

The Potential for Non-Agricultural Cooperatives in Rural Communities

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Introduction

In the 1990s, rural development task forces argued that the need for a rural economic resurgence would lead to, and in some areas require, a new wave of cooperative development (Duffey; Egerstrom). Those arguments were based on the belief that cooperatives possess the potential to foster economic growth at the firm, community and regional level. They are supported by the fact that the spirit of cooperation is prevalent in rural areas. According to Castle, a member of the National Rural Studies Committee, “cooperation, both formal and informal, has always characterized group behavior in the countryside. The distances involved and the common problems that must be faced have contributed to the uniqueness of rural institutions” (Castle, p. 367). As direct federal assistance for rural development and agriculture declines, and as agriculture plays an increasingly smaller role in the rural economy, the potential for cooperatives to play a more vital and direct role in rural economic development increases.

One can argue that the structure and objectives of cooperatives compel them to behave differently from other organizational structures in their communities (Fulton and Ketilson). By virtue of being locally owned and controlled, with benefits distributed based on use, cooperatives are considered by some to be an ideal model for rural community development:

Cooperatives are oriented to solving local problems by organizing local people into stable organizations... and [they] have an explicit mission to keep funding, distribution of benefits, and responsibility and accountability in local users' hands (Stafford, p. 85).

Cooperatives are also a way for a group of individuals to pool their limited resources to achieve a critical mass. Individuals who may have been unable to achieve a goal (e.g., start a business, purchase bulk items, etc.) on their own can do so through joint action. In a survey of 162 non-agricultural cooperatives, 44% of the respondents said they could not have opened their business had it not been organized as a cooperative (Bhuyan, Leistritz, and Cobia). Cooperatives “aggregate people, resources, and capital into economic units that overcome the historic barriers to development” (Ziewacz, p. 189).

A USDA report in 1989 found that “The cooperative model has been extremely successful in rural areas and is valid for expanded applications in rural development” (Stafford et al., p. iv). While agricultural cooperatives are common in many rural areas, housing co-ops, consumer co-ops, and the like are less so. Although farmers will often look to the cooperative as a model for new business ventures related to the farm, they and other rural residents often ignore it for non-farm business opportunities (Bhuyan and Olson). There is enough anecdotal evidence to suggest that the cooperative model could be useful for a wide variety of businesses (Nadeau and Thompson; Stafford et al.). In urban areas, and some rural communities, cooperatives provide credit, health care, insurance, education, childcare, and housing, among other services.

Little research has, however, analyzed the true potential of non-agricultural cooperatives in rural development. To better understand the conditions under which non-agricultural cooperatives have played a successful role in rural development fourteen innovative non-agricultural cooperative ventures across the US were studied in 2001. The paper begins with a brief overview of economic development issues, followed by a more pointed discussion of the strengths and weaknesses of the cooperative model. The cooperative business structure has some characteristics that make it an excellent choice for non-agricultural, rural business opportunities and other attributes that can create significant challenges. The research methodology, results, and finally the conclusion, compose the remainder of the paper. The results section briefly summarizes and groups the cases into three categories: successful cooperative ventures; co-ops facing challenging situations; and new opportunities for the cooperative model.¹

Economic Development Issues

In the narrowest sense, economic development involves increasing the number or quality of jobs in a community so that individual and aggregate income expands. Successful employment-oriented strategies can result in the majority of the population feeling that conditions for them and their neighbors have improved. However, misguided efforts can lead to major conflicts within a community. For example, most communities have adopted industrial recruitment strategies that try to convince relatively large firms from regions outside their city or town to move to their location. In many cases, the firms that relocate do so in a way that results in increased employment and income opportunities for the community with no significant local costs. In other cases, the community may face many unanticipated costs: environmental degradation; an influx of new residents creating stress on housing and community services; no net gain in new jobs (many may be taken by new residents); and a significant increase in taxes to cover infrastructure improvements (frequently a necessary condition to attract a new company). In the most adverse situation, the new company closes operations in the community within a few years, before generating significant new tax revenue. The community can be left with an unemployment rate higher than when it first decided to attract a new company (assuming new residents stay) and the remaining, often long-term, costs.

In recent years it has become common to use an expanded definition of economic development that includes various quality of life measures of residents over time. Typical quality of life measures include the distribution of income and employment, changes in tax burden, measures of environmental quality, changes in crime rates and other social indicators, and measures of social cohesion or the sense of shared values within the community. This expanded definition makes it possible to argue that an increase in jobs and income can leave a community worse off if the full effects of the change are considered. However, the relative importance of these measures varies from place to place. Some communities may be more willing to accept larger losses in some categories to gain greater increases in others. While using this broader index makes it

¹ The complete case studies can be found in “*Non-agricultural Cooperatives in Rural Areas: 14 case studies.*” UWCC Case Study Series (Case Study #1, 2003).

more difficult to quickly judge the success of an economic growth strategy, it offers a more complete assessment of development efforts.

The use of a broader economic development definition has led to a shift in development strategies. As the negative consequences of some industrial recruitment cases became clear, communities began to reconsider their economic growth programs. While most cities and counties continue to recruit firms from outside their regions, they are also increasingly likely to implement a business retention and expansion program and a systematic effort to stimulate the formation of new entrepreneurial firms. Business retention and expansion efforts are born from the realization that it is typically far easier and cheaper to help existing local firms prosper than it is to convince an external firm to move to the community. The interest in stimulating the formation of new firms stems from research findings that small businesses have accounted for a very large share of net job formation in the United States over the last decade. Further, when new firms have engaged in fast growing sectors like microelectronics, software, and medical technology, communities have experienced phenomenal increases in local income and employment.

