin, op. cit., p. 19.

* Elsworth, op. cit., p. 17.

zations, e. g., Land O'Lakes Creameries; second, farm organizations such as the Grange, Farmers' Union and Farm Bureau; third, independent movements—isolated stores, insurance associations, etc.

According to Bureau of Labor statistics, there were 3,600 consumer cooperatives in the United States in 1936. They had a total membership of 677,750 and a total business of \$182,685,000.¹³

Successful purchasing associations give the following as some of the main causes of their success:

Self-Service at Lower Cost—The one who sells is employed by the member-purchasers.

Elimination of Waste—Competition may promote efficiency; but at the same time, it often involves expensive practices, such as two stores, the patronage of which might well be handled by one with but small increases in overhead costs.

Reduction in Costs—Savings are made up in part by eliminating expensive services, by curtailing certain expenses inherent in competition and through returning to the member patrons the portion of handling margins which ordinarily goes to profits in private business.

Selling Merchandise of Known Quality—Since the buyer is selling to himself, there is no incentive whatever to conceal the true quality of the goods handled.

There are many different kinds of consumer cooperative associations; e. g., grocery and general merchandise stores, oil associations, lumber associations, bakeries, hatcheries, refineries, wholesale associations of different kinds, and the purchasing departments of farmers' creameries and elevators. The following is a discussion of several of the most important types of consumer cooperatives.

Cooperative Gasoline and Oil Associations.—Probably the first cooperative gasoline and oil distributing associations were developed in the Midwest. Local oil cooperatives were started in South Dakota in 1924, but the movement did not have much growth until 1926. There are now probably a thousand or more associations distributing petroleum products cooperatively in the United States. There were 51 in South Dakota in 1937.

Cooperative oil associations are primarily farmers' organizations with but few serving urban centers. Perhaps this is natural, for farmers use large quantities of petroleum products for tractors and trucks in addition to that used in automobiles. A large proportion of the sales are delivered directly to the farms in tank trucks.

Cooperative Stores (Grocery and General Merchandise).—In the United States, cooperative stores have not developed to such an extent as they have in some foreign countries. Only about 500 stores are owned and operated cooperatively in this country. They are most numerous in the Midwest, principally in the Great Lakes region of Minnesota, Wisconsin, and Michigan. In South Dakota there were 18 such stores in 1937.

Regional and Wholesale Purchasing Associations.—A number of regional purchasing and marketing associations have developed sizable businesses in farm and household supplies during the past few years, mainly since 1920; and several large regional marketing associations have estab-

13. U. S. Dept. of Labor, Serial No. R.718, p. 1.

lished supply departments. One of these, the Land O'Lakes Creameries, Inc., did a jobbing business in feeds totaling approximately \$630,000 in 1934; in addition it handled \$1,430,000 worth of creamery equipment and supplies.¹⁴

In the United States in 1934, there were 25 wholesale and retail cooperative associations which sold farm and household supplies in amounts exceeding a million dollars each. The largest of these is the Cooperative Grange League Federation Exchange, Inc., which did a wholesale farm supply business of over \$24,000,000 and a retail business of over \$16,000,000.¹⁵

PRODUCER TYPE.—A cooperative sales (producers') association is a voluntary business organization established by its member-patrons to market farm products collectively for the direct benefit of the member-patrons. Members, as owners and operators of the association and contributors of the commodities handled, are the direct beneficiaries of the savings that may occur.

The immediate purpose of a producers' sales association is to obtain the highest farm price. The ultimate purpose is to elevate the plane of living on the farm. The objective of a cooperative is not to eliminate private middlemen, but to lower the cost of distribution, improve production, integrate marketing and production operations, eliminate waste, prevent expensive duplication of agencies, and distribute products in a systematic manner.

Agriculture in the United States is carried on chiefly by small unit enterprises. As a result, farmers have found it advantageous to work with one another in accomplishing certain production and marketing tasks which they cannot do individually. Such informal farmers' cooperative associations, as spraying, silo filling, threshing rings, and cornhusking and barn-raising bees are examples of cooperative efforts in production. Probably in no industry is there such an expression of joint effort in solving the problems of production as there is in agriculture.

