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Agricultural Cooperatives: Part 1 The Development and Significance of Agricultural Cooperatives in the American Economy

Part I

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NOTES

AGRICULTURAL COOPERATIVES

Part I

The Development and Significance of Agricultural Cooperatives in the American Economy

At the close of the 1949-50 marketing season, there were 10,035 agricultural cooperative organizations in the United States.[1] Their membership exceeded six and one-half million persons, representing participation in cooperation by an estimated three out of every five farmers in the country.[2] Total business for the season amounted to more than eight and one-half billion dollars;[3] approximately thrice the volume of a decade ago.[4]

This present economic prominence is the result of an evolutionary growth which may be traced in its entirety through many centuries. Group effort in economic enterprise was advocated in ancient communal societies, in the guilds of the Middle Ages, and in the writings of Plato, More, and Bacon.[5] Following the Industrial Revolution, cooperation became a socio-reformistic movement led by Blanc, Fourier, and Owen to alleviate the sordid conditions under which early industrial employees lived and worked.[6] The emergence of the basic tenets of modern co-operation is generally attributed to the famed Rochdale experiment.[7] It

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1. 18 NEWS FOR FARMER COOPERATIVES No. 6, p. 11 (1951).
2. *Ibid.*
3. *Ibid.*
4. *Ibid.*
5. See BLANKERTZ, MARKETING COOPERATIVES 20-41 (1940).
6. *Id.* at 29-37. HENNELL, AN OUTLINE OF THE VARIOUS SOCIAL SYSTEMS AND COMMUNITIES WHICH HAVE BEEN FOUNDED ON THE PRINCIPLE OF CO-OPERATION (1844).
7. The famed Rochdale pioneers were a group of flannel workers living in Rochdale, England. Blighted by poverty and unemployment, they banded together in 1844 to open a store to sell the staples of their existence. The principles of their Equitable Pioneers' Society have become the basis of later cooperation and are seven in number: open membership; democratic control based on one vote per member; limited interest on capital; patronage refunds; political and religious neutrality; cash trading; and the promotion of education. See BLANKERTZ, MARKETING COOPERATIVES 45 (1940); HOLY-

was at this time, the middle of the 19th century, that the movement took root in the United States,[8] beginning a development through six stages.[9]

The first period, in the years preceding 1870, was one of experimentation with no more than sporadic and scattered attempts to achieve effective cooperation. The most successful of these early efforts were in the dairy business, although similar activity occurred in the fruit, cotton, livestock and wool industries.[10] The Civil War culminated in an agricultural depression which saw the National Grange emerge as spokesman for the farmers. The Grange contemplated total cooperation on both marketing and purchasing levels and presented the Rochdale principles to the nation in 1875 by indorsing them at the national convention and promulgating a set of rules based thereon.[11]

By 1880 the Grange was no longer nationally significant.[12] Nevertheless, the third period, lasting from its decline until World War I, was one of gradual expansion. The cooperatives organized during this time were predominantly local in nature and devoted to the marketing of particular commodities, such as the cotton and grain growers of Texas, the cheese rings and creameries of Wisconsin and the New England

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OAKE, THE HISTORY OF THE ROCHDALE PIONEERS (1907); 1 AND 2 HOLYOAKE, THE HISTORY OF COOPERATION (1906).

8. One of the first attempts at agricultural cooperation occurred in 1841 when a group of Wisconsin farmers endeavored to cooperatively market their dairy products. See: HANNA, THE LAW OF COOPERATIVE MARKETING ASSOCIATIONS 4 (1931); 2 HOLYOAKE, THE HISTORY OF COOPERATION c. XXXI (1906); HISTORY OF COOPERATION IN THE UNITED STATES, Johns Hopkins University Studies in Historical and Political Science (1888).

9. In general SEE: Frost v. Corporation Commission, 278 U.S. 515, 529 (1928) (Brandeis' dissenting opinion); BAKKEN & SCHAARS, ECONOMICS OF COOPERATIVE MARKETING 66-71 (1937); BLANKERTZ, MARKETING COOPERATIVES 20-41, 72-98 (1940); FETROW & ELSWORTH, AGRICULTURAL COOPERATION IN THE UNITED STATES 103 (F.C.A. BULL. No. 54, 1947); HANNA, THE LAW OF COOPERATIVE MARKETING ASSOCIATIONS 3-7 (1931); NOURSE, THE LEGAL STATUS OF AGRICULTURAL COOPERATION 25-119 (1927); THE COOPERATIVE LEAGUE YEARBOOK 1-57 (1950); Hamilton, *Judicial Tolerance of Farmers' Cooperatives*, 28 YALE L.J. 936 (1929).

10. BAKKEN & SCHAARS, ECONOMICS OF COOPERATIVE MARKETING 68 (1937).

11. Journal of the Proceedings of the Ninth Session of the National Grange of the Patrons of Husbandry 94-100, as quoted in HANNA, THE LAW OF COOPERATIVE MARKETING ASSOCIATIONS 6 (1931); NOURSE, THE LEGAL STATUS OF AGRICULTURAL COOPERATION 35-38 (1927).

12. Other farm organizations related to cooperative growth included the Farmers' Alliance, organized about 1875 with special development in the southern states. The Rochdale principles found their first operative expression in consumers' stores in America in the Sovereigns of Industry, which lasted from about 1874 to 1879. The Farmers Educational and Cooperative Union, popularly called the Farmers Union, was founded in 1902 and had particular influence in the promotion of the cooperative sale of livestock and cotton in the southwest. It now has approximately 455,000 members. See BLANKERTZ, MARKETING COOPERATIVES 81-82 (1940); THE GENERAL FARM AND NATIONAL COOPERATIVE ORGANIZATIONS OF THE UNITED STATES, THE AMERICAN INSTITUTE OF COOPERATION (1951).

area, and the livestock shipping associations of Nebraska and other western states.[13]

The large foreign markets for agricultural products created by the first World War caused an agricultural boom which quickly receded into a depression when these markets ceased to absorb the American exports.[14] The result was a rapid development of agricultural cooperation during the fourth period, from 1916 through the 1920's, stemming largely from propitious federal legislation. Cooperation was considered to be a cure for the farmers' economic ills, and the favorable legislation was encouraged by the courts and scholars.[15] The first federal income tax exemptions had been granted in 1913.[16] Section 6 of the Clayton Act of 1914[17] removed the authorized activities of certain types of these associations from the antitrust laws. In 1922, Kentucky adopted the favorable Bingham Cooperative Marketing Act,[18] which rapidly became the standard state incorporation act for marketing associations. The Capper-Volstead Act[19] specifically authorized the cooperative association of agricultural producers; and, in addition, it clarified their antitrust exemption. The Federal Farm Board, predecessor to the present Farm Credit Administration, was created by the Agricultural Marketing Act of 1929[20] with a 500 million dollar revolving fund available for lending to cooperative businesses so as "to promote, protect, and stabilize the marketing of agricultural commodities." The board organized national cooperatives for many commodity groups including grain, cotton, and livestock.[21] The number of associations increased from 5,149 in 1915

13. HANNA, THE LAW OF COOPERATIVE MARKETING ASSOCIATIONS 7 (1931).

14. Between 1916 and 1920, farm prices rose spectacularly and the value of farm land increased in some areas by 300 to 450 percent in three years. Following the usual economic cycle, the depression found agriculture among its first victims, and farm incomes plummeted from $17 billion in 1919 to $9 billion in 1921, to $5.3 billion in 1922. Total land values decreased from $78.5 billion in 1920 to $43.3 billion in 1932. See BLANKERTZ, MARKETING COOPERATIVES 87-88 (1940).

15. "Agricultural depression is giving great impetus to the co-operative movement. There are many who believe that the co-operative marketing system is the most hopeful measure yet inaugurated to improve the financial condition of the farmer and to enable the producer to obtain just returns." Ballantine, *Co-operative Marketing Associations*, 8 MINN. L. REV. 1 (1923). In general see: Arnold, *Can the Courts Aid Cooperative Marketing?* 15 MINN. L. REV. 40-74 (1930); Hamilton, *Judicial Tolerance of Farmers' Cooperatives*, 38 YALE L.J. 936-954 (1929); Henderson, *Co-operative Marketing Associations*, 23 COL. L. REV. 91-112 (1923); Miller, *Farmers' Co-operative Associations as Legal Combinations*, 7 CORNELL L.Q. 293-309 (1922); Sapiro, *The Law of Cooperative Marketing Associations*, 15 KY. L.J. 1-21 (1926); Tobriner, *The Constitutionality of Co-operative Marketing Statutes*, 17 CALIF. L. REV. 19-34 (1928).

16. Revenue Act of 1913, § II, G, 38 STAT. 172 (1913). See PART V, p. 447, *infra*.

17. 38 Stat. 730, 731, 15 U.S.C. § 12 (1946). See PART IV, p. 437, *infra*.

18. Ky. Laws 1922, c. 1; KY. REV. STAT. c. 272 (1948).

19. 42 STAT. 388 (1922), 7 U.S.C. § 291 (1946).

20. 46 STAT. 11 (1929), 12 U.S.C. § 1141(a) (1945).

21. See BLANKERTZ, MARKETING COOPERATIVES 90-91, 112 (1940).

to 10,546 in the 1929-30 season, and their seasonal volume of business jumped from 624 million to over two billion dollars in the same period.[22]

Despite government aid and encouragement, economic failure beset cooperatives in the 1930's after their original expansion following World War I. The number of farmers' marketing and purchasing associations declined from 10,546 in their peak season of 1929-30, to 7,943 in the 1940-41 season; and their total business fell from about two and one-third billion dollars to approximately one and three-quarters billion in the 1939-40 season.[23] Of the total number of associations which discontinued operation in the years down to 1942, 84 percent of them did so from 1920-39. The greatest decline occurred in 1930, when about three cooperatives closed for every banking day.[24]

The Great Depression was brought to a definite end by World War II, which began the sixth and final period of cooperative development. In conjunction with the general upsurge of business activity following the War,[25] cooperative business volume reached an all time high of more than nine billion dollars in the 1948-49 season.[26] In the 1949-50 season, however, there was a decline of nearly six percent which was accounted for entirely by the marketing associations,[27] attributable largely to the eight percent drop in the farmers' cash receipts.[28] Of the various marketing organizations, dairy cooperatives had the largest volume of business; grain, which had led in previous years, dropped to second place; livestock associations ranked third; and fruits and vegetables were fourth.[29]

In the same season, marketing associations comprised 69 percent of all agricultural cooperative organizations, 62 percent of the membership, and 81 percent of the total volume of business.[30] Purchasing co-

22. FETROW & ELSWORTH, *op. cit. supra* note 9, at 210, 212 (Tables 30 and 32).

23. *Ibid.* The decrease in cooperative business of approximately 25.1 percent, which occurred from 1929 to 1939, reflected the general decline of wholesale prices. The wholesale price index for farm products in 1929 was 104.9 as contrasted with 65.3 in 1939, a 37.7 percent drop. The decrease in cooperative business was thus not as severe as might have been expected. See 1950 STATISTICAL ABSTRACT OF THE UNITED STATES 279.