As communities encourage the creation of new business enterprises, the structural characteristics of business firms also need to be taken into consideration. A cooperative firm, by virtue of its structure, could have very different impacts on a community than an investor-oriented firm (IOF). Cooperatives, like all forms of business, have certain strengths and weaknesses. The potential role for cooperatives in rural economic development must include a discussion of the model's limitations.

Strengths of the Cooperative Model for Non-Agricultural Ventures

(1) Community Interest

From a local development perspective, a critical feature of the cooperative model is that it can be owned and controlled by community residents. Thus, a cooperative is more likely to be interested in promoting community growth than an investor-oriented firm (IOF) controlled by non-local investors. Further, since the residents control the firm, they can ensure their objectives are met. Privately-held firms and small limited liability companies (LLCs) share this strength with the cooperative model, since they can also be locally owned and controlled and could also be interested in promoting community economic development. Further, in all three cases, assuming a largely local trading area, economic development translates into increased business revenue.

(2) Flexible Profit Objectives

Unlike IOFs, most cooperatives do not have to be concerned about share value and maximizing investor returns. Their objectives are set by their members and may not include profit maximization at the firm level. Indeed, many non-agricultural cooperatives are created to serve a local need, not to generate investor returns. Consequently, cooperatives may be more likely to stay in the community. IOFs can be under considerable pressure by investors to grow as fast as possible because this maximizes their return on investment. As a result, the business may outgrow the community in

which it was established and relocate to a place where the supply of labor is larger and other inputs can be more easily and efficiently obtained.

(3) Financial Advantages

Cooperatives are eligible to apply for loans and grants from a number of federal and state agencies designed to support co-op development. This can provide a significant source of low cost start-up and operation funds for the cooperative business. In addition, there are other non-governmental financial intermediaries (e.g., cooperative banks) that provide relatively low cost loans to cooperatives either because they are chartered to do so by the federal government or because they have been established to assist cooperatives and non-profit firms. Cooperatives can also benefit from significant tax advantages. If firm profits are distributed to members, they will not be taxed as income at the firm level.

In certain situations, cooperatives may also face lower labor costs. In many consumer and service co-ops, members are willing to invest some of their labor instead of the traditional equity investment. Members typically provide a certain number of “free” labor hours as part of their membership fee. Members may also be willing to volunteer their time when they believe that it provides a significant cost saving for the cooperative, or where there is a strong common bond that provides a social benefit to members from associating with their peers. In addition to the financial advantages non-compensated member labor may provide, it also helps maintain member involvement in and knowledge of the operation of the cooperative.

Weaknesses of the Cooperative Model for Non-Agricultural Ventures

(1) Management and Leadership Issues

The leaders of the cooperative, the Board of Directors, are drawn from the cooperative membership. This creates a challenge: finding members with the ability (appropriate skills) and the willingness (the time for and interest) to serve as a director. While finding able directors is generally not a problem for most cooperatives, it can be a significant difficulty if the business grows or if it engages in more sophisticated marketing and finance systems. In these circumstances, it may be difficult to find potential Directors who have adequate knowledge and expertise to keep the co-op operating efficiently. To overcome this challenge, cooperatives need to invest in financial and other types of training for their directors. In some cases, this may require substantial financial commitments. Finding members willing to serve is a more frequent problem, especially for large cooperatives. Since no individual member owns a significant share of the cooperative business, and often their co-op investment represents a small share of their personal wealth, their incentive to take an active interest in the business is reduced. Cooperatives willing to sufficiently compensate directors for their time have a better chance of finding new directors.

Since most cooperatives try to operate with a very slim profit margin, there is often a reluctance to compensate managers at the same rate as IOFs. Further, cooperatives cannot rely upon stock options as a compensation mechanism, which therefore increases

their direct compensation requirements. Consequently, cooperatives can have a difficult time attracting qualified management.

With a more decentralized leadership structure, cooperatives often take longer to make business decisions than IOFs. Some boards of directors may want to be involved in all business decisions, relegating little to management. Others may focus on larger issues, but may delay decisions because of insufficient information and fear of making the wrong move. Inability achieving a consensus among board members can also constrain efficient decision making within cooperatives. Although it depends on the cooperative's specific by-laws, most decisions that could significantly affect the future of the cooperative (e.g., mergers or changes to leadership and bylaws) have to be brought before the membership for approval. Building a consensus among members to support some decisions may also take time.

(2) Business Creation and Growth Difficulties

One of the major impediments to the creation of new cooperatives stems from the fact that a large section of the population remains unfamiliar with the model. People who are familiar with cooperatives tend to think of using the model only for the specific context in which they are already in use. For instance, those familiar with agricultural cooperatives may not readily understand how the cooperative approach could be used for housing. Consequently, the cooperative model may not be frequently considered when a new business venture is being discussed. For those who do wish to form a cooperative, they may have difficulty finding lawyers, accountants and lenders with sufficient cooperative knowledge. Cooperative business regulations are not uniform across states, further complicating the process. Given these factors, and the fact that forming a cooperative involves building mutual interest and trust among a group of people, organizing a cooperative can take much longer than creating an IOF. In contrast, there is a well functioning process that links public firms with potential investors.