The first organization to stimulate definitely the collective selling of farm products was the Grange, especially during the period from 1870 to 1876. Another organization fostering marketing activities was the Farmers' Alliance (1875); this organization during ten years of its most active existence placed a great deal of emphasis upon cooperative activities. The Farmers' Educational and Cooperative Union and the American Society of Equity were organized in 1902. One of their main purposes was and has been to market farm products cooperatively. Before 1915 the chief activities of the Union were in the South and were primarily concerned with the marketing of cotton; since 1915 the Union has been an important influence in the establishment and operation of cooperatives in the northern part of the United States. In 1920, the American Farm Bureau Federation was organized; one of its primary purposes was to promote orderly marketing of farm products.

Dairy.—The first dairy marketing organization was established in this country about 1810. South Dakota's first cooperative creamery association was established in 1896. At the present time there are 40 creamery associations in this state. Large federated associations have been develop-

14. Agri. Econ. Dept., University of Wisconsin, op. cit., p. 33.

15. Ibid., p. 26.

ing in the United States since 1921, and today five federated sales associations, such as the Land O'Lakes Creameries, Inc., sell about one-fifth of the creamery butter of the nation.¹⁶

Livestock.—The cooperative marketing of livestock dates back to the colonial period. The farmers' livestock shipping association at Superior, Nebraska (1883), is commonly considered to be the first association of the more strictly cooperative type. About 1917, and continuing for the next eight years, the organization of local livestock shipping associations underwent a very rapid expansion, so that by 1925 between 3,000 and 4,000 livestock shipping associations were in operation.¹⁷ In South Dakota the first livestock shipping associations were organized in 1915. It has been estimated that there were between 215 and 500 livestock shipping associations during the period 1923-26. By 1929 there were 125 associations in existence, and by 1937 there were only 14 active associations.

Grain.—General dissatisfaction with price policies of independent and line elevators, objections to the grading and docking practices, and general criticism of excessive railway freight charges impelled the farmers throughout the grain-producing regions to organize their own cooperative elevators. The first cooperative elevator was established at Madison, Wisconsin, in 1857. The first cooperative elevator in South Dakota was organized in 1887, and at the present time there are 203 active associations.

SERVICE TYPE.—Numerous cooperative associations have for years rendered services for their members—sometimes as part of a producers' or consumers' association or as a separate organization. Among the numerous services rendered are: Insurance, medical care, financing, telephone, electrical, housing, restaurants and cafeterias, burial, education, publishing, laundering, auditing, recreational, milk distributing, garage, and library.

Farmers' mutual fire insurance associations carry about 55 per cent of the total fire insurance on farm buildings.¹⁸ Some of the associations have expanded into the fields of automobile and life insurance. Medical and hospital associations are becoming more numerous. The present economic conditions have induced people to form hospital, medical and dental cooperatives. The credit union is the application of cooperation to financing, providing short-term credit at fair rates of interest. By pooling small savings these associations are able to lend to members. Ninety-five per cent of the credit unions are found in urban centers. We are indebted to Germany for many of our early ideas on credit cooperatives.

LOCAL ASSOCIATIONS.—Most common of all the types of agricultural cooperative associations is the local, found in large numbers among the producers of almost every type of agricultural commodity that is marketed cooperatively. A local association serves a relatively small number of persons who have similar selling or buying problems, and since the members usually live within a relatively restricted area, it is essentially a neighborhood enterprise.

16. Bakken, H. H., Schaars, M. A., *THE ECONOMICS OF COOPERATIVE MARKETING*, p. 52.

17. *Ibid.*, p. 53.

18. Bakken, *op. cit.*, p. 76.

A local marketing association is primarily interested in securing the greatest efficiency in assembling, processing, grading, and shipping of farm products. It is strictly an individual organization but may join with other local groups to form an overhead organization, such as the federated sales association.

FEDERATED ASSOCIATIONS.—The federation, one type of large scale central marketing organization, is primarily a sales association that renders marketing services connected with the handling and selling of goods produced by the members of the local association. The membership of a federation consists of local associations. It is usually the custom for a federation to be established after a number of local associations have been in existence and have voluntarily agreed among themselves to set up a central selling agency.