24. FETROW & ELSWORTH, *op. cit. supra* note 9, at 187-190.

25. The total sales of all business increased from 133.4 billions of dollars in 1939 to 458.3 billion in 1948. Total sales declined 5.8 percent in 1949 to 431.5 billions of dollars. The fluctuation of the business volume of agricultural cooperatives thus roughly paralleled that of the total business sales. 1950 STATISTICAL ABSTRACT OF THE UNITED STATES 445 (Table 519).

26. 18 NEWS FOR FARMER COOPERATIVES No. 6, p. 11 (1951).

27. *Ibid.*

28. *Ibid.*

29. Dairy Cooperatives did a total business of $2.032 billion; grain $1.953 billion; livestock $1.3 billion; and fruits and vegetables $784 million. *Ibid.*

30. *Ibid.*

operatives accounted for 31 percent of the number of such organizations, 38 percent of the membership, and 19 percent of the business. Within the last decade, however, the purchasing cooperatives have shown an average rate of increase in number, membership, and business of 5.96 percent over marketing associations.[31] At the close of 1950, there were 3,113 farm purchasing cooperatives, having a total membership of a little over two and one-half million, and doing almost one and two-thirds billion dollars worth of business.[32] Allowing for duplication, regional purchasing cooperatives served two out of every five farmers in the United States in 1950, as compared with one out of every five in 1942, the first year in which figures were collected.[33] A study of twenty major regional farm supply purchasing cooperatives reveals that their total volume of business in 1950 exceeded all other years to reach a total of 835 billion dollars.[34] The business of wholesale and retail outlets have each nearly tripled since 1942;[35] although the number of retail cooperatives declined five percent from 1949.[36] The 1950 savings for members were 29 million dollars, a 46 percent increase over 1949, but 24 percent less than 1948, the peak year.[37]

The heaviest concentration of agricultural cooperatives has consistently been found in the north central area of the country.[38] In the 1949-50 season, this region accounted for about 60 percent of their num-

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31.

	Associations		*Membership*		*Business*	
	1940	1950	1940	1950	1940	1950
Marketing	74.9%	69%	71.2%	62%	83.8%	81%
Purchasing	25.1	31	28.8	38	16.2	19

Ibid.

32. 18 NEWS FOR FARMER COOPERATIVES No. 6, p. 11 (1951).

33. *Id.* at 7.

34. This was due to a five percent increase in sales of feed, eight percent in petroleum products, and ten percent in fertilizer. The 1950 farm supply dollar of the twenty major regional purchasing cooperatives may be broken down into the following items: feed, 42.4%; petroleum products and related supplies, 28.1%; fertilizer, 9.5%; seed, 4.1%; lumber, paint and hardware, 2.8%; packaged materials, 2.4%; farm machinery, 3.2%; others 7.5%. 18 NEWS FOR FARMER COOPERATIVES No. 5, p. 7 (1951).

35.

	1942	1950
Wholesale outlets:	$229,901,601	$679,357,811
Retail outlets:	54,211,449	155,420,992
	$284,113,050	$834,778,803

Ibid.

36. 18 NEWS FOR FARMER COOPERATIVES No. 5, p. 7 (1951).

37. *Ibid.* See 1949-1950 HANDBOOK OF MAJOR REGIONAL FARM SUPPLY PURCHASING COOPERATIVES (F.C.A. MISC. REP. No. 150, 1951).

38. The Farm Credit Administration defines this area as including the states of Illinois, Indiana, Iowa, Kansas, Michigan, Minnesota, Missouri, Nebraska, North Dakota, Ohio, South Dakota, and Wisconsin. 18 NEWS FOR FARMER COOPERATIVES No. 6, p. 12 (1951).

ber, more than 55 percent of the total membership, and nearly 53 percent of the estimated total business.[39]

Comparative statistics regarding the volume of cooperative and non-cooperative business in agricultural industries are both rare and incomplete. Available figures indicate that in the dairy industry, cooperatives market approximately 21.7 percent of all milk sold from farms in the United States,[40] 15 percent of the cheese, 40 percent of the butter, and 60 percent of nonfat, dry milk solid.[41] Cooperatively marketed cranberries have not fallen below 50-65 percent of the total crop in the last forty years.[42] In 1948, approximately 74 percent of the California and Arizona citrus fruit shipments were marketed through the California Fruit Growers Exchange,[43] and forty percent of the shipped fresh fruit from Florida was handled by cooperatives.[44] Purchasing cooperatives, while experiencing a gradual growth, have remained relatively small as compared with other business organizations in most areas of the country. With the possible exception of the feed business, purchasing cooperatives do not account for a large proportion of the total volume of business in the various industries in which they operate.[45]

Despite its recent growth, the cooperative method of business is not precisely described nor readily distinguishable from other corporate endeavor. No single definition of cooperation exists.[46] Concepts vary and fluctuate around the seven original Rochdale principles of open membership; democratic control, based upon one vote per member; patronage refunds; limited interest on capital; political and religious neutrality; cash trading; and promotion of education.[47] These principles were

39. *Ibid.* The exact reasons for this have never been determined. Some attribute it to the fact that large segments of the population of this area are of Scandinavian origin; and since cooperation has long flourished in the Scandinavian countries, it is thought that they brought cooperative principles with them. See CHILDS, SWEDEN THE MIDDLE WAY (Rev. ed. 1947).

40. ACTIVITIES OF THE NATIONAL MILK PRODUCERS FEDERATION, EDUCATION SERIES No. 42, p. 4 (1951).

41. 14 NEWS FOR FARMER COOPERATIVES No. 7, p. 15 (1947).

42. FETROW & ELSWORTH, *op. cit. supra* note 9, at 73.

43. GARDNER & MCKAY, THE CALIFORNIA FRUIT GROWERS EXCHANGE SYSTEM 22 (F.C.A. CIRC. C-135, 1950).

44. 16 NEWS FOR FARMER COOPERATIVES No. 3, p. 11 (1949).

45. In 1951, cooperatives owned less than one-half of one percent of the total producing oil wells in the United States, and they refined about two percent of the total amount refined by thirty principal oil companies. Their investment was less than one percent of that of the same leading thirty companies. 18 NEWS FOR FARMER COOPERATIVES No. 9, p. 11 (1951). The same general situation prevails as to the cooperative manufacture of farm machinery and equipment. See FRANCIS, DISTRIBUTION OF MACHINERY BY FARMERS' COOPERATIVE ASSOCIATIONS (F.C.A. CIRC. C-125, 1941).

46. FETROW & ELSWORTH, *op. cit. supra*, note 9, at 4.

47. BAKKEN & SCHAARS, ECONOMICS OF COOPERATIVE MARKETING c. VII (1937); BLANKERTZ, MARKETING COOPERATIVES c. 20 (1940).

directed toward the creation of a business enterprise in which the individual member retained control and received as a patron the benefits of such cooperative effort.

While political and religious neutrality and promotion of education are still in effect practiced by cooperatives in free countries,[48] they are ethical or social principles and are not concerned with the actual cooperative method of business; so that of the original seven tenets, only five constitute a *modus operandi*. Open membership is interpreted to refer to occupation, and membership in agricultural cooperatives is usually open only to those connected with agricultural production.[49] Cash trading was a necessity to the Rochdale pioneers due to their lack of operating capital. Although still encouraged, particularly on the retail level, it has often given way today to credit transactions.[50] The remaining trinity, democratic control, the patronage refund, and limited

48. Cooperation is, of course, world-wide, and the international organization is the International Cooperative Alliance which was founded in 1895 and is a union of the federated cooperative societies. In 1938, it had an affiliated membership of more than 71 million. At the I.C.A. Congress of 1937 endorsement of the Rochdale principles was attempted, but the conflicting political and ideological theories of the nations represented prevented the adoption of either religious and political neutrality or of educational promotion as obligatory principles. These, together with cash trading, were merely recommended; while open membership, democratic control with one vote per man, distribution of surplus to members in proportion to their transactions, and limited interest on capital were adopted as required principles for agricultural cooperatives. See: COLE, A CENTURY OF COOPERATION (1944); THE COOPERATIVE MOVEMENT IN THE AMERICAS, AN INTERNATIONAL SYMPOSIUM (1943); WARBASSE, THE INTERNATIONAL COOPERATIVE MOVEMENT, Co-ops PLAN FOR THE POST-WAR WORLD, Report of International Planning Done at the Washington Conference (1944); WARBASSE, COOPERATIVE DEMOCRACY c. III (5th ed. 1947). As to the cooperative role in rehabilitation and reconstruction, see THE COOPERATIVE MOVEMENT AND PRESENT-DAY PROBLEMS, International Labour Office Studies and Reports Series H, No. 5 (1945).

At the 1951 Congress of the I.C.A., open membership, democratic control, and freedom from outside interference or persuasion from governments or political parties were established as the criteria for admission to the I.C.A. By a new rule, members are obliged to conform in their activity to the principles of Rochdale. *International Cooperation Congress, Copenhagen, 1951* 74 MONTHLY LABOR REV. No. 1, p. 45 (1952).

49. *E.g.*, the Indiana Cooperative Marketing Act places this restriction on those eligible to hold common stock: "Such individuals or political subdivisions must be engaged in the production of agricultural products. A lessor or landlord of land used for such production or any natural person devoting a substantial part of his time in assisting others to produce agricultural products, whether employed by a farmer, or an agricultural cooperative corporation or an association, shall be considered so engaged. Except as above provided, the holders of common stock in any associations limited by its articles of incorporation to one (1) or more of the particular agricultural services shall be such producers of agricultural products as use the articles or services to which the activities of the association are so limited." IND. ANN. STAT. § 15-1606(b) (Burns' Repl. Vol. 1950).

50. See: 16 NEWS FOR FARMER COOPERATIVES No. 9, p. 11 (1949); 15 NEWS FOR FARMER COOPERATIVES No. 2, p. 7 (1948); 12 NEWS FOR FARMER COOPERATIVES No. 12, p. 11 (1946); *Id.* at No. 3, p. 12; 11 NEWS FOR FARMER COOPERATIVES No. 12, p. 10 (1945); 9 NEWS FOR FARMER COOPERATIVES No. 8, p. 8 (1943).

interest on capital, is believed to constitute the distinction between cooperation and other corporate enterprise.[51]

Democratic control, originally considered the most revolutionary aspect of cooperation,[52] substitutes membership for capital interest as the basis for voting. The cooperative has been conceived of as a representative body in which each member is a delegate and a spokesman for his economic unit in the aggregate.[53] Cooperative incorporation laws of approximately three-fourths of the states restrict each member to one vote regardless of the amount of stock owned or the extent of patronage,[54] and it has been estimated that about 86 percent of the cooperatives in the United States adhere to this principle.[55] Where deviation occurs, it is usually to base voting on the number of shares held or upon the amount of patronage given, but even then a maximum number of votes is normally established.[56] By so limiting the voting power of each

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51. FETROW & ELSWORTH, AGRICULTURAL COOPERATION IN THE UNITED STATES 10-12 (F.C.A. BULL. No. 54, 1947); LARSON, AGRICULTURAL MARKETING 449 (1951); VENNES & BINKLEY, FARMER COOPERATIVES, Agricultural Extension Division, College of Agricultural and Home Economics, 484 University of Ky. Circ. c. III (1950).