Once a cooperative has been established, further growth may be restricted because of limited access to internal equity capital. While it is possible to increase equity by asking members to make additional contributions, this is a difficult and often unpopular path. Further, for most cooperatives, membership shares cannot be transferred and have no intrinsic value. The new generation cooperative (NGC) structure includes transferable delivery rights (based on strict delivery contracts) and substantial up-front equity investments by members (Zeuli and King). These structural modifications were made to counteract the equity problems that typically plague traditional cooperatives.

(3) Difficult Transfer of Ownership

At some point in time, the cooperative business may no longer optimally fit the cooperative model. It may be too large and thus, become restricted by a distant and fractured membership. Or, as generations pass through, it may simply have lost touch with its cooperative identity. The members (and management) may decide they no longer want to operate the business as a cooperative. However, transforming a cooperative into an IOF can be difficult, requiring all members to sell their membership shares and provoking difficult decisions regarding the handling of unallocated equity.

Research Methodology

Contacts at cooperative development centers, university cooperative centers, and state cooperative trade associations, helped identify innovative non-agricultural cooperatives involved in rural development activities. An effort was made to find cooperatives in sectors that had the greatest potential to stimulate local economic growth. While consumer and service cooperatives, such as those involved in housing, day care and groceries, play important support roles in a local economy, they are not major engines of economic growth. Fourteen cooperative organizations were chosen based on the following factors: (1) location (they represent rural areas in different regions across the US); (2) the innovativeness of the business; and (3) the local economic development impact (table 1).

The case studies involved visits to the cooperatives and detailed interviews with co-op managers, board members, and key community individuals. A sample questionnaire, which was modified somewhat to fit the position of the person(s) being interviewed, is attached (Appendix). The data gathered through the interviews and secondary sources included information on the following:

- Management/organizational structure of the cooperative
- Cooperative membership statistics
- Capitalization of the cooperative
- The cooperative's rationale for engaging in economic development activities
- Description of the primary activity of the cooperative
- Description of economic development activities, both qualitative and quantitative (to the extent possible), undertaken by the cooperative
- Description of the cooperative's impact in the community/region
- Other factors cooperatives identify as important to their economic development role

By virtue of the selection criteria, all fourteen case studies represent innovative, non-agricultural cooperative ventures serving rural communities. The case studies include cooperatives that have (independently or jointly with other cooperatives) created new economic development ventures unrelated to their core business. Many of these examples are rural electric cooperatives that have financed and organized new small businesses, which may or may not be organized as cooperatives. Other cases cover cooperatives whose core business is an innovative approach to local economic development; for instance, an artist cooperative that operates a local gallery. These cooperatives tend to exist outside the mainstream cooperative movement and have very limited or no contact with other cooperative organizations. Finally, a set of cases that represent new opportunities for the cooperative model were also studied. They comprise examples of development initiatives where many of the core features of a cooperative characterize the firm but a cooperative model was not chosen.

Table 1. Cooperative Case Studies		
Name of Cooperative (and development venture)	Location	Economic Development Activities
Northern Electric Cooperative (Lefse Shack)	Opheim, Montana	Specialized bakery
Northwinds Publishing Company	Great Falls, Montana	Printing and publishing
Flathead Electric Cooperative (Evergreen Rail Industrial Park)	Kalispell, Montana	Industrial park
Rural Electric Cooperative (Country Living Homes)	Lindsay, Oklahoma	New house construction
Central Iowa Power Cooperative (Iowa Capital Corporation)	Cedar Rapids, Iowa	Business recruitment, venture capital, etc.
Pee Dee Electric Cooperative (Pee Dee Electricom)	Florence, South Carolina	Business recruitment, industrial park, etc.
Foodworks Culinary Center	Arcata, California	Kitchen incubator program
The North Coast Co-op	Arcata, California	Full service grocery store
Northcoast Artists	Fort Bragg, California	Art gallery
Salmon Trollers Marketing Association	Fort Bragg, California	Collective bargaining and lobbying for salmon trollers
Rural Wisconsin Health Cooperative	Sauk City, Wisconsin	Promotes and provides rural health care
Garrett Rural Information Cooperative	Garrett County, Maryland	Internet service provider
Locally Owned Business Organization	Grand Junction, Colorado	Promotes locally-owned businesses in the county
Northern Colorado Water Conservancy District	Loveland, Colorado	Manages water transfers from Colorado river

Case Study Results

The selection process created a somewhat biased sample. Almost every case represents a relatively successful business venture. Failed efforts would have been more difficult to find and indeed, only two were unintentionally identified, the Locally Owned Business Organization in Colorado and the Foodworks Center in California. In addition, failed co-ops would have been less useful for this research since the primary purpose was to identify a set of factors or conditions that enable cooperatives to be *successful* rural economic development agents. The case studies do in fact represent different degrees and types of success.

Analysis of the case study results revealed several factors or conditions that made some of the cooperatives particularly successful ventures. In the aggregate, these elements seem to support the following proposition: the co-op's degree of success is related to how well they have compensated for the disadvantages of the cooperative model in their

unique business environment. Therefore, the case studies can be divided into three categories.