CENTRALIZED ASSOCIATIONS.—Another type of large scale marketing organization is the centralized association which is similar in many respects to the federation. The difference is mainly in form of organization and in the relationship of its members. The members of a centralized association are individual farmers, whereas members of a federated association are local associations. These associations, as the name suggests, centralize into one organization the marketing activities of a large number of farmers who reside over a widespread area.

STOCK OR NONSTOCK.—The capital needs of an association often determine whether it will be organized on a stock or on a nonstock basis. In a capital stock corporation, certificates of stock are issued upon payment of a certain sum of money or its equivalent. A nonstock corporation issues certificates of membership to those who pay membership fees. "Nonstock" does not mean "noncapital."

The price of capital stock shares may be no higher than membership certificates in a nonstock association. The difference between the two—stock and nonstock—is primarily legal in nature. Perhaps owning a share of stock gives a greater feeling of financial responsibility than owning a membership. There were 306 stock and 47 nonstock associations in South Dakota in 1937.

Organization of Cooperatives

LEGISLATION.—The development of legislation permitting and facilitating the operation of cooperatives according to accepted standards of membership has been a slow process in the United States. Many states led the federal government in recognizing the need for legislation differentiating cooperatives from other forms of business organizations. All states but one now have laws designed to facilitate and to promote the formation of cooperative associations. Before 1922, one of the difficulties faced by cooperatives was the uncertainty of their activities with respect to provisions of the Sherman Anti-trust Law of 1890. Competitors threatened to sue cooperators on the grounds that the mere act of combining to conduct business was in restraint of trade and illegal under the anti-trust laws. Congress, by the adoption in 1914 of Section 6 of the Clayton Amendment to the federal anti-trust laws, attempted to confer upon farmers' cooperatives a somewhat distinct position in their relation to the federal anti-trust laws.

Congress, at that time, undoubtedly intended to permit farmers' associations to operate without regard to federal legislation prohibiting "monopolies" and without regard to the committing of acts in "restraint of trade" providing such companies were (a) composed entirely of farmers, (b) organized without capital stock, and (c) operated for the mutual benefit of their members and not for profit.

In accordance with the interpretation of the law, the farmers were free to organize for collective bargaining. The mere act of organizing was not to be construed as being in restraint of trade. But the actions of such an organization were in no wise immune from the provisions of the anti-trust law. Furthermore, the amendment applied only to nonstock associations. There were few of these and few states with legislation facilitating their organization; hence, the application of the amendment was extremely limited as far as existing cooperatives were concerned. The question was not cleared until the passage by Congress of the Capper-Volstead Act in 1922. (See appendix 1.) By this act, the federal government made a marked advance in defining the legal position of farmers' cooperative business enterprises.

South Dakota has two cooperative laws in force at the present time: the general cooperative law entitled "Cooperative Corporations and Associations," enacted in 1913; and the "Cooperative Marketing Law," of 1923. These two laws are not coordinated in their requirements. (See appendix 2.) Which of the two South Dakota cooperative laws is the better is difficult to state, as such judgment must be passed in light of the type of association contemplated. The 1923 cooperative law was designed for use by agricultural producers only, while the 1913 cooperative law is more general in its membership requirements.

FORMS OF BUSINESS ORGANIZATIONS.—Partnership—Two or more persons may join in the operation of a commercial enterprise. Their contributions of capital and services, the allocation of control, and their division of profits are matters of agreement. But under the law, except in the case of limited partnerships formed as prescribed by law, each partner is liable for the all the obligations of the firm. Unlimited liability of each partner is the outstanding characteristic of a partnership.

Corporation.—There are many types of corporations. The distinguishing characteristic is that the liability of each stockholder for the obligations of the corporation is limited to the amount of his subscription to or for capital stock, and when this amount is fully paid he is under no liability to the creditors of the corporation. The number of votes, and hence the amount of control exercised, is governed by the number of shares of stock owned. Profits are distributed to the stockholders on the basis of shares of capital stock owned or capital contributed to the enterprise.

Cooperative.—The cooperative corporation differs from the usual corporation in that each member or stockholder usually has only one vote regardless of the number of shares of stock he may hold; and earnings are distributed not on the basis of stock owned, but on the basis of the amount of business conducted with the organization. One distinguishing feature of the cooperative is that it is owned by and operated for the benefit of the members as patrons. The rate of dividend on shares of stock is generally limited by law.