52. EMELIANOFF, ECONOMIC THEORY OF COOPERATION 192 (1942).

53. *Id.* at 90.

54. FETROW & ELSWORTH, *op. cit. supra* note 51, at 10.

55. 1947 AMERICAN COOPERATION 24.

56. FETROW & ELSWORTH, *op cit. supra* note 51, at 10; PACKEL, THE LAW OF THE ORGANIZATION AND OPERATION OF COOPERATIVES 104-107 (2d ed. 1947).

Of the 10,752 cooperative associations in 1938, the following bases of voting were used by the number of associations indicated:

one vote per member	9,219	85.74%
stock or other financial unit	1,335	12.42
patronage (including 60 assoc. in which basis in combination of membership & patronage)	125	1.16
other and unknown	73	.68
	10,752	100.00%

STATISTICAL HANDBOOK OF FARMERS' COOPERATIVES 55 (F.C.A. BULL. No. 26, 1938). But see the results of a survey made of approximately 100 cooperative marketing associations in the states of Arizona, Utah, Nevada, and California showing that only 42% of them had equal voting with the remaining 58% providing for unequal voting generally based upon patronage. BAKKEN & SCHAARS, ECONOMICS OF COOPERATIVE MARKETING 154-156 (1937).

The Indiana Act provides that the articles of incorporation or the by-laws of the association may provide that after a stated time, or under stated conditions, "no one shall own more than a stated percentage of its outstanding common stock and/or that no member or stockholder shall be entitled to more than one (1) vote, regardless of the amount of capital invested, or number of shares of stock owned, by such member." IND. ANN. STAT. § 15-1613 (Burns' Repl. Vol. 1950). It is significant that this limitation is expressed in discretionary language. The 1931 amendment to the act deleted provisions limiting ownership by one stockholder to one-eleventh of the common stock and limiting each member or stockholder to one vote regardless of size of

member, it is thought that equality of membership is fostered, in keeping with the democratic spirit which permeated the conception of cooperation.

Equally significant is the principle of the patronage refund. Instead of distributing business returns to stockholders, as is done in non-cooperative enterprises, the cooperative attempts to direct the benefits of corporate activity to those who utilize its services. This is accomplished through the patronage refund which, in theory, returns to the patron-member the remuneration received by the organization in the conduct of its business after allowance for costs and reasonable reserves.[57] This return is at times referred to as the savings realized by participating in the cooperative method of business.

To further de-emphasize the importance of the organization as a distinct entity, interest is limited on capital to discourage speculation in cooperative stock. The profits to be gained from cooperative enterprise are not in the trading of its stock, but in the use of its method of business.[58] In addition, many states place restrictions on the amount of stock which may be held,[59] together with limitations on the extent of non-member business.[60] These restraints accent the fact that a coopera-

holdings, Acts. 1931, c. 34 § 10, p. 79. It would thus appear that the intent of the legislature was to enable cooperatives to depart from the principle of one man, one vote without limiting stock ownership.

57. See: BLANKERTZ, MARKETING COOPERATIVES 134-136 (1940); DIGBY, THE WORLD COOPERATIVE MOVEMENT 19-20 (1948); EMELIANOFF, ECONOMIC THEORY OF COOPERATION 83 (1942); ENFIELD, CO-OPERATION: ITS PROBLEMS AND POSSIBILITIES 6-8 (1927); HOLYOAKE, THE HISTORY OF THE ROCHDALE PIONEERS c. IX, 278-281 (1893); NOURSE, THE LEGAL STATUS OF AGRICULTURAL COOPERATION 21-24 (1927); PACKEL, THE LAW OF THE ORGANIZATION AND OPERATION OF COOPERATIVES 190-194 (2d ed. 1947); Adcock, *Patronage Dividends: Income Distribution or Price Adjustment*, 13 LAW AND CONTEMP. PROB. 505-525 (1948).

58. BLANKERTZ, MARKETING COOPERATIVES 129, 349-50 (1940); DIGBY, THE WORLD COOPERATIVE MOVEMENT 19 (1948); FETROW & ELSWORTH, AGRICULTURE COOPERATION IN THE UNITED STATES 11 (F.C.A. BULL. No. 54, 1947); 1 HOLYOAKE, HISTORY OF CO-OPERATION 277-278 (1906); PACKEL, THE LAW OF THE ORGANIZATION AND OPERATION OF COOPERATIVES 196-197 (2d ed. 1947).

59. The cooperative marketing statutes of nearly half of the states expressly limit the number or proportion of shares which can be owned by a single member, or empower the cooperative to do so. The limitation is either as to percent of total or as to dollar volume. See BLANKERTZ, MARKETING COOPERATIVES 128-129, 178-179, 350 (1940). This restriction is discretionary with the cooperative in Indiana. IND. ANN. STAT. § 15-1613 (Burns' Repl. Vol. 1950).

60. In Indiana, non-member business must not exceed in amount the total of similar business transacted by the association for its own members during the same fiscal year. IND. ANN. STAT. § 15-1605(a) (Burns' Repl. Vol. 1950). The same restriction must be met to come within the provisions of the Agricultural Marketing Act so as to be entitled to borrow from the various federal agencies, 46 STAT. 11 (1929), 12 U.S.C. § 1141(j) (1945). See PART V, pp. 452-453, *infra;* PACKEL, THE LAW OF THE ORGANIZATION AND OPERATION OF COOPERATIVES 159-162 (2d ed. 1947).

tive is an organization whose members have equal standing and whose primary purpose is the benefit of its patron-members.

The three fundamental tenets of cooperation, democratic control, patronage refund, and limitation of interest on capital, distinguish the agricultural cooperative from other types of corporate enterprise. The importance of the distinction is not in the mechanics of the organizational structure. Rather, the significant differential lies in the general emphasis of cooperative organization, which stresses the benefit of patron-members by facilitating and promoting their functioning as individual economic units.[61]

An agricultural cooperative is categorized according to the territory served as a local, regional, or national association; while in terms of administrative organization it may be classified as centralized or federated.[62] The local, centralized association was, naturally, predominant among the early forms of agricultural cooperative organization in the United States.[63] But like all creatures, once conceived, the local associ-

61. Other definitions are: "Cooperative organizations represent the aggregates of economic units [the individual farms]. . . . An aggregate of economic units is a plurality or group of these units coordinating their activities but each fully retaining its economic individuality and independence. [It is the] . . . center of their coordinated activities or . . . an agency of associated economic units, owned and controlled by them, through which they conduct their business activities." EMELIANOFF, ECONOMIC THEORY OF COOPERATION 248 (1942).

"Co-operation is organized self-help. . . ." 2 HOLYOAKE, HISTORY OF CO-OPERATION 589 (1906).

"An agricultural cooperative association is a business organization, usually incorporated, owned and controlled by member agricultural producers, which operates for the mutual benefit of its members or stockholders, as producers or patrons, on a cost basis after allowing for the expenses of operation and necessary reserves." HULBERT, LEGAL PHASES OF COOPERATIVE ASSOCIATIONS 1 (F.C.A. BULL. No. 50, 1947).

"A Cooperative is an association which furnishes an economic service without entrepreneur or capital profit and which is owned and controlled on a substantially equal basis by those for whom the association is rendering service." PACKEL, THE LAW OF THE ORGANIZATION AND OPERATION OF COOPERATIVES 3 (2d ed. 1947).

"It is indicated that cooperative corporations in general possess many of the essential attributes of ordinary business corporations, the most noticeable differences being in the matters of voting power and the basis of distribution of their net earnings. In the cooperative corporation each member or stockholder has one vote regardless of the number of shares he may hold, whereas each share of stock is entitled to one vote in the ordinary business corporation. . . . The business corporation usually divides part of its profits among its shareholders in proportion to the shares owned, while a cooperative corporation, after distributing part of its profits to shareholders in the form of a dividend not exceeding a rate generally fixed by statute, distributes the remainder in proportion to the volume of members' purchases and sales. Because of a definite and limited return accruing to an investor in a cooperative, his status has been distinguished from that of a stockholder in a business corporation and analogized rather to that of a bondholder." Farmers Cooperative Co. v. Birmingham, 86 F. Supp. 201, 211 (N.D. Iowa 1949).

62. See: BAKKEN & SCHAARS, ECONOMICS OF COOPERATIVE MARKETING 212-241 (1937); BLANKERTZ, MARKETING COOPERATIVES 102-103 (1940).

63. BLANKERTZ, MARKETING COOPERATIVES 79 (1940).

ation began to grow, and the need for inter-cooperative and large-scale organization became apparent. Farmers within a region, functioning through their respective cooperatives or individually, foresaw the advantages inherent in quality control, standardization of production and operating methods, and procedures designed to decrease costs of handling and distribution. The results sought to be achieved were an effective bargaining position in the market and, in general, the extension of cooperative services and their more efficient rendition to the members. The transition to large-scale cooperation was effected both within the framework of the centralized organizational structure and through the development of the federated societies, thus culminating in the formation of these two distinct schemes of cooperative administrative organization.

Large centralized associations first became numerous during the years from 1920-25, beginning on the Pacific Coast and spreading particularly to the South in the cotton and tobacco industries.[64] Many such organizations which came into existence in this early period were the result of high-pressure promotional campaigns which stirred farmers to sign long-term marketing agreements.[65] Unlike the composition of federated associations, there are no autonomous local organizations in the centralized cooperative. Control and authority are thus concentrated in the headquarters of the group, and the members directly elect the board of directors. Features which recommend this administrative structure are the ease with which it may be organized and the strong central control which it provides. Business and policy matters may be dealt with in a more direct and expeditious manner than a decentralized management is able to exert. Moreover, it may provide the volume which is essential to reduce costs, to insure more economical use of by-products, and to acquire greater bargaining power in the market. This method of organization has been used by purchasing cooperatives[66] and also in the marketing field, chiefly by the cotton, rice, and tobacco interests of the South and by the wheat growers of the Middle West.[67] The California dried fruit cooperatives also are organized in this manner, as are many of the wool producers of the Pacific Northwest.[68] Marketing

64. See: BAKKEN & SCHAARS, ECONOMICS OF COOPERATIVE MARKETING 219-222 (1937); HANNA, THE LAW OF COOPERATIVE MARKETING ASSOCIATIONS 9-10 (1931).