The first category includes those cases that represent clearly successful cooperative ventures, from both business and community development perspectives, which are stable organizations with good prospects for long-term viability. They include the following six cases: The Lefse Shack; North Coast Co-op; Rural Wisconsin Health Cooperative; Northcoast Artists; Pee Dee Electricom; and Evergreen Rail Industrial Park.

The second category includes five ventures that represent more complex cases. In most instances, the organization is a relatively successful business and yet there is some question about the stability and long-term viability of the firm as a whole or as a cooperative. The cooperative model seems to be creating more challenges than opportunities for these businesses. In some cases the problems occurred early on in the life of the business while in other cases they developed after the business had been in operation for some time. The following cases are included: Garrett Rural Information Cooperative; Country Living Homes; Foodworks Culinary Center; Iowa Capital Corporation; and Northwinds Publishing Company.

The third category includes the three cases that represent new opportunities for the cooperative model—development initiatives where many of the core features of a cooperative characterize the firm but a cooperative model was not chosen. Each of these organizations performs a significant economic development function and acts to advance the public interest. These can be viewed as having failed to overcome a significant disadvantage of the cooperative model in non-agricultural, innovative areas: its relative obscurity. The Northern Colorado Water Conservancy District; the Salmon Trollers Marketing Association; and Locally Owned Business Organizations comprise this third group.

The following briefly summarizes the findings from each case study in the context of the three categories described above.

Success Stories

The Lefse Shack

Granrud's Lefse Shack specializes in the production of lefse, traditional Norwegian potato bread. This specialized bakery is a c-corporation, operated as a wholly owned subsidiary of Northern Electric Cooperative (NEC), a rural electric cooperative with headquarters in Opheim, Montana. NEC bought it when the original owners of the Lefse Shack wanted to retire and sell the business and no local buyer emerged. The only other potential buyers intended to move the business out of Montana. Although the Lefse Shack is a relatively small business, the loss of the 27 jobs it provided would have been significant in the town of Opheim, where it remains one of the larger employers. The firm typically generates annual profits that are returned to NEC, its sole stockholder.

This case presents a successful example of the expansion of an existing cooperative into a new, unrelated activity. Certainly other cases of cooperatives purchasing failed investor-oriented firms (IOFs) exist. A successful sugar beet cooperative in Minnesota was created by this method. More recently, however, cooperatives have purchased firms that are unrelated to their core business (e.g., gas stations and tire stores) in an effort to maintain services and jobs in their local community. Because the Lefse Shack is a small firm that produces a single product with a well-established market, it was relatively easy for NEC to maintain those operations. The cooperative was not required to learn a great deal about the production or marketing of lefse. Further, NEC was able to provide accounting, legal and maintenance services at lower rates than the Lefse Shack was able to obtain as an independent business. Finally, because the Lefse Shack remains an independent corporation, NEC has retained the ability to sell the business at a future date if it becomes a financial burden or members lose their commitment to the project. This would enable NEC to potentially recoup some of its expenses rather than having to dissolve the firm if it were structured as a cooperative.

North Coast Cooperative (NCC)

Located in Arcata, California, NCC is an example of a consumer cooperative that has expanded from simple bulk distribution for a small group of members to operating two large full service supermarkets and providing significant financial support to local social and cultural organizations. NCC has also worked continually with local agricultural producers to build supply chains and improve the diversity and quality of local food production. This has provided their customers with a better variety of local products and also stimulated new investment in and production activities on local farms. NCC's steady expansion placed it in a position to compete with other larger chain supermarkets in the area. NCC's commitment to local economic development is reflected in its philanthropic and volunteer activities. It operates a foundation, the Co-op Community Foundation, that donates money to a wide variety of community organizations and causes. Members can donate directly, or sign over their cash discount and/or patronage refund to the foundation.

While various consumer food cooperatives exist around the country, they tend to be small, fringe players in their local markets. NCC's ability to compete and act as a competitive yardstick improved the product selection and reliance on local products for all area consumers. NCC's interest in local agriculture created a dual-development impact. NCC provides important employment opportunities for local townspeople (Arcata is a relatively poor town) and equity for cash-poor organizations. It further helps bolster a dwindling local agricultural sector, providing markets and support for a more diverse agriculture. This devotion to the community, its ability to grow and yet stay in the same physical location, and its continuity in management, helped maintain member interest as NCC grew. The senior management has been with the enterprise since its early days and has been able to grow with the organization, now providing leadership to a large, complex organization. This leadership and a committed and stable membership helped the co-op overcome capital constraints to growth. Established in 1973, NCC is now entrenched in the local community.

The Rural Wisconsin Health Cooperative (RWHC)

Located in Sauk City, Wisconsin, RWHC provides a variety of personnel, billing and other services to its member hospitals. It was originally created to help small rural hospitals identify and recruit healthcare professionals. By aggregating the demand for this function, RWHC was able to perform it more efficiently. Since then, RWHC has expanded its functions to include insurance reimbursement services, doctor credential verification and a rural health policy advocacy role.

RWHC is a good example of how well a cooperative structure might be used in an area where other forms of organization are more common (e.g., trade associations and non-profits). While a different form of business may have been able to deliver the same services, the founders of RWHC believed the cooperative form offered advantages in the form of assured equal footing and better direct ownership links between the hospitals and RWHC. In that part of the country, the cooperative model is fairly well known and a cooperative development infrastructure exists. The cooperative has been able to survive by refining its mix of services to meet the changing needs of members. Its ability to do so again relates to excellent, stable leadership (the manager helped create the co-op), a stable, relatively small and homogeneous membership, and regular communication between the two parties.