WHY THE COOPERATIVE FORM OF ORGANIZATION IS CHOSEN.—Why is it that consumers and producers have in many cases chosen to group themselves into cooperatives rather than to utilize one of the other types of business organizations? Obviously, a general partnership with its unlimited liability feature does not meet the needs of large groups for most business purposes. Many cooperatives did operate as corporations of the usual type before the state and federal governments enacted legislation suited to the needs of cooperative business undertakings. It requires no lengthy explanation to point out that the usual form of corporation does not fill the needs of producers or consumers who are banded together for the purpose of conducting a business, the success of which depends largely upon their own patronage.

In the corporation, capital is the all-essential; control and benefits are dependent upon its ownership. In the cooperative, patronage is the important consideration; control is equal, but benefits are upon a patronage basis.

It is clear that one of the main reasons for the continued development and expansion of the cooperative business undertakings is that other forms of conducting business do not meet the needs of those who wish to serve themselves. They have patronage to contribute to the undertaking, and desire to be rewarded on the basis of that contribution. In effect the members pool their individually small volume in their cooperative in the hope of effecting a saving on their own sales or purchases.

The usual legal business structures did not provide for distribution of benefits in this fashion; hence, a new form has been created during the past 100 years. It has been during the past 25 years only that this new creation—the cooperative—has been recognized legally in anything approaching an adequate manner.

MEMBERSHIP RELATIONS.—Inasmuch as a cooperative is organized for, supported by, and composed of its members, it is essential that the members be adequately informed about the organization and operations of the association. Membership loyalty is one of the keystones of successful cooperation. Some associations have adopted a selective rather than an open membership policy. An example of a selective policy is found in some associations which allow only producers to be members. In cooperative purchasing associations, the open membership policy is universally used. One means of defining the rights and duties of both the members and the association is through the use of a membership contract. Such a contract which calls for the delivery of all the products marketed by the member for a certain period of time has both an economic and a legal value in the association. The contract has not been used extensively in South Dakota.

It is essential to create and maintain among the members a correct attitude toward their association. A full understanding of what a cooperative can and cannot do, why things are done as they are, and how things must be done is important. It is particularly difficult to keep the support of members if the object of their membership is impossible to attain; hence, the possibilities of cooperation must be correctly interpreted to the membership.

There are numerous ways of keeping the membership adequately informed. These vary from the methods used by national or central associations to those followed by the small local associations. Some of the means

are: personal participation in some activity of the cooperative; direct contacts with directors, officers, fieldmen, and the manager of the association; business and social meetings of the entire membership; issuance of enlightening annual reports and of informative house organs; and a constant willingness of the management to explain matters courteously to inquiring members. The problem is relatively simple in local associations and sometimes difficult in large-scale associations.

DIRECTORS' RELATIONSHIPS.—At the present time the democratic procedure of electing representatives resolves itself into the usual custom of selecting men who show promise of possessing good business judgment, who undertake human nature and who demonstrate an ability to get along with people. Beyond this it is difficult to stipulate other qualifications, and under the circumstances it is questionable whether anyone can arbitrarily enumerate specific attributes required for success. Of course, it is assumed that the man's character is beyond reproach in his business dealings, and that he will be loyal to the interests of the group he professes to serve.

The duties of a director cannot be assumed too lightly. The position is a trusteeship which bestows certain rights upon those elected to the office, and these rights imply that certain duties may be performed. Some duties of the directorate are:¹⁹

To formulate policies.

To employ managerial executives.

To inform themselves upon the nature of the business of their association and to study the possibilities of applying the principles and successful practices of cooperation.

To enforce the policies which they enumerate.

To attend all meetings of the board and to maintain a record of its deliberations.

To maintain contact with the leadership of their respective communities.

To instill confidence in their cooperative organization.

In the final analysis, the directorate is the management of a cooperative association. Its origin and functions are similar to the legislative branch of our government. It is empowered to enlarge or restrict, within the law, the rights of individual members in the association, whenever such acts are necessary for the welfare of the total membership.

MANAGEMENT.—The manager's task is that of supervising the operating details of the enterprise. The more extensive the business, the greater are the problems of supervision and coordination. Members of cooperative associations are apt to minimize the importance of a good executive, a fact which is manifested in a reluctance to pay salaries comparable to the services received.