65. BLANKERTZ, MARKETING COOPERATIVES 109 (1940).

66. The giant Cooperative Grange League Federation Exchange, Inc. is one of the leading centralized purchasing cooperatives. In 1950, it distributed a total dollar volume of farm supplies of $245,559,300. ABRAHAMSEN & SCEARCE, 1949-50 HANDBOOK ON MAJOR REGIONAL FARM SUPPLY PURCHASING COOPERATIVES 2-6 (F.C.A. MISC. REP. No. 150, 1951).

67. HANNA, THE LAW OF COOPERATIVE MARKETING ASSOCIATIONS 7 (1931),

68. *Ibid.*

associations in the dairy industry are centrally managed to a limited extent.[69]

The federated association is, however, the more common method of large-scale cooperative organization in the United States. A federation has the dual task of assisting its local member-associations in their production and sale problems while conducting its own affairs as a terminal marketing or purchasing agency.

Within the marketing category, a federation may be one of three types.[70] It may be a regional marketing association, actually handling its members' products and assembling, grading, standardizing, processing, packing, branding, storing, financing and selling them. Or, it may be a regional bargaining association, having as its main function the bargaining for prices, terms, and conditions at which members will sell to local dealers who perform the actual marketing functions. This is an arrangement frequently used in the milk industry.[71] Finally, it may be a regional sales agency which merely sells members' products on a commission basis and performs no other marketing function.

Within the federated organization, a pyramidal hierarchy of command is adopted which, in theory, retains the local members' control over the peak association. The local farmer-member elects the board of directors for his local cooperative which, in turn, elects one or two representatives to the board of the regional. The directors of each regional in turn choose directors of organizations with which they may be affiliated.

As other business entities within the competitive economy, agricultural cooperatives have shown a tendency gradually to assume organizational characteristics necessary for large-scale operation. Once a modicum of success was achieved at the local level, these associations encountered the same two forces which have constantly affected other businesses: the desire created by success to become more successful, and the competition of non-local large-scale business. Together, these have produced the pyramidal expansion of the local cooperative.

To further achieve the efficiencies of size with the resulting increase in bargaining strength, injurious competition among cooperative associations is now being discouraged and greater coordination of effort is urged.[72] Accordingly, consolidation might well be termed a major policy

69. *Ibid.*

70. See BAKKEN & SCHAARS, ECONOMICS OF COOPERATIVE MARKETING 215-219, 223-225 (1937).

71. See DISTRIBUTION OF MILK BY FARMERS' COOPERATIVE ASSOCIATION 1 (F.C.A. CIRC. C-124, 1941).

72. "Cooperatives have made tremendous progress in coordinating their efforts in

of modern agricultural cooperation.[73] It was largely due to this policy that the Farm Credit Administration attributed the decrease in the total number of agricultural cooperatives in the United States from 10,700 in the 1938-39 marketing season to 10,035 in the 1949-50 season.[74] Moreover, in recent years relatively few of these organizations have a substantial portion of all cooperative business.

By the end of 1945, large-scale marketing cooperatives, embracing varied economic activities and extending over a wide geographic area, accounted for over 50 percent of the business done by all marketing associations.[75] Yet, the organizations responsible for this portion of the total business numbered but 7.3 percent of all cooperatives engaged in marketing functions.[76] In the purchasing area, only 3.5 percent of all purchasing cooperatives operating on a large scale handled more than 40 percent of the total volume of business.[77] Of all the cooperative marketing and purchasing associations in the same 1944-45 season, 6.2 percent accounted for 48.7 percent of the total business and 42.6 percent of the total membership.[78]

It thus can be seen that agricultural cooperation, unlike its former character as a small, directly controlled economic influence in a particular community, has assumed in large measure the administrative, economic, and geographic proportions of big business. The natural inquiry is whether this substantial metamorphosis has produced a modification in the basic cooperative principles. A further question, if alteration has occurred, is whether the result has been to diminish the desirability of cooperation as a distinct form of economic enterprise for farmers.[79]

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recent years and there is reason to believe that such coordination will greatly increase as the problem of reducing excessive competition is courageously tackled.

"There is an answer to the problem of excessive competition between cooperatives. It lies in more cooperation wherever this will benefit cooperative members." 16 NEWS FOR FARMER COOPERATIVES No. 11, p. 18 (1950); See 16 NEWS FOR FARMER COOPERATIVES No. 12, p. 3 (1950); 1949 AMERICAN COOPERATION 341-376.

73. "Few realize the extent to which local cooperatives have joined regional cooperatives in recent years. In fact, there are now relatively few local cooperatives that are not affiliated or are not members of larger organizations. The 17 major regional purchasing cooperatives now have over 4,000 member associations as compared to 2,500 about 7 years ago. Grain, dairy, and other types of marketing cooperatives have also federated in many areas." 16 NEWS FOR FARMER COOPERATIVES No. 11, p. 18 (1950). See, *Big Business without Profit*, 32 FORTUNE 152 (1945).

74. 18 NEWS FOR FARMER COOPERATIVES No. 6, p. 11 (1951).

75. FETROW & ELSWORTH, AGRICULTURAL COOPERATION IN THE UNITED STATES 191, (Table 26 F.C.A. BULL. No. 54, 1947).

76. *Ibid.*

77. *Ibid.*

78. *Ibid.*

79. The tendency is well described by the T.N.E.C.: "The vaster they [the corporations] become the more difficult are the structural problems of organization, coor-

PRINCIPLES IN PRACTICE

The tenet that interest return on capital must be limited has at times proved the most inconvenient to cooperative development. However, this fundamental principle has been adhered to closely. It was evolved as a means to reduce the speculative character of cooperative stock and to emphasize the fact that a cooperative does not furnish primarily a source of investment, but rather a method of performing for members some needed service at cost. Both federal and state laws have recognized this principle. The Capper-Volstead Act[80] establishes a maximum interest rate of eight percent, but only if members vote on any basis other than one vote per member. If voting is so limited, then the interest rate is unrestricted. However, to come within the exemption provisions of the federal revenue act, a cooperative must limit its interest to either eight percent or to the legal rate in the state of incorporation, whichever is greater.[81] The state agricultural cooperative acts either specify an interest rate or require that the corporate by-laws establish a fixed rate that is reasonable.[82]

The result of the limited interest principle was to deprive the early cooperatives of much needed capital,[83] for individuals were loath

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dination, and control, and the human problems of incentive and leadership. Large corporations, like other large human enterprises, are bureaucratic. They tend to live by fixed rules rather than acumen, by the meshing of many component parts rather than the quick decision of an entrepreneur. Organization grows in importance as size increases. . . . And like other large organisms, the larger the modern corporation becomes, the more it tends to move slowly, adapt itself with increasing difficulty, be increasingly concerned with its inner rules and procedures. Hence, it stands in danger of losing that flexibility of price adjustment and resiliency of managerial outlook which is the most valuable social asset of free competition." DIMOCK & HYDE, BUREAUCRACY AND TRUSTEESHIP IN LARGE CORPORATIONS 3-4 (TNEC Monograph 11, 1940).

This thought, as applied to cooperatives, was expressed by one writer in this manner: "As I sit in the meetings of farmer cooperatives and listen to the discussions and decisions of management, I am impressed with the fact that the rules of the game are becoming more and more the rules of big business. . . . You must meet changing conditions. But perhaps this too brings new problems and new orientation. . . . I am beginning to question more and more whether the expansion of cooperatives through the establishment of new departments or of new enterprises is in the interest of our rural economy. To what extent is it a move, and an understandable one, on the part of management to foster vested interests?" Wood, *Cooperatives, Competition and Free Enterprise*, 1950 AMERICAN COOPERATION 217.

80. 42 STAT. 388 (1922), 7 U.S.C. § 291 (1946).

81. INT. REV. CODE § 101 (12) (a).

82. The Indiana Act sets an eight percent maximum on dividends of any kind or class of stock based upon par value of the respective stock, and if no par then upon book value. IND. ANN. STAT. § 15-1613 (Burns' Repl. Vol. 1950).

In 1940, one state limited interest on capital to 5%, five states to 6%, one to 7%, eleven to 8%, and two to 10%. The remaining states specified that a fixed amount should be set by the by-laws within a fair rate of interest. BLANKERTZ, MARKETING COOPERATIVES 349 (1940).

83. See BLANKERTZ, MARKETING COOPERATIVES 349-350 (1940); FETROW & ELS-

to invest in cooperative enterprise and banks were reluctant to lend. This difficulty was partially alleviated by the establishment by the Federal Government of agricultural credit agencies, and later by the creation of central and district banks for cooperatives.[84] Of greater significance as a current method of offsetting the limitation placed upon sources of capital by the restricted interest device is the modification of another cooperative tenet, the patronage refund.

In theory, the patronage refund represents, not profits of the associations, but savings made for the members by their dealings through the cooperative.[85] Its strict application on a cash basis would result in cash flowing through the cooperative organization while such funds were critically needed for financing. In their search for capital, cooperatives began to retain a portion of the cash and to distribute instead to the patron-member some form of certificate evidencing the amount of his refund.[86] This process of retaining the cash savings and substituting certificates containing provision for possible subsequent retirement is designated as the revolving-fund plan of financing,[87] a technique which has become one of the most significant aspects of modern cooperative financial administration. For example, in 1950, the Farm Bureau Cooperative Association, Inc. of Ohio, reported a total savings to members of ten million dollars for its seventeen years of operation. Of this amount, 35 percent had been refunded in cash to the shareholders and patrons, and the balance of 65 percent had been retained and used by the association.[88] In 1946, the 6,009 agricultural cooperatives which qualified for tax exemption under Section 101 (12) of the Internal Revenue Code credited $106 million to patronage refunds. Of these funds, approximately $16.5 million or 15.5 percent actually was paid out in cash.[89]

WORTH, AGRICULTURAL COOPERATION IN THE UNITED STATES 11 (F.C.A. BULL. No. 54, 1947); HULBERT, LEGAL PHASES OF COOPERATIVE ASSOCIATIONS 3 (F.C.A. BULL. No. 50, 1942).

84. See HULBERT, *op. cit. supra* note 83, at 311.

85. See IND. ANN. STAT. § 15-1613 (Burns' Repl. Vol. 1950); EMELIANOFF, ECONOMIC THEORY OF COOPERATION 183-185 (1942); Jensen, *Terminology in Cooperative Corporation Law*, 1948 AMERICAN COOPERATION 288.

86. At the close of their fiscal year in 1942, the then seventeen major regional purchasing cooperatives had a total net worth of $37,646,846. Of this amount, 66% had been retained out of savings, while 33.5% represented sums accumulated through the sale of stock. 1941-42 HANDBOOK ON MAJOR REGIONAL FARM SUPPLY PURCHASING COOPERATIVES, 60 (F.C.A. MISC. REP. No. 67, 1943).