Northcoast Artists

Located in Fort Bragg, California, the Northcoast artist co-op operates a gallery that displays and sells members' work. The co-op was formed by local artists in the mid-80's in an effort to market their work to a broader audience while retaining a greater percentage of the retail sales price than existing independent galleries offered. While Northcoast historically has had few direct ties with the Fort Bragg community, it recently joined the Chamber of Commerce and is helping promote the work of other local artists through joint events.

Northcoast Artists represents a well-organized cooperative that creates new markets and captures more profit for its members. It shows how cooperatives can participate in traditional local business organizations, such as the Chamber of Commerce, to help the larger community. Its success is due in part to its small, stable and homogeneous membership (about 20 artists with very little turnover). Members keep engaged through compulsory meetings and gallery work. This helped the co-op avoid major internal conflicts (a characteristic problem with artist co-ops that involve members working in different mediums) and keeps the gallery focused on member needs. The co-op also found a unique solution to the management problem. The members run the gallery as a collective; no management or non-member labor has ever been hired.

Pee Dee Electricom

Pee Dee Electric, a rural electric cooperative with headquarters in Florence, South Carolina, first established Pee Dee Electricom as a for-profit subsidiary that would sell local digital television services. This enterprise was eventually sold and Electricom now

functions as the co-op's property development arm. Electricom is currently developing Commerce City, a 717-acre industrial park that will serve a six county area.

While other cooperatives have developed industrial parks, the complexity of this park and its scope of functions make it distinctive. Most importantly, Pee Dee Electric co-op has been able to broker a partnership with local city and county governments to jointly support the park. This was possible since these parties viewed the cooperative as a vital part of the community with no ulterior motives. The co-op overcame capital constraints with financing from the Cooperative Finance Corporation, a specialized cooperative intermediary, and through the use of some of its own capital. Its members understood the potential for long-term gain, since the return on the co-op's investment will not likely materialize for years. A particularly innovative aspect of the co-op's development effort is incorporating local universities and community colleges into the firm recruitment process. Once again the vision and experience of the cooperative, as well as its positive reputation within the community, were instrumental in obtaining the support of these local partners.

Evergreen Rail Industrial Park (ERIP)

ERIP, another industrial park example, is located in Kalispell, Montana. It is owned and operated as a subsidiary of the Flathead Electric Cooperative. As in the Pee Dee Electricom case, the cooperative is interested in developing the industrial park both as a means to directly stimulate demand for electric power as well as to improve economic conditions in the community. Again, like the Electricom case, Flathead was only able to develop the ERIP site because it had established a strong relationship with the city of Kalispell. At that time, Kalispell received its power from another utility. Because the sewage treatment plant in Kalispell was near peak capacity, the city had placed restrictions on further local development. ERIP was given permission to develop because of Flathead's close ties to the community and its previous contributions to community development.

Challenging Cases

Garrett Rural Information Cooperative (GRIC)

Garrett Community College (GCC) was instrumental in the creation of GRIC, an Internet service provider (ISP) co-op located in Garrett County, Maryland. GCC recognized the importance of providing local Internet connections for its students and the community at large. Prior to GRIC, local residents were forced to pay long-distance connection charges. GCC provided an initial home for GRIC and still houses the server, computer equipment, and technicians (who also work for GCC). GRIC has since established its own identity and moved its administrative offices out of GCC. A cooperative model was chosen for GRIC because it retained local ownership and control within the community and because it avoided potential problems for GCC associated with creating an IOF. Some of GRIC's initial founders (GCC employees) were raised on farms and were familiar with agricultural cooperatives and this led them to the cooperative structure.

The ISP industry has evolved to the detriment of GRIC. It is an industry dominated by a small number of large national firms with enough capital to make substantial investments in technology subject to rapid obsolescence. Consequently, the opportunities for a small ISP have diminished and GRIC faces the challenge of having to either make a major capital investment to keep pace with current technology or possibly dissolve the business. As discussed above, finding substantial capital can be a significant challenge for cooperatives. GRIC also had difficulty creating a cooperative identity among its members. Most members, as well as the current management, have little knowledge about the co-op model and are unclear as to its benefits. Since GRIC is a cooperative, selling the firm would be difficult.

Country Living Homes (CLH)

Country Living Homes is a corporate subsidiary of Rural Electric Cooperative (REC), a rural electric distribution cooperative located in Lindsay, Oklahoma. Rural electric cooperatives in Oklahoma recognized that a shortage of affordable housing was limiting economic development in rural communities in their service territory. To address this problem, a group of eight cooperatives developed a plan to jointly form and own a new housing construction and property development cooperative. After considerable discussion this effort was abandoned, in part because existing state law did not allow the cooperatives to proceed with a joint subsidiary cooperative, and in part because the mechanics of coordinating such an investment were formidable. REC decided to proceed with the idea independently and created CLH. REC had previous experience with forming subsidiary companies for economic development purposes and considered a housing construction firm a viable business opportunity that its members would support. Initially they intended to focus on building moderately priced speculative homes. However, they found that a significant niche existed for steel frame homes since no local builders were involved in such construction. Therefore, CLH began to focus on building higher-priced custom homes. Although they have only been building homes for about one year, they have a backlog in orders.