A competent manager should be capable and resourceful in directing a business upon cooperative principles and in interpreting the intent of the directors in complying with their policies. He must be tactful in dealing with employees and members. His sympathy should be genuine in attempting to fulfill the aims of those whom he serves, provided their objectives are intended to promote social and economic well-being. He is the servant of all members and is completely responsible to the directorate in his stewardship of their business venture.

19. Agri. Econ. Dept., University of Wisconsin, op. cit., p. 102.

DISTRIBUTION OF EARNINGS.—The financial gains which come to a cooperative association in the ordinary course of business transactions are commonly termed savings or profits. The amount of these savings will depend on the type of association, the method of doing business, the volume and efficiency of the organization.

The laws of the various states provide methods of distributing the earnings. The usual procedure is: First, to pay interest on capital stock; second, to place a certain per cent of the earnings in the reserve fund; third, to set aside a specified per cent to the educational fund; and fourth, to proportion the balance to the members or to all patrons, as the case may be, on the basis of the amount of business transacted with the association.

Financing of Cooperatives

Before an association actually starts business operations, money is usually needed to meet the expenses of organization; however, many times the persons interested will donate their time or small sums to pay the cost of organizing. After organization is completed, a cooperative business association's first need for money is for acquiring facilities such as plant, plant site, machinery and equipment. The next need is money for operating purposes; this includes money for the payment of salaries and wages, insurance, taxes, purchase of goods for resale by purchasing associations, and in general, for all out-of-pocket expenses. It is a common experience to find cooperatives reasonably well financed from the standpoint of money for fixed assets, but without enough operating capital.

CAPITAL STRUCTURE.—Members of an association usually must provide the initial capital for business purposes. The manner in which this is done will depend largely upon the form of organization and the nature of the business.

Capital Stock.—Associations are organized usually on a stock basis when large amounts of capital are needed. Members tend to look upon the purchase of stock both as an investment and as a membership responsibility. Capital stock is ordinarily issued in the form of common stock and is occasionally supplemented by preferred stock. The board of directors determines annually up to the limit permitted by the by-laws what dividend rate, if any, is to be paid on common stock, while preferred stock carries, as a rule, a set rate of interest.

In stock associations the ownership of one or more shares of common stock is usually required for membership and voting privileges. Moreover, the ownership of common stock is often limited to producer members and is restricted as to the amount each member may own at any one time. It is desirable in planning a cooperative to make adequate provisions to assure that the stock will be kept in the hands of active patron members at all times.

Preferred stock seldom carries voting or membership privileges. Restrictions on ownership are seldom placed on preferred stock in cooperative associations. Thus holders of preferred stock are likely to be more interested in the association as investors than they are as members.

Membership Fees.—When the non-stock plan of organization is followed, initial capital is usually provided through membership fees. This plan is less adaptable to associations requiring large amounts of capital;

no doubt, for the reason that people tend to look upon membership fees as charges or donations. An association using the non-stock plan should state members' rights of ownership. Because of the varying amounts of products purchased from or marketed through the association, it is usually provided that ownership rights shall be in proportion to the business transacted by the patron with the non-stock association.

Certificates of Indebtedness (Revolving Fund).—Certificates of indebtedness are issued by some cooperatives as evidence that capital has been invested by members or patrons. The two most common methods of accumulating capital by the use of certificates of indebtedness are: First, to hold back a small amount from each payment for products marketed through the association, and to issue a certificate for that amount; and second, to retain earnings (patronage dividends) which have been prorated but not distributed, and to issue a certificate for a like amount. Certificates of indebtedness, when used as evidence of investments by members in a revolving fund, do have the advantage of keeping the ownership of the association in the hands of active members, approximately in proportion to the volume of business transacted currently with the association. Certificates of indebtedness should be issued with no definite interest rate and no due date. The board of directors then determines each year what proportion of the certificates shall be purchased and cancelled during any year by the association.

OPERATING CAPITAL.—It is possible to obtain operating capital through the ordinary transactions of the business; for instance, when payments are delayed to producers for the products marketed or when accounts payable are due but unpaid, these funds add to the available operating capital of the association.