87. See PART II, pp. 394-395, *infra*.

88. 1950 ANNUAL REPORT, THE FARM BUREAU COOPERATIVE ASS'N., INC., OHIO 9.

89. TAX TREATMENT OF COOPERATIVES, PART 2, p. 4, by Staffs of the Treasury and the Joint Committee on Internal Revenue Taxation (Apr. 1951). See PART V, p. 464, *infra*.

It is thus illustrated that through the revolving fund device, a major portion of cooperative cash receipts allocated to patronage refunds is in fact diverted to financing reserves. Consequently, patronage refunds have in large measure assumed the form of deferred payment certificates, issued to members as evidence of their equity in the assets of the organization. Moreover, cooperatives have exhibited recently a discernible tendency to further restrict the return of cash savings, equivalently extending the distribution of members' equity certificates. The total net savings of the twenty major regional farm supply purchasing cooperatives for the fiscal year ending in 1950 amounted to $28,810,648, a forty-five percent increase over 1949.[90] In the distribution of this amount, as compared with 1949, deferred patronage refunds increased 44.5 percent while cash refunds increased only 36.6 percent; although the latter exceeded the former by approximately a million dollars.[91] The total amount of savings retained, including deferred refunds and reserves, increased 64.4 percent over 1949; and the retained reserves increased 96.5 percent.[92]

This manner of administering the patronage refund principle impinges upon the third basic tenet of cooperation, that of democratic control. In an effort to avoid the concentration of control in the hands of a few, which was found to occur in regular corporate enterprise, the Rochdale principles attempted to equalize control by basing voting upon membership and not upon economic interest.[93] The goal has been to discourage and, if possible, to prevent the accumulation by a few individuals of inordinate economic interest in the organization by means of which they may exert greater influence upon the management of the cooperative. Accordingly, many states have restricted the amount of stock which a member may hold.[94] The amount of patronage, of course, has not been limited with the result that patronage refunds necessarily are inequal. So long as these refunds are paid in cash, whereby no

90. ABRAHAMSEN & SCEARCE, 1949-50 HANDBOOK ON MAJOR REGIONAL FARM SUPPLY PURCHASING COOPERATIVES 54 (F.C.A. MISC. REP. No. 150 1951).

91.

Distribution of Net Savings	1949	1950	Percentage Increase
Cash patronage refunds	$ 7,011,268	$ 9,575,268	36.6
Deferred refunds	5,910,421	8,542,596	44.5
Cash dividends on stock	3,238,331	3,504,797	8.2
Retained in reserves	3,658,691	7,187,987	96.5
Total	$19,819,360	$28,810,648	45.4

92. *Ibid.*

93. *Supra*, p. 360.

94. BLANKERTZ, MARKETING COOPERATIVES 350 (1940). HANNA, THE LAW OF COOPERATIVE MARKETING ASSOCIATIONS c. 2 (1931).

continuing obligation to the members exists, their inequality plausibly would not present a challenge to the principle of democratic control. The retention of cash savings, however, and the issuance of certificates of equity in their stead in effect transposes patrons into investors in proportion to the amount of patronage and resulting refunds retained. Through an indirect process, therefore, large inequalities of economic interest in the assets of the organization may arise to threaten democratic control. For it is entirely probable that policies will be at least partially determined, perhaps unconsciously, on the basis of their effect upon holders of the major economic interest in the cooperative.

Democratic control is challenged not alone by the emergence of inequalities of economic interest. It is also subject to the strains produced by the increasing size and complexity of modern cooperative endeavor.[95] There are great differences in the problems of management and control of a local cooperative as compared to those of large federated associations involving packing and processing plants, machinery and fertilizer factories, oil refineries and pipe lines—all interrelated by interlocking directories and holding companies.[96] This expansion has come about so rapidly within recent years that frequently the business operations have outdistanced the membership relations' programs,[97] and a tendency has developed to neglect the human relations phase of cooperative administration.[98] As the levels of administration increase through federation and consolidation, it logically becomes more difficult for the individual member of the local to understand and to participate in the development of the policies governing the business. But although expansion and large-scale operation has divested management control from ownership in the modern corporate structure,[99] a similar result in cooperative administration is not an inevitable corollary.

95. The diversification which has occurred in the activities of the larger cooperatives is recognized by the Farm Credit Administration, which has developed a new tabulation method to reflect this change. Formerly, if more than 50% of a cooperative business was, for example, dairy, then it was listed in its entirety in the dairy group. No separate recognition was made of any other types of business in which it could also be engaged, as grain or poultry. Beginning in 1952, however, the cooperatives are to report on the basis of their actual business in each individual commodity or service fields. Grain elevators, for example, which have shown a tendency to begin selling farm supplies, such as feed and petroleum, and often market other products, will now report such activities. 18 NEWS FOR FARMER COOPERATIVES No. 6, p. 12 (1951).

96. 1948 AMERICAN COOPERATION 111-118; The Ohio Farm Bureau Cooperative Association, Inc., for example, has investments in fertilizer plants, refinery operations, pipe line operation, farm machinery plants, warehouses, feed plants, grain terminals, an alfalfa mill, seed plants, milking machine factory, and a hatchery. 1949 ANNUAL REPORT, OHIO FARM BUREAU COOPERATIVE ASSOCIATION, INC. 11.

97. 1948 AMERICAN COOPERATION 114.

98. See 1950 AMERICAN COOPERATION 309-342; 1948 AMERICAN COOPERATION 133-143.

99. See BERLE AND MEANS, THE MODERN CORPORATION AND PRIVATE PROPERTY (1932, reprinted 1948).

Control actually is vested in each intermediary board of directors in the cooperative hierarchy, but theoretically its roots are in the local association and its members. The managerial structure is thus a representative one common to modern corporate enterprise. The Southern States Cooperative is illustrative. That association serves seven states[100] and has a membership of over a quarter of a million farmers.[101] It was decided that members could feasibly exercise control only by vesting their authority in a delegate body attending the annual stockholders' meetings.[102] In each locality where there is established a cooperative service agency, members elect a local board of directors to represent them both in the conduct of the local service and in the policy making of the Southern States Cooperative itself. Single delegates selected from each of these local boards constitute the delegate body.[103] At the annual meeting, the delegates elect the Cooperative Board of Directors in whom ultimate authority reposes.

Both the representative system of control and the concentration of the members' power at the annual meeting to effect policy through their representatives are logical and common developments in democratic control. However, a danger inherent in predicating control upon this basis is the relative inability of an individual member to perceive the effect that his vote may have. This results in an apathetic attitude on the part of members toward participation in the affairs of their organization. For example, a recent study of the agricultural cooperatives in Iowa[104] revealed that two-fifths of the members felt that they exerted no influence in the management of their cooperative, and the same proportion had never attended the scheduled meetings.[105] While 70 percent felt that they had some responsibility toward their organization, only six percent mentioned that this was to be evidenced by voting and attendance at meetings; and of this small number, slightly more than half actually engaged in these activities.[106]

Since the entire representative system is predicated upon the judicious selection of a local board, it is essential that the members actively

100. They are Delaware, Kentucky, Maryland, North Carolina, Tennessee, West Virginia, and Virginia. 28TH ANNUAL REPORT, SOUTHERN STATES COOPERATIVE 1 (1951).

101. *Id.* at 3.

102. For many years it was the policy to have all local board members attend the annual meeting, but when their number reached 3,304 it became a near physical impossibility. *Id.* at 2.

103. See 28TH ANNUAL REPORT, SOUTHERN STATES COOPERATIVE 2-3 (1951).

104. BEAL, FESSLER, AND WAKELEY, AGRICULTURAL COOPERATIVES IN IOWA; Farmers' Opinions and Community Relations, Agricultural Experiment Station, Iowa State College, Research Bull. No. 379 (1951).

105. *Id.* at 193-194.

106. *Id.* at 191.

participate on the local level. However, a survey made by the F.C.A. of 237 managers and 2,750 members of the Southern States Cooperative disclosed that 73 percent of the patron-members had not attended the last meeting of their local cooperative, and 45 percent had never attended an annual meeting.[107] This low degree of participation in the local organization in the Southern States may be partially explained by the fact that it is primarily a purchasing cooperative, and it might be expected that member interest would not be as great as in a marketing association where economic benefit is more directly keyed to its successful functioning. This, however, in no way excuses or modifies the fact that democratic control is not being utilized to a safe extent. Moreover, this same lack of direct interest and contact on the part of members was found by the F.C.A. in the milk distributing associations of the country, in whose functioning the members should be vitally concerned.[108]

Membership participation in cooperative affairs is found to vary inversely with the size of the association and with its technicality and specialization, for the members, unskilled in the techniques of mass purchasing and marketing operations, find it increasingly difficult to comprehend and make decisions on the problems of large-scale cooperative enterprise. The representative system results, and the members help formulate the broad policies within which the board of directors and the manager chosen by the board function. To insure the rendition of experienced service, stability of membership on the board is encouraged. Accordingly, some cooperatives have retained the same directors for twenty to thirty-five years,[109] with the trend favoring staggered terms of from six to ten years.[110] The manager, who is now responsible for the complex details of cooperative administration, is no longer merely a farmer-member who devotes whatever time he can spare to the business for but nominal remuneration. The requirements of modern cooperation demand that he be a full-time, skilled businessman.[111]

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107. 18 NEWS FOR FARMER COOPERATIVES No. 7, p. 11 (1951). For a study of Vermont Cooperatives, see ADAMS, VERMONT COOPERATIVES, THEIR BUSINESS AND ACTIVITIES, Agricultural Experiment Station, University of Vermont and State Agricultural College Bull. No. 540, p. 25 (1950).

108. HERRMANN AND WELDEN, DISTRIBUTION OF MILK BY FARMERS' COOPERATIVE ASSOCIATIONS 66 (F.C.A. CIRC. C-124, 1941).

109. 1948 AMERICAN COOPERATION 179-180.

110. See 1948 AMERICAN COOPERATION 180; 15 NEWS FOR FARMER COOPERATIVES No. 2, p. 14 (1948) advocating staggered terms rather than an automatic retirement plan. See also SURVEY STRUCTURE AND METHODS OF (OHIO) FARM BUREAU COOPERATIVE ASSOCIATION INC. AND ITS MEMBER COUNTY ASSOCIATIONS 19 (F.C.A. SPEC. REP. No. 123, 1943).