CLH is particularly interesting because it represents a successful business that was not, however, successful when structured as a type of federated cooperative. While this type of structure, owned by several cooperatives, had the potential to reach a larger group of customers and hence create more profits, it proved impossible to implement because of state specific legal restrictions and because several of the cooperatives balked at the cost of capitalizing a firm that would be large enough to operate on a state-wide basis. Instead a smaller project was undertaken, with a clearer focus and simpler structure. This new model still faces some restrictions because it is a subsidiary of a cooperative, but it has demonstrated rapid growth and has significant potential as a model to be adopted in other areas.

Foodworks Culinary Center

The Arcata Economic Development Corporation (AEDC) established Foodworks as an incubator for small food processing companies and a place for a shared community kitchen. It was structured as a cooperative to encourage incubator tenants (the co-op members) to work together and capture joint procurement and joint marketing

efficiencies. The co-op model is well known in Arcata and the AEDC CEO at the time had significant experience working in the co-op sector. When it was created, AEDC believed that the members would take over the facility after about five years, which did not happen. Further, although some businesses graduated and moved into the community, many of the original members are still located in the incubator. AEDC is now trying to sell the facility.

Foodworks illustrates the type of problems that can arise with a top-down cooperative model. While all the tenants are engaged in some form of food processing, there are very few synergies among them. The founders at AEDC assumed they could find common interests by virtue of all being food processing firms. The businesses, however, identify more with their product than the general business and thus, the intended opportunities for collaboration and joint activity never materialized. Further, the members are more interested in growing their own business than in strengthening and managing the cooperative. Indeed, their focus on personal business profitability encouraged behavior that was not compatible with the viability of the cooperative. For example, initially utility expenses were jointly shared, but some businesses used far more resources than others, causing conflicts that required an expensive remodeling of building utilities. In sum, because individual interests overwhelmed the common interest, the inherent strengths of the cooperative model were never realized.

Iowa Capital Corporation (ICC)

The Central Iowa Power Cooperative (CIPCO) is an electric generation and transmission company based in Cedar Rapids, Iowa. In addition to its core business of providing power to its parent distribution cooperatives, it operates a comprehensive economic development program that includes recruitment functions, land development and a construction management enterprise. As part of this program, CIPCO also operates ICC, a subsidiary venture capital firm. ICC was initially capitalized by CIPCO, Corn Belt (another Iowa generation and transmission cooperative), and the state government for the purpose of loaning capital to Iowa businesses. Several years after ICC was established, CIPCO bought out the state and Corn Belt interests because of the difficulty inherent in managing a venture capital firm where the partners had conflicting goals. CIPCO manages ICC with the objective of maximizing the internal rate of return. While local economic development impacts are a significant priority, they are secondary to profitability.

ICC was more successful with its early investments than initially anticipated and CIPCO used a portion of the revenue to cover costs in its core generation and transmission business. The management of ICC would like to increase the venture capital pool to a more efficient size. However, such future business growth is limited because the fund is part of CIPCO, a slow moving conservative organization. An equity institution modeled as a cooperative theoretically could help avoid the problems some institutions face as they try to balance financial and development objectives. Since the cooperative does not require the same rate of return on its investments as an IOF, it might choose to make an investment that is beneficial to the community and not the bottom line. ICC does not

represent such a model and instead seems to be hindered by the cooperative structure of its parent company.

Northwinds Publishing Company

Northwinds was formed by a group of rural electric and telephone cooperatives in Montana to control their printing and publishing expenses and generate additional revenue. Rather than invest a lot of initial equity in the venture, the cooperatives agreed to guarantee the loans the company took out to buy equipment and a building. The seven general managers of the participating cooperatives became the board of directors for the business (structured as a joint venture) and a manager was hired. Plans to attract business from other printers in the area were unsuccessful and losses mounted. While some of the partners wanted to close the company, this would have triggered the loan guarantees and it seemed cheaper to invest more money in the form of equity and reorganize the business. However, after more losses, several of the cooperatives abandoned their investment and withdrew from operating the firm. The remaining co-ops decided to sell the business, which was unsuccessful. Eventually, after a new manager was hired and the size of the firm was significantly reduced, the firm was once again profitable.

Northwinds illustrates the consequences when cooperatives embark on new joint ventures with inadequate planning and weak management. The cooperatives that invested in Northwinds failed to conduct a careful market analysis and underestimated the competition they would face. In addition, the general managers had too many other obligations at their co-ops that precluded them from effectively supervising the new company. The decision to finance Northwinds through debt rather than equity resulted in short term savings for the parent cooperatives but ultimately exposed them to large future investment obligations (that made dissolving the firm a much more difficult choice) and gave Northwinds a significant debt service burden.

Opportunities for Cooperative Development

Northern Colorado Water Conservancy District (NCWCD)

In 1937 the state of Colorado gave legislative authority for the establishment of water conservancy districts. These districts established a tax- based revenue source for water supply projects. Members of NCWCD include city and county governments and a number of irrigation groups. While the original purpose of NCWCD was to finance water projects, it has since taken on expanded functions. NCWCD has been able to act as a neutral party, helping to resolve inter-jurisdictional disputes. This function has become significant enough to merit additional resources being devoted by NCWCD to facilitating water-use conflict resolution. NCWCD has also become a regional planning agency for its members, estimating future demands for water.