Surplus and Reserves.—Other methods of building operating capital are: (1) to deduct from the payments to the patrons amounts larger than are necessary for actual expenses; (2) to apply a portion of the earnings or savings to the reserve and surplus accounts; (3) to apply patronage dividends toward stock or certificates of indebtedness.

Sound financing of a cooperative requires the building of reserves which are sometimes referred to as its financial shock absorbers. These funds are the association's protection against financial risks which are not covered in ordinary operating expenses. The desirable size of reserves will, of course, depend upon the nature of the business, the association's operating policies and its general plan of financing. An association should have large reserves if it is engaged in a business in which there are frequent changes in competitive conditions or a great risk of price variation or of quality deterioration.

Loans.—It is unusual for cooperative associations to derive from their members sufficient funds to supply all the capital required at all times. Loans from credit agencies and other sources are therefore necessary. Adequate financing does not necessarily mean complete financing by the members at all times, but the combination of support from members and loans from other agencies which would result in the highest efficiency.

Possibilities and Limitations of Cooperatives

A cooperative selling or purchasing association should not be expected to solve all the farmers' problems. The membership of a cooperative will more likely continue to support the association if the objectives are at least partially attainable. Consequently, it is well to discuss for a moment what we should and should not expect a cooperative to do.

WHAT WE SHOULD EXPECT FROM A COOPERATIVE.—If a cooperative is to continue it must do its job at less cost or at no greater cost to the patron than any other type of business organization can do. This may take the form of giving the same service at a lower cost, greater service at the same cost, or a large amount of service at slightly increased costs. The greater efficiency should result from increasing the volume of products handled, from reducing some of the losses from extensive duplications and competition, and from a greater knowledge of market conditions on the part of the membership.

The cooperative association should be owned by the patrons and members. The patrons should expect to receive the profits or savings made by the association; but they also must accept the responsibility and risk involved in management.

A group of individual operators working through a cooperative are naturally in a better bargaining position than any one of the individuals acting separately. The cooperative is in a position to have a greater volume of business, better knowledge of current prices, contact with more than one outlet for products, and more than one source of supplies.

A cooperative after improving the quality of its products may build a strong demand so that the wholesalers and retailers find it to their advantage to buy the cooperative products. The best examples of this are the "Sunkist" oranges and "Land O'Lakes" butter. These associations have standardized their products and then graded very closely so that neither oranges nor butter goes to market that does not meet those standards. Thus, the housewife can order "Sunkist" oranges on the phone and be sure she is getting quality products. Many elevators in South Dakota have built a reputation for quality products which is recognized and paid for by the terminal markets.

A cooperative is in a position to carry on quality programs with its patrons by paying on the basis of quality, through educational work of the manager, and by proper handling. This may result in higher prices for quality products. The consumer will be more anxious to pay these high prices if they know they are getting quality.

Many of the farmers' products are harvested during short seasons of the year and are consumed throughout the year. Most farmers must sell their products as soon as harvested to get money on which to operate the next year. A cooperative may aid in the "orderly marketing" of farm products. By "orderly marketing" we mean two things: First, the products will be put on the market at the time of year that they are to be used. This prevents the price from going extremely low during harvest season when the farmer sells his product, and also prevents extremely high prices between harvests. Second, "orderly marketing" means selling on the market that is paying the best price; for instance, if Minneapolis is paying more for wheat than Chicago, the wheat should be sold in Minneapolis to give the producer a better price and to tend to bring the

price in the two markets together. This type of marketing has been very successfully done by the large poultry and fruit cooperatives on the west coast.

A cooperative selling farm products is in an advantageous position to let the producers know what kind of products the market wants. The cooperative discovers these demands through its selling experience and then is able to discuss them in membership contacts. If a cooperative finds too many products of one kind on the market, the membership can be informed in many cases soon enough to shift production to a more profitable enterprise. A purchasing or consumers' cooperative can determine what its patrons need and demand that product from the producer.

WHAT WE SHOULD NOT EXPECT FROM A COOPERATIVE.—For many years cooperatives were "sold" to farmers with the claim that a cooperative would fix farm prices at cost of production. Very few cooperatives have been able to do this. Before planning to fix prices three things must be considered:

- (1) Can a few associations control a large share of the products and their production?
- (2) At what price can substantially all the products be sold?
- (3) Is substitution of food products relatively easy or difficult?