111. A 1950 Indiana study revealed that the salary range for managers in the state was from $3,000 to $11,000, the average being $5,200. Letter to the INDIANA LAW JOURNAL from Vance E. Lockhart, Educational Fieldman, Indiana Farm Bureau Co-

The information upon which intelligent democratic control is based is being provided principally through the annual meetings, house organs, circular letters, annual reports, and personal contact through fieldmen. While managers tend to consider annual meetings as the most important educational and contact method, the recorded evidence of the interest in and attendance at these meetings indicates that they are not always so regarded by the members. In a federated organization, while large attendance at the annual meeting may not be necessary because of the delegate system, the local association's meetings should be well attended. In a centralized cooperative, the annual meeting is of unquestioned importance. In a recent study,[112] however, patrons voted the annual meeting as fifth in importance, voting house organs as of first importance in their contact with and information on cooperative activities, personal contact second, the circular letter third, and the annual report fourth. This willingness to rely for information upon printed material prepared by interested parties, which furnishes little opportunity for scrutiny as to accuracy, may be related to the apparent tendency to abdicate control.

It is evident that modern cooperative development has modified the two functional principles of the patronage refund and democratic control. The patron-member no longer necessarily receives directly the savings which cooperative effort theoretically nets him. A change has likewise occurred in the application of the principle of democratic control, where a representative system has in many large cooperatives replaced direct influence, and the sphere of control of the individual member has been transformed from one involving the detailed operation of the business to one composed of broad policy determination. To meet the practical requirements of business management, greater authority is being centered in the boards of directors and the general manager of the state or regional society. Thus, in becoming big business, cooperatives have assumed the correlative organizational characteristics with consequent alteration of traditional cooperative principles. The logical inquiry concerns the remaining advantages of cooperative enterprise.

The study of Iowa agricultural cooperatives, which may be considered illustrative, revealed that almost 40 percent of the farmers interviewed acquired membership in order to save money.[113] Nearly 30

operative Association, Inc. (Nov. 19, 1951). See also HOLLANDS, MONTANA FARMER COOPERATIVES 1941 AND 1946, Montana State College Agricultural Experiment Station Bull. No. 449, pp. 10-11, 20-21, 27, 31, 35-36 (1948).

112. 18 NEWS FOR FARMER COOPERATIVES No. 7, p. 11 (1951).

113. BEAL, FESSLER AND WAKELEY, *op. cit. supra*, note 104, at 187.

percent indicated that they became members because the cooperative was the most convenient marketing or purchasing source.[114] Seven percent joined because they approved of the cooperative business methods.[115] In listing the benefits which they considered resulted from cooperative membership, 92 percent were of the opinion that the cooperative actually saved them money.[116] Seventy-eight percent believed that the competition which the cooperative injected into the market had an advantageous effect upon prices.[117] Forty percent considered that gain resulted from doing business with one's own company.[118] There are thus two general areas in which benefit is thought to result, the economic and the socio-psychological.

While cooperation may not return to members cash in substantial amount through the patronage refund, economic gain nevertheless is thought to result. The principle merit of cooperative association is its ability, either directly by its own operating efficiency or indirectly through its competitive effect on quality, on services, and on prices to effect substantial savings for its farmer-members. The modern state and regional association, in addition to its function as a marketing outlet for agricultural products, may be a source of fertilizer, feed and seed, petroleum, and farm machinery and supplies.[119] For example, the Farm Bureau Cooperative Ass'n, Inc. of Ohio had a total volume of business in 1950 of about 52.5 million dollars.[120] Marketing activities accounted for 34 percent of the total, feed and seed sales for 23 percent, petroleum sales for 22 percent, farm machinery and supplies 12 percent, and fertilizer 9 percent.[121] In addition to the benefits of united purchasing and marketing, farmers through cooperative effort are able to devote funds to agricultural research designed to develop improved feeds, fertilizers, seeds and plants, together with the development of new uses for farm products.[122] They are able to undertake large promotional campaigns

114. *Ibid.*
115. *Ibid.*
116. *Id.* at 198.
117. *Id.* at 197.
118. *Id.* at 198.
119. Owen Forbes, President of the Southern States Cooperative expressed cooperation's value in this manner: "The net worth or patron equity is now nearly twenty-two million dollars. However, I do not think that this is a true yardstick to measure the worth of Southern States to farmers. The true worth of Southern States to me as a farmer lies in the fact that I and 250,000 other farmers can get our feed, seed, fertilizer, and farm supplies—that have stood all the tests as to quality—at a fair and reasonable price." 28TH ANNUAL REPORT, SOUTHERN STATES COOPERATIVE, 1 (1951).
120. 1950 ANNUAL REPORT, OHIO FARM BUREAU COOPERATIVE ASS'N, INC. 5.
121. *Ibid.*
122. See for example the report made of the research activity of the Eastern States Farmers' Exchange, Inc., in 27 EASTERN STATES COOPERATOR No. 4, pp. 6-9 (1951).

to increase sales and to develop consumer loyalty to their brand names, as evidenced by the market demand for Sunkist oranges, Diamond Walnuts, and Eatmore Cranberries.

While many of these services are rendered by the state association exclusively, in some areas where the operational and development costs are high, several state associations combine. United Cooperatives, Inc., for example, is a national organization which serves as a manufacturing and procurement agency to obtain miscellaneous farm supplies for twenty-seven regional associations throughout the United States and Puerto Rico.[123] Cooperative Mills, Inc. operates a large feed mill at Reading, Ohio, and is owned by four cooperative associations.[124] Six state and regional cooperatives jointly own Select Feeds, Inc., which provides its members with a purchasing and processing service of grasses and legume seeds.[125] The National Farm Machinery Cooperative, Inc., is owned by twelve such organizations.[126]

The California Fruit Growers Exchange System furnishes an excellent example of what farmers may accomplish through cooperative effort.[127] Practically every phase of the processing and marketing of members' products is owned by them. The System not only packs and sells the fresh fruit, but also through its exchange product companies processes the fresh fruit into juices, liquid and frozen, concentrates, acids, molasses, pressed and distilled oils, pectin albedo, the various pectates, pectins, and vitamin "P". The producers thus own a business which utilizes the whole fruit, the juice, the peel and the pulp. No single farmer could accomplish this and gain the resulting marketing advantages. Through this method, a surplus of fresh fruit may be offset by markets for processed products, and, in the processed form, the product may be withheld from the market until prices improve.[128]

In addition to economic benefit accruing to farmers from cooperation, socio-psychological advantages may result as well. As was noted

123. See SOLVING A PROBLEM, PENN. FARM BUREAU COOPERATIVE ASSOCIATION 23 (2d ed. 1951).

124. *Id.* at 25.

125. *Ibid.*

126. *Ibid.*

127. See THE CALIFORNIA FRUIT GROWERS EXCHANGE SYSTEM 72-87 (F.C.A. CIRC. C-135, 1950).

128. For example, the Cranberry Growers Council formed in 1949 by the American Cranberry Exchange, the marketing agency, and the National Cranberry Association, the processing organization, determines the percentage of the crop to be sold fresh, the percentage to be processed, and the amount to be retained by the Council to be disposed of as conditions warrant. In 1951, the decision was to market 40 percent of the crop fresh, to can a like amount, and to hold the remaining 20 percent. 18 NEWS FOR FARMER COOPERATIVES No. 9, p. 8 (1951). For a discussion of some of the early efforts at production control see: BLANKERTZ, MARKETING COOPERATIVES 223-236 (1940); NOURSE, THE LEGAL STATUS OF AGRICULTURAL COOPERATIVE 12-20 (1927).

in the Iowa study,[129] 40 percent of the cooperative members conceived a benefit from doing business with a firm in which one holds interests. Cooperation in this respect is considered a great moral force, re-humanizing business, integrating self-interest and social responsibility, and bridging the gap between the producer, the entrepreneur and the consumer.[130]

Finally, there is the very sincere feeling of cooperative advocates that the cooperative structure, based as it is upon mass ownership, benefit, and control, is an example of the initiative, the courage, and the resourcefulness of free men to solve their economic problems, and as such is a practical alternative to socialism, fascism, and communism.[131]

CONCLUSION

The modification of the Rochdale principles, although altering the form in which benefits are derived from cooperative enterprise, does not decrease the value of such effort. The original theory of the patronage refund resulting in immediate monetary gain has been largely supplanted by a less direct form of economic benefit arising from the market advantages of large scale operation. The concomitant expansion has forced members to relinquish direct control over details of opera-

129. See note 118 *supra.*

130. "When and wherever the urban economy and, later, the commercial and capitalistic economy develops, all social bonds between producers and consumers are broken, not merely by the physical distance separating the two groups, but still more by the impersonal and abstract nature of purely economic relations. . . . Cooperatives both of town and of countryside develop an awareness of the bonds uniting them . . .[to] bring new life to the old moral conceptions of the 'fair price' and the 'fair wage'." FAUQUET, LE SECTEUR COOPÉRATIF. *Essai sur la place de l'homme dans les institutions cooperatives et de celles-ci dans l'économie* 35-36 (4th ed. 1942) as quoted in THE COOPERATIVE MOVEMENT AND PRESENT-DAY PROBLEMS, International Labour Office Studies and Reports Series H, No. 5, p. 81 (1945). See LANDIS, COOPERATIVE ECONOMY 17, 172 (1943).

A sociological trend of recent years has been the gradual decrease of the village, once so vital in American life. Cooperation may offer a means by which to at least partially counteract this tendency. A recent study of Iowa villages, communities of less than 5,000, shows that since 1925, an increasing number of them have cooperatives and those that do are in better financial condition than those which have no cooperative in them. 18 NEWS FOR FARMER COOPERATIVES No. 9, p. 6 (1951).

131. "Cooperation is more than a manner of conducting business, it is a way of life . . . . Cooperation does not partake of the evils of the other two choices [totalitarianism or capitalism]. It does not demand obedience to a totalitarian state nor does it allow wealth to be concentrated in the hands of the few. It effectively circumvents both of these evils by placing the control of business in the hands of the people where it belongs. This is free enterprise of the highest order." 1950 AMERICAN COOPERATION 151, 172. See SELLING, FARMER COOPERATIVES AS COMPETITORS, 24 HARV. BUS. REV. 215 (1946).

Some writers advocate a complete cooperative democracy. See WARBASSE, COOPERATIVE DEMOCRACY cc. X & XVI (5th ed. 1947).

tion to the boards of directors and managers, yet retaining potential influence over broad policy considerations through a representative system which is effective only to the extent of the members' active participation in cooperative affairs.

Viewed in historical perspective, the fundamental tenets were a means of inducing individuals to pool their economic activity and, as owners and primary beneficiaries, to organize it in what is now substantially a corporate form. Today the advantages of cooperation accrue, not from those abstract principles, but from the actual results of such combined activity tailored to meet the demands of a modern competitive economy. Economic gain to members, the most significant aspect of cooperative endeavor, is complemented, in an association with an active membership-relations program, by the psychological satisfaction derived from doing business with one's own company, the pride of ownership and success.

Cooperation is thus seen as a form of self-help by farmers, as aided by the governmental policy of encouraging private ownership and economic initiative. The continued success of such united effort is keyed to the degree of adherence to the basic premise that it is exerted to advance the well-being of the farmers who comprise the cooperative membership.