Like most cooperatives, water districts were created to meet a common need that required collective action. Since the districts have specific powers delegated by the state government, this could pose some challenges to the cooperative model. However, today many local governments are forming shared service cooperatives and overcoming these

types of challenges. The opportunity to create natural resource cooperatives should not be overlooked.

Salmon Trollers Marketing Association

Located in Noyo Harbor, California this association represents approximately 60 local fishermen. Although the Association was originally organized to bargain with fish plants to obtain better prices for its members, this is no longer its primary function. As the number of fish plants declined and government regulation increased, the focus of the Association shifted to lobbying on behalf of its members to ensure more informed regulations. The Association faces a free-rider problem: many local fishermen are not members of the association and most members have little involvement in the work of the Association. When the Association was bargaining over price and delivery terms it was able to exclude non-members from at least some of the benefits it created. The association may actually be performing a more valuable function now because it is the only organization representing the interests of fishermen in a policy process that deals with a lot of competing pressures. In its current function, the cooperative business model would probably not make the Association any more or less successful.

Locally Owned Business Organization (LOBO)

A group of small business owners in Grand Junction, Colorado established LOBO as a non-profit corporation to promote small business development in the community. The founders believed that the only way they could compete effectively with large chain stores was to increase their numbers and market share. Member firms and their employees received discounts at other members' businesses and the organization publicized the contribution that small business owners make to the community. Although there were potentially 5,000 members in the county, LOBO was able to attract only 62 firms, which was well below the 100 it needed to be financially sustainable. Part of the problem was convincing potential members that they would receive adequate value for their dues. Another problem was fear by the local Chamber of Commerce that LOBO was competing for members. Finally it was difficult to sell the concept that small business is good for community development. After one year of operations, LOBO became inactive.

While LOBO was not organized as a cooperative, its structure and behavior were very amenable to the cooperative model. Adopting a cooperative structure may have helped LOBO survive. The cooperative structure could have attracted more members who would be assured of equitable ownership and control. This also would have more clearly distinguished LOBO from the Chamber of Commerce. Finally, LOBO could have taken advantage of a variety of services available to cooperatives.

Conclusions

The set of case studies analyzed for this research provides some general insights into the potential impact cooperatives can have on rural economic development. A few cases also illustrated new areas for cooperative development. Clearly, the cooperative model can be adapted to fit a wide range of business ventures. Most importantly, however, the cases suggest how cooperatives can become more successful in their economic development

role. Succinctly stated, the co-op's degree of success is related to how well they have compensated for the disadvantages of the cooperative model in their unique business environment. The following discussion proposes some other general observations on indicators of success.

Perhaps one of the most important observations is that community support for the cooperative and/or its new venture is key to its viability and success. This was especially evident in the industrial parks created by rural electric cooperatives. The parks could not have been created without the support of the local community, especially the local government. Local support can provide the cooperative with a competitive advantage over external firms seeking to undertake the same enterprise.

Cooperatives are able to gain such support when their work clearly benefits both the members of the cooperative and the rural community at large. Cooperatives that want to engage in business that places them in direct competition with small locally owned firms are clearly at a disadvantage. This seems to have been part of the challenge for Northwinds Publishing. Cooperatives seem to have an easier time gaining community support when they purchase an existing business that the community would like to see remain, but which has no other potential buyers, such as the Lefse Shack.

In some instances, the cooperative will have to work on educating their community regarding the benefits of cooperative businesses in the local economy. For instance, in the Garrett Rural Information Cooperative case, the members and management seemed unaware of these benefits. Local citizens, therefore, would probably be unlikely to continue their patronage of the co-op if a large national Internet service provider offered lower cost service. Community support for existing co-ops is also essential for their future growth and viability.

One barrier opposing any business growth, including cooperatives, is lack of equity capital. Equity capital is necessary not only for the creation of new business ventures, but also for the financing of business expansion (Gaston; Parker and Parker; Thompson and Bayer). Innovative rural equity institutions have been created in some regions to fill the need for equity capital in rural areas, although not all have been successful (Barkley et al.). Another novel approach is direct investment in local communities by existing, equity-rich cooperatives such as rural electrics. The future of rural electric cooperatives is tied to the future of their rural communities. The case studies included several rural electric cooperatives that have financed and organized successful new small business ventures in rural towns.

Excellent communication among members and between members and management also seems to be an important hallmark of success. Required, regular meetings seem to be effective, as was evident in both the Rural Wisconsin Health Cooperative and Northcoast Artists cases. Membership ambivalence and feuding are often problems for larger co-ops and those with a very diverse membership. In a cooperative with few members, everyone usually knows each other and personal ties can be relied upon to facilitate operations and resolve problems. In a cooperative with several thousand members, more formal

management procedures may have to be employed. Although smaller cooperatives have an inherent advantage in maintaining open communication, they still have to invest considerable effort in ensuring that it takes place. Communication is also an important issue for subsidiaries and parent cooperatives.