A cooperative may with some difficulty gain control of a large share of farm products; but if the price is high enough to cover everybody's cost of production, the farmer with lower costs will expand his production. Since there are between six and seven million farmers in the United States, it is almost impossible to control all of the products and also the production of those products which is so necessary if satisfactory prices are to be fixed. Where price-fixing has been successful, the "fixers" have recognized the above points and in addition have had the entire production located in a small area and produced by a few operators.

Members of cooperative associations must not expect their cooperative to do away with the middleman's services. In the purchasing and selling of products there are several things that must be done, whether it be by a cooperative or by some other type of business organization. These services may be grouped into the following classes:

- (1) Buying—negotiating contracts for purchase.
- (2) Selling—negotiating contracts for sale.
- (3) Transportation—movement of the physical goods.
- (4) Storage—holding products for the best market or to condition for market.
- (5) Standardization and grading—setting up standards and making products conform to them.
- (6) Risk-taking—risks of price change and physical damage.
- (7) Financing—furnish money to pay producer before the consumer has made his purchase.

The cooperative does not eliminate any of these marketing functions. It must do them, or some of them, if it is to be in the marketing business.

How to Organize a Cooperative

If there is ample interest among the people of a community toward the formation of a cooperative association, plans should be started. Every care should be taken, however, to start undertakings under favorable conditions. An essential of success is a membership thoroughly informed on the fundamentals of cooperation. Educational work should be started well in advance of the actual organizing. There may be a question as to who should take the lead. Should the farmers do it themselves? Not necessarily, although this way is better. However, the farmers should participate to the extent that they have a complete understanding of the whole plan. To be successful an organization must spring from a real need. Do the farmers feel there is a real need; is it a real or an imaginary need? Those are questions that should be answered satisfactorily before advancing organization plans too far. When interest has developed to the point where action seems advisable, a meeting of the interested parties should be called. Also, the Agricultural College should be contacted, as it may be able to supply helpful information.

First Meeting.—The first business should be the election of a temporary chairman. Then, the meeting should be open for discussion; points for and against organization should be considered and debated thoroughly. Economic need for the association is the most important and first consideration. If the picture looks favorable up to this point, an investigating committee should be appointed or elected which should gather the following data:

1. Extent of the area, intensity of production, and the volume of the product that was shipped from the community during past years.
2. Estimated amount that can be expected to be handled by the proposed association now and in the future.
3. Estimated probable support of producers in the community from the standpoint of (a) financial support, (b) patronage support.
4. Comparison of the services and facilities made available by the present institutions, their costs and efficiency of operation, with those expected from the new organization.
5. Possibility of a competent manager being hired.
6. Success or failure of past cooperative efforts in the community.

Such a survey will give some definite ideas as to the need for organization and the obstacles that may be encountered.

Second Meeting.—The second meeting is called and presided over by the chairman of the investigating committee. The committee's report is given, and the meeting is then open for discussion. After the committee's report and other problems have been discussed thoroughly, there should be a vote on whether to go ahead with the organization of the association or to drop the idea. If those present are actively in favor of proceeding with organization, the next step is the appointment of several committees.

1. Organization and by-laws committee. Its duty is to draw up the articles of incorporation and by-laws, choose the correct cooperative law, assume the responsibility of reviewing critically all preliminary work, revising and approving plans, deciding the course of action and directing activities.

2. Stock subscription committee. Its duty is to solicit the sale of shares of stock; that is, to obtain signatures of application for membership.
3. Building and equipment committee. Its duty is to investigate and find a suitable location, secure plans for a building, get bids from contractors as to the cost, get bids on equipment. It may be necessary to visit and study present associations.

Meeting of Subscribers.—After the chairman of the organization and by-laws committee is satisfied that all committees are ready to report, he calls a meeting. All subscribers should be given ten days' notice of the meeting, and nonsubscribers should be welcome.