Part II

Legal Aspects of Cooperative Organizational Structure

A leading proponent of agricultural cooperation has characterized the plight which engendered the need for agricultural marketing combinations as the inability of the individual farmer to exact from a buyers' market his "just economic due."[1] The terminology employed alone renders the advocate's objectives suspect. But claims for preferential treatment of the cooperative corporation or association cannot be summarily rejected. They may be intelligently appraised only against the backdrop of economic conditions which stimulated the cooperative movement and which, to an unascertained extent, still prevail.

Due to seriously depressed conditions in the agricultural markets in the early decades of this century, it was perceived that encouragement of producer combination to augment the farmers' bargaining power was essential not only to their own well-being but also to that of the economy as a whole. To this end, solicitous judicial treatment and favorable legislative enactments have insulated agricultural organizations from the impact of state and federal statutes condemning combination.[2] The agricultural marketing organizations which have evolved have assumed various forms. Legal relationships figuring prominently in this evolution include the corporation, unincorporated association, trust, agency, partnership, and bailment. The cooperative, chameleon like, may staunchly invoke its status as an entity in one situation while emphasizing in another context, the agency aspect of its activity.

Judicial acceptance of such apparent inconsistencies finds adequate explanation only in an inarticulate conviction that cooperation should be facilitated even at the sacrifice of individual interests and doctrinal symmetry. In each instance, the fundamental problem is one of balancing the desirability of deferring to the aims of cooperation by characterizing a transaction in the light most favorable to the association against the disadvantage this course entails, such as defeat of an adverse party's reasonable expectation. Decision rests ultimately on social and economic

1. "By 1890, however, labor and agriculture generally realized that their bargaining ability to extract their just economic due from the total annual goods and services was feeble when compared with the bargaining power of capitalistic corporate groups inherent in the pricing power of big corporations and their subsidiaries and affiliated companies." Jensen, *Integrating Economic and Legal Thought on Agricultural Cooperatives* in COOPERATIVE CORPORATE ASSOCIATION LAW—1950, 37 (Jensen Ed. 1950).

2. See Part IV *infra, passim.*

policy considerations beyond the scope of this discussion. It is an ambitious objective merely to attempt to cast aside the judicial trappings frequently obscuring troublesome facets of the organizational structure of cooperatives and objectively present the controversies involved.

A major source of difficulty in fitting the farm cooperative, whether a corporation or an unincorporated association, into the same legal mold as its counterpart in businesses conducted solely for profit[3] is the dual relationship of the patron-member to the enterprise. He is both a proprietor and one of the vendors with whom the cooperative transacts the bulk of its business. Hence the rights and obligations of the member and of the organization stem from two distinct sources. The vendor-vendee[4] aspect of this relationship is usually governed by a comprehensive, standardized agreement, entered into by each grower, referred to as the marketing contract. While the numerous problems emanating from this relationship will be discussed in detail in a later section, recognition of the court's reluctance to release a producer from his contractual obligation in the event of a material breach by the association is important at this juncture.[5]

Problems to which the immediate discussion is addressed are primarily those created by the association agreement, which governs the member's relation to the cooperative in his capacity as an investor and proprietor. This includes matters commonly embraced in the articles and by-laws of an ordinary corporation, such as provisions relating to powers of the organization, election and duties of directors and officers, rights of creditors, qualifications of membership, and allocation and distribution of income. The unique position of the patron-member may compensate, in part, for seeming inequities in judicial construction of the marketing agreement. Improvident management detrimental to the interests of the grower may frequently be checked in his capacity as a

3. "Profit" is used in the traditional sense, *i.e.* return on invested capital. Viewed from another perspective, the co-op is not a nonprofit enterprise. It lacks all of the distinguishing characteristics of an eleemosynary corporation. Its activities are calculated to enhance the financial position of its participants in proportion to their patronage.

4. This term is used loosely to characterize the marketing transaction. See Part III *infra, passim.*

5. Since the success of cooperation depends upon accumulation of substantial market control to enable farmers to present a unified front against the highly organized market for the produce, the courts have long accorded equitable remedies to the cooperative to enforce marketing contracts, while regarding with disfavor attempts of the individual grower to withdraw his crop from the pool. *E.g.,* in Nebraska Wheat Growers' Ass'n v. Smith, 115 Neb. 177, 195, 212 N.W. 39, 44 (1927), in a suit for specific enforcement of a marketing agreement, the court rejected a defense of mismanagement by the association's officers. It was observed that the members had at their disposal ample means to insure the directors' compliance with the trust reposed in them without resort to repudiation of their marketing contracts. See Part III *infra, passim.*

shareholder or proprietor of the enterprise, not only through immediate control over directors and officers but also by means of remedies available to correct abuse of discretion.

The interaction of these two aspects of the member-patron's relationship to the cooperative is aptly illustrated in *Brame v. Dark Tobacco Growers Cooperative Ass'n.*[6] The ostensible purpose of the cooperative was to market dark tobacco grown by its members. Several growers discontinued production of dark tobacco and entered the more lucrative business of raising burley. The Dark Association received this substitute crop, disposing of it through an agreement with a burley cooperative, and adopted the position that its contracts with its members entitled it to handle *all* tobacco grown by them. Patrons of the Dark Association had entered into separate marketing and association agreements. At the instance of a recalcitrant burley producer, the court determined that the growers had not obligated themselves to deliver to the organization any tobacco except the dark variety. In arriving at this conclusion, the court conceded that the liberal use of "tobacco" in the *marketing* agreement would support the broad construction urged by the association. However, the *association* agreement and subsequent articles of incorporation indicated clearly that the sole purpose of the organization was to merchandise dark tobacco.[7]

While sometimes realistically merged with the marketing contract, the association agreement constitutes a distinct relationship independently governing numerous aspects of the member's interest in and obligations

6. 212 Ky. 185, 278 S.W. 597 (1925).

7. A persuasive factor militating against the contrary result may be found in the court's determination that the two products are not in competition since dark is mostly exported and used for different products. "An orderly marketing of burley is not essential to establish dark tobacco markets or minimize speculation or waste in production or marketing of dark tobacco." Brame v. Dark Tobacco Growers' Coop. Ass'n, 212 Ky. 185, 196, 278 S.W. 597, 602 (1925).

The technique here employed presumably achieved a result commensurate with the actual intent of the parties to the two agreements. Careful differentiation of the two relationships will facilitate clear analysis of the difficulties which arise between members and cooperative and promote certainty in their dealings. Following meticulous characterization of the problem, however, resort to a separate set of relations may well be justified in seeking indicia of the intended connotation of the particular agreement in question. The courts frequently have not observed this degree of care in their approach to the problems of cooperatives.

Another decision in which the court apparently relied heavily upon the membership arrangement to solve a conflict arising under the marketing contract is Kansas Wheat Growers' Ass'n v. Rowan, 125 Kan. 710, 266 Pac. 101 (1928). In a suit to recover damages for breach of the marketing contract and to enjoin the grower from disposing of wheat then in his possession, the defense was interposed that the agreement had been procured by fraudulent representations of the co-op's agent. Pointing out that defendant had signed the articles and by-laws and hence was affected with knowledge that the representations were ultra vires, the court rejected his contention that he had justifiably relied upon such representations.

to the cooperative which are entirely beyond the scope of the former instrument. For example, in *Burley Tobacco Growers' Cooperative Ass'n v. Tipton*,[8] all marketing contracts with growers had expired. It was urged that the association having become inactive, continued retention of the so-called "1% fund", deducted from gross sales for operating costs, credits and commercial purposes, served no useful purpose. Hence, suit was initiated to compel the association to reduce the fund to cash and distribute it among the members. The court conceded that ultimately the fund was destined for such distribution. But it sustained the directors' exercise of discretion in retaining this asset, invested in warehousing corporations upon which possible future operation was dependent, on the ground that maintaining the association in readiness to resume business might well be in the best interest of the members. Under the association agreement, authority to make such decisions is conferred upon the board of directors; that the organization no longer possessed any marketing contracts did not vitiate this underlying agreement.

The validity of the marketing contract, on the other hand, may well depend upon the existence of a supporting membership agreement between the patron and the association. In *Tulsa Milk Producers' Cooperative Ass'n v. Hart*,[9] the cooperative sued an alleged member for nondelivery of his crop. Since he only had signed a marketing agreement, prior to incorporation, and had never thereafter perfected his membership in the organization, the court sustained his defense based on the theory that under the by-laws the contract could not become operative until the contracting grower had become a member of the association.[10]

8. 227 Ky. 297, 305, 11 S.W.2d 119, 122 (1928).

9. 145 Okla. 263, 292 Pac. 558 (1930).

10. See also Edmore Marketing Ass'n v. Skinner, 248 Mich. 695, 227 N.W. 681 (1929). Plaintiff, a cooperative, sued defendant for liquidated damages for nondelivery of a portion of his 1928 crop (deliveries had been made for prior years). Defendant successfully defended on the ground that a condition precedent to enforcement of the marketing contract had not been fulfilled, since 50% of the potato acreage in the specified territory had not been enlisted. Defendant's prior deliveries were not deemed to constitute a waiver since he had no means of knowledge regarding compliance with the condition. It was further argued on behalf of the co-op that since liquidated damages provision had been incorporated in the by-laws, the grower was liable on that basis. However, it was found that defendant had exercised no rights of membership aside from his participation in the marketing agreement. Since the latter was invalid, so was the alleged membership. This case provides further illustration of the complex inter-relationship between the two agreements.

An interesting decision concerning a suit upon a pre-incorporation marketing contract is Hart Potato Growers' Ass'n v. Greiner, 236 Mich. 638, 211 N.W. 45 (1926). A 50% acreage provision similar to that in the Edmore case was involved. After the co-op had been incorporated and defendant had received proper notice that the requisite acreage had been acquired, he defaulted on his commitment to deliver his crop. Sustaining the cooperative's cause of action, the court spurned defendant's insistence that plaintiff

This complex status of the grower-member, a significant point of differentiation between the cooperative and other corporations,[11] explains an important peculiarity of cooperative law. The modern position with regard to ultra vires transactions and apparent authority—to the effect that a corporation is estopped to disclaim the detriment of a contract entered into in the regular course of business on the ground that the undertaking was beyond its power or its agent's authority—has limited impact upon the dealings of a cooperative. The farm cooperative transacts most of its business with members. And, since members are presumed to have cognizance of the exact scope of the cooperative's powers, they may not urge the doctrine of estoppel against the organization if it subsequently repudiates the arrangement as an unwarranted assumption of authority or an ultra vires act.[12]

Potentially one of the most effective weapons available to the member to insure honest, prudent direction of his organization and prevent unwarranted inroads upon his proprietary interest is the suit to redress breach of a fiduciary duty. It seems plausible that the source of such a fiduciary relationship may be either the association agreement or the marketing contract. Indeed, this is an area in which the courts have failed to articulate precisely the origin of the obligations which they impose. It may be suspected that such a duty is frequently derived from the overall character of the two interconnected relationships. A possible explanation may well be a judicial desire to find a substitute remedy to fill the gap left by the extraordinary constructions which have been engrafted upon marketing contracts to enable cooperatives to preserve their market control. In view of the inadequacy of established contract remedies to protect the interests of patrons, the fiduciary theory of

had no legal existence when the contract was made and that it was initially wanting in mutuality. Defendant had made an offer in writing to enter a contract with the proposed corporation and had held the offer open until it had been accepted by the duly constituted entity. In another suit on a pre-incorporation marketing contract the same result was achieved on the basis of estoppel. Kansas Wheat Growers' Ass'n v. Windhorst, 131 Kan. 423, 292 Pac. 777 (1930).