Not surprisingly, the presence of visionary and strong leadership was evident (and indeed seems to be a necessary condition) among all the successful ventures. In most of the cases involving the creation of independent cooperatives (instead of spin-offs), the co-op was initially championed and led by a small group of individuals, often one person. Their vision and commitment was necessary to overcome initial obstacles. In several cases (e.g., Rural Wisconsin Health Cooperative), the initial leader remained as manager, providing continued vision and stable leadership. Without strong management (e.g., Northwinds) the business often fails, especially when it operates in a new sector. Strong management can also stem from the members themselves, as in the Northcoast case. Northcoast members became very informed about the operation of their business, which proved to be an asset to the cooperative.

In most of the cases, successful cooperative spin-offs were created as wholly owned, non-cooperative subsidiaries. While this may seem a violation of cooperative principles, it can be a prudent business practice. In the case of Country Living homes, an attempt to create a cooperative owned by other cooperatives was in fact intractable, making the creation of a joint venture impossible. The Iowa Capital Corporation and Northwinds examples also illustrate the difficulty of creating joint ventures among parties with different objectives and long-term interest levels. Because new activities are typically removed from the core mission of each cooperative, establishing and operating them are difficult and finding common agreement on business strategies can be impossible. Several of the cooperatives with subsidiaries had already sold earlier spin-offs to investors and were using the proceeds to fund their new ventures.

The subsidiaries are also managed somewhat differently than the parent co-op. Since the subsidiary's function (e.g., making Lefse) does not directly serve member needs, it must be able to generate profits for the members (or at least not drain the parent co-op reserves). Therefore, the subsidiary is typically operated with a clear profit maximizing strategy. As stated above (p. 4), cooperatives often have multiple objectives. Maximizing member returns may not always be the same as maximizing firm profits.

Several of the cases illustrated the importance of having a clear exit strategy and understanding the conditions that will trigger it. In some cases, such as with the ISP sector, market evolution removes the primary need for the cooperative. Successful ventures either exit or find a way to adapt to these changes. For example, the Salmon Trollers began to focus on lobbying rather than price negotiation. Clearly, they have been able to provide another vital service for their members. The inability to identify other essential services for members should be cause for considering an exit strategy. This may be the case with the Garrett Rural Information Cooperative. Market changes may not be the only cause for difficulties. Business growth that requires more capital and demands increasingly sophisticated management may create significant challenges for a

cooperative. When the strengths of the cooperative model begin to be outweighed by its weaknesses, the sensible thing to do may be to disengage and sell the firm or dissolve.

Finally, as the three “new co-op opportunity” cases illustrate, the cooperative model is still largely unknown and often misunderstood. It suffers from a lack of familiarity and from its strong association with agriculture and small-scale consumer services. Even in communities where cooperatives provide important services, often there is little awareness about the cooperative model in general or even knowledge that local firms have a cooperative structure (again, this is exemplified in the Garrett Rural Information Cooperative case). Clearly, more education on the cooperative model is warranted in rural areas. Related to this issue is the difficulty some of the innovative cooperatives had in gaining access to services (e.g., credit, technical assistance, etc.) that are more readily available to main-stream cooperatives. If the cooperative sector wants to expand its membership it will have to find ways to be more open to cooperatives that do not fit the standard models.

A critical mass of local knowledge and experience with cooperatives is also needed to successfully create new cooperatives. This not only includes citizen awareness of the potential of cooperatives, but it extends to the presence in the community of professionals such as attorneys and accountants who are familiar with cooperatives. However, it should be recognized that a top-down approach to cooperative development is difficult to implement successfully. In the Foodworks case, for example, the member businesses were not cooperative and therefore, the creation of a cooperative was artificial and ceased functioning fairly quickly. The incubator has continued to function because of management by an external entity. Cooperatives work best when they are the idea of future members.

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Appendix

Cooperative Interview Schedule

Background Information on the Cooperative

1. What are the origins of the cooperative and its mission? Has the mission changed since the cooperative's inception?
2. What are the cooperative's main activities?
3. How is the cooperative financed?
4. Does the cooperative have a specific geographic focus?
5. Describe the membership of the cooperative:
Number of members:

Changes over the past five years:

Socioeconomic make-up of the members:

Membership open?
6. Can non-members use the cooperative?

7. What subsidiary organizations does the cooperative control or participate in?

8. Where do you think the cooperative will be five years from now in terms of membership, activities, service territory, etc.?

9. What factors constrain the operation of the cooperative?

10. Is the cooperative considering any new investments?

Information on the “Innovative Activity”

1. Why did the cooperative choose to get involved in this activity?

2. History of this involvement

Activity first considered:

Activity first initiated:

Relationship to cooperative:

3. What other organizational forms were considered to achieve the same end and why were they not implemented?

4. Are there other partners in this new venture? If so, how were they identified and what share do they control?

5. How was the new venture financed?

6. How easy was it to arrange this financing?

7. Was there opposition within the cooperative to this action? Was there external opposition?

8. Were there models considered in setting up this venture and, if so, what were they and how did you identify them?

9. What problems were encountered in establishing this organization and how were they resolved?

10. Has the organization changed its structure or function since it was created? If so, how?

11. How satisfied is the cooperative with this investment?

12. Would the cooperative repeat this investment, knowing what you know today?

13. What would the cooperative do differently if the investment were made today?

14. What are the main opportunities for the new investment? What are the major problems?

15. Does the cooperative contemplate exiting the investment? If so, when and how?

16. How profitable is this activity and how are profits and losses allocated?