Report of the stock subscription and the building and equipment committees should be given and accepted by vote. The report of the organization and by-laws committee should be given. The articles of incorporation should be read and accepted by vote. The persons forming the association must sign and acknowledge the written articles and send the original to the secretary of state. The articles of incorporation establish the legal status of the association as a corporation. The by-laws should be read section by section; discussion and voting should follow each section, until the complete set of by-laws has been formed and passed. The by-laws of an organization are its working plans, without which it could not be established, much less conducted successfully afterward.

Election of a board of directors for the association from among its members (subscribers) should take place. A meeting of the directors should be held immediately. Election of a president, a secretary, and a treasurer should be the first business. Then other necessary business, such as arranging for the needed physical facilities, equipment, finance, collection of subscriptions, and hiring a manager, should be taken care of.

By-Laws And Articles of Incorporation.—It is impossible to formulate a set of by-laws and articles of incorporation that are general enough to meet all situations. To organize or reorganize a cooperative, it is necessary to consider its special problems or conditions.

Before the preparation of the by-laws and articles of incorporation, a new association should secure by-laws and articles of incorporation from other similar associations which have been successful. Many times information and help may be secured by writing to the State College.

APPENDIX

1. The following is quoted from the

Federal Capper-Volstead Act of 1922¹

"That persons engaged in the production of agricultural products as farmers, . . . may act together in associations, corporate or otherwise, with or without capital stock, . . . Such associations may have marketing agencies . . . : Provided, however, that such associations are operated for the mutual benefit of the members thereof, as such producers, and conform to one or both of the following requirements:

"First: That no member of the association is allowed more than one vote because of the amount of stock or membership capital he may own therein, or,

"Second: That the association does not pay dividends on stock or membership capital in excess of 8 per centum per annum.

"And in any case to the following:

"Third: That the association shall not deal in the products of nonmembers to an amount greater in value than such as are handled by it for members."

2. The following are summaries of the South Dakota cooperative laws.

Cooperative Corporations and Associations, 1913.²

1. Five or more persons may organize an association. (Section 8839)
2. Each stockholder is entitled to only one vote. (Section 8844)
3. Stock ownership is limited to \$1,000 in associations of \$100,000 or less capital stock, and to 1 per cent of the stock in associations of more than \$100,000. (Section 8844)
4. Interest on capital stock shall not exceed 10 per cent.³ (8849)
5. Not less than 10 per cent of the annual net profits shall be set aside for a reserve fund, until an amount has accumulated of not less than 50 per cent of the paid-up capital stock. (Section 8849)
6. Not less than 1 per cent nor more than 5 per cent of the annual net profits shall be set aside in an educational fund. (Section 8849)
7. Balance of the annual net earnings, after necessary deductions are made, shall be apportioned among the stockholders, or stockholders and patrons, in proportion to the amount of business transacted with the association. (Section 8849)
8. The word "cooperative" shall not be used in the title of any business unless organized under Sections 8839-8853. (Section 8850)

Cooperative Marketing Law of 1923⁴

1. Five or more agricultural producers may organize an association. (Section 2)
2. Each member or stockholder is entitled to only one vote. (Section 13)
3. Stock ownership is limited to 1/20 of the issued common stock. (Section 13)
4. Only producers of the products handled may become members or stockholders. (Section 6)
5. Common stock cannot be transferred to nonproducers of the products handled. (Section 13.)
6. Associations shall not handle agricultural products of nonproducers to an amount greater in value than is handled for members. (Section 5a)
7. Associations shall make provision in by-laws for automatic suspension of the rights of membership when a member ceases to be eligible, and for the purchase by the association of a member's interest upon death, withdrawal or expulsion. (Section 9f)
8. Each association shall send an annual report to the Secretary of Agriculture of the State of South Dakota. (Section 17)

1. U. S. Code of 1935, Title 7, Chapter 12, Sec. 291-2.

2. South Dakota Revised Code, 1919 and 1929, and amendments, Sections 8837 to 8853. (South Dakota Revised Code of 1939, Vol. 1, Title 11, Part II, Chapters 11.00 and 11.11.)

3. Eight per cent is now the maximum contract rate of interest for all contracts in South Dakota. Chapter 123, Sec. 2, Session Laws of 1933.

4. South Dakota Compiled Laws of 1929, and amendments, Sections 8007-D to 8007-Y. (South Dakota Code of 1939, Vol. 1, Title 4, Part V, Chapter 4.16.)

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