11. To this effect see Cooperative Milk Service v. Hepner, 81 A.2d 219, 224 (Md. 1951). "Cooperative associations differ from ordinary business corporations principally in that they do most of their business with their own members. . . . It may be doubtful whether an ordinary business corporation, if and when it deals with its stockholders as such, is under any less duty of fairness and equality than a cooperative. Stockholders are not trustees or *quasi* trustees for each other. . . . But when majority stockholders use their voting power for their own benefit, for some ulterior purpose adverse to the interests of the corporation and its stockholders as such, they thereby become fiduciaries and violate their fiduciary obligations."

12. California Canning Peach Growers' Ass'n v. Williams, 69 P.2d 893 (1937), *subsequent opinion*, 11 Cal.2d 221, 78 P.2d 1154 (1938); California Canning Peach Growers Ass'n v. Harkey, 69 P.2d 915 (1937), *subsequent opinion*, 11 Cal.2d 188, 78 P.2d 1137 (1938); Kansas Wheat Growers' Ass'n v. Rowan, 125 Kan. 710, 266 Pac. 101 (1928).

redress and other remedial devices assume increased significance in this area. Hence, more widespread acceptance of this theory is to be encouraged, as is the development of high standards of director responsibility.

Due to the principle of equality, which is deeply engrained in the philosophy underlying the cooperative movement,[13] and the fact that directors are typically farmers who themselves conduct considerable business with the association and are therefore thoroughly familiar with its method of operation, a persuasive argument can be advanced for the imposition of a higher fiduciary standard upon such directors than that enjoined upon ordinary corporate officials. However, if encouragement of a vigorous and expanding cooperative program is the primary objective, the desire to subject cooperative officials to an exacting standard of conduct for the protection of individual participants must be tempered by the realization that such stringent requirements may unduly fetter managerial discretion or deter capable men from assuming the burdensome responsibilities.[14]

Under the traditional view applied to ordinary corporations, a director is not responsible for the misdeeds of officers or agents, other than his co-directors, unless he was a direct participant, failed to exercise ordinary care in the selection or supervision of the offending officer, or knew or had reason to know of the dereliction. This rule has been applied to cooperative directors,[15] although to absolve such officials from liability to this extent is perhaps unrealistic, in view of the directors' more intimate connection with the everyday affairs of the association. When the action of directors themselves proves highly detrimental to certain stockholders with a consequent advantage inuring to others, a fiduciary duty has been imposed. Where directors of a corporation, pursuant to a plan for reorganization, arranged the purchase of shares from stockholders ineligible for membership in the contemplated cooperative,

13. See notes 43-57 *infra*, and accompanying text.

14. "Experience demonstrated that if co-operative societies were to be really encouraged, a law was necessary which would offer the advantages of corporate form to exchanges, unions, and other associations, and at the same time allow great freedom of self-direction and self-control in the co-operative effort for mutual benefit." Loch v. Paola Farmers' Union Coop. Creamery & Store Ass'n, 130 Kan. 136, 138, 285 Pac. 523, 524 (1930).

15. In Lowell Hoit & Co. v. Detig, 320 Ill. 179, 50 N.E.2d 602 (1943), the court enunciated this general rule, absolving directors from liability for conversion by the manager of the cooperative, of which the directors had no knowledge and which they could not have discovered in the exercise of ordinary and reasonable supervision.

For a decision imposing a patently lax standard of conduct upon erstwhile directors who perfect preferences in the insolvent co-op's assets immediately upon resignation, see Farmers Co-operative Ass'n of Bertha, Minn. v. Kotz, 222 Minn. 153, 23 N.W.2d 576 (1946).

the court perceived a fiduciary relation between the managing officers and the shareholders, with a concomitant duty to make full disclosure to such shareholders of all facts relevant to evaluation of the shares subject to purchase.[16] In *Bogardus v. Santa Ana Walnut Growers Ass'n*,[17] members of a marketing cooperative sought to prevent the association from distributing to withdrawn members money returned to the local from the central cooperative. There funds had originated in the central's operating reserve fund to which the ex-members had contributed. The court construed a by-law forfeiture provision as inapplicable to a withdrawn member's interest in the revolving fund to which he has contributed. Despite language of purchase and sale and references to passage of title in the marketing contract, the actual relation between the grower and the cooperative was one of a trust or fiduciary character.[18] The funds in controversy constituted a trust res, distributable on a pro rata basis to each contributor.[19] Implicit in *Cooperative Milk Service v. Hep-*

16. Snyder v. Colwell Cooperative Grain Exchange, 231 Iowa 1210, 3 N.W.2d 507 (1942).

17. 41 Cal. App.2d 939, 108 P.2d 52 (1941).

18. Another case which has recognized the "trust fund doctrine", at least to a limited extent, is Burley Tobacco Growers' Cooperative Ass'n v. Brown, 229 Ky. 696, 707, 17 S.W.2d 1002, 1006 (1929). The court there observed: "It may be that it would be improper to call the fund a general corporate asset, [1% reserve fund] and it may be that it would be improper to call it a trust fund, but it is a corporate asset which may be used for the specific purposes mentioned in the contract, and it partakes of the nature of a trust fund in that any balance unexpended for purposes mentioned in the contract will be distributed at some time, either when the association so directs, or when its existence is at an end."

In Rhodes v. Little Falls Dairy Co., 230 App. Div. 571, 245 N.Y. Supp. 432 (Sup. Ct. 1930), a patron sued a milk handling cooperative for an accounting and for distribution of his proportionate share of withheld earnings. The court observed that plaintiff's complaint alleged facts constituting a fiduciary relationship similar to a joint venture, "in which case an action in equity is maintainable for an accounting, and is not unlike that of an agent who has been intrusted with his principal's money or property to be expended or dealt with for a specific purpose, in which case the agent is at all times amenable to the process of the court to show that his trust duties have been performed and the manner of his performance." Nor was it necessary that there be a technical trust. Where a relationship of agency and confidence exists and the agent has received property of the principal for which he refuses to account, a court of equity may take jurisdiction. *Id.* at 573, 245 N.Y. Supp. at 434.

19. It should be noted that the fiduciary duty extended to withdrawn, as well as existing members, and required distribution on a pro rata basis to each contributor to the fund in question. Bogardus v. Santa Ana Walnut Growers' Ass'n, 41 Cal. App. 2d 939, 956, 108 P.2d 52, 58 (1940).

A case in which the court arguably refused to limit the scope of a director's fiduciary duty to consequences of his own acts or omissions is Kansas Wheat Growers' Ass'n v. Windhorst, 131 Kan. 423, 292 Pac. 777 (1930). Defendant member sought to resist suit for breach of his marketing contract on the ground that the acreage control requisite to put the contracts into effect had never been achieved. He had been an inactive member of the committee responsible for certifying that the prescribed acreage had been secured. The court rejected his contention that only his own acts and omissions should be imputable to him. However, the case can be viewed as one in which he had no right

ner[20] is a similar recognition that officers and directors of a cooperative occupy a position of trust with regard to their members and may not favor one faction at the expense of another.[21] The court also suggested an interesting analogy which might be used as a basis for advocating recognition of a fiduciary duty in all instances in which officials deal with members, *i.e.*, the most highly developed observance of the fiduciary concept in the corporate field is in the area of direct dealings between officers and shareholders. As previously pointed out, this phenomenon, unique in ordinary corporate dealings, is a typical attribute of co-operative transactions.[22]

One pitfall which the injured patron must carefully avoid is the adeptness with which courts have discerned a waiver of rights against directors and officers based on some form of acquiescence in the challenged activity. Failure to object promptly upon discovery of fraudulent inducement to enter a marketing contract has been deemed a waiver of the right to rescind.[23] Amendment of a charter to permit accumulation of reserves, although only prospective in effect, coupled with negotiation of a new marketing contract subsequent to the change, has been regarded as an affirmation of the association's previous improper accumulation of reserves.[24] The absence of objection to a deviation from the prescribed allocation of profits and losses until such time as the non-observance of this provision proves detrimental to the challenger has been characterized as consent to modification of the contract.[25] Failure to select competent officers may deprive members of the right to question performance of the trust reposed in such officials.[26] While these decisions may appear harsh due to the absence of certain elements of estoppel, in each case acceptance of the plaintiff's theory of recovery might have proved injurious to the success of the organization. Under such circumstances the court may be tempted to subordinate the rights

to rely upon the good faith and diligence of other members of the committee and hence was held for a negligent omission.

20. 81 A.2d 219 (Md. 1951).

21. In the Hepner case, *supra* note 20 at page 224, the court suggested that when majority shareholders use their voting power for their own benefit, to the detriment of the interests of the co-op or its minority shareholders, they may become fiduciaries and violate their fiduciary obligations.

22. However, see notes 55-56 and accompanying text, to the effect that some members may be benefitted to a greater extent than others, if for reasons beyond the control of the co-op.

23. Kansas Wheat Growers' Ass'n v. Oden, 124 Kan. 179, 257 Pac. 975 (1927).

24. Mountain View Walnut Growers' Ass'n v. California Walnut Growers' Ass'n, 19 Cal. App.2d 227, 65 P.2d 80 (1937).

25. Matanuska Valley Farmers' Coop. Ass'n v. Monaghan, 188 F.2d 906 (9th Cir. 1951).

26. Nebraska Wheat Growers' Ass'n v. Smith, 115 Neb. 117, 195, 212 N.W. 39, 44 (1927).

of the individual to the interest of the group and may indulge in hypercritical scrutiny of the plaintiff's conduct to uncover some technical basis for denying recovery. Hence, the patron-member must exercise considerable diligence if he is to protect his interests against the neglect or depredations of those who conduct the cooperative enterprise.

Beyond the direct suit to redress breach of a fiduciary duty in the name of the association or in the plaintiff's own behalf, there are several other devices which may prove successful in vindicating the rights of injured members in appropriate circumstances. Perhaps foremost among these is an action for an accounting. This is an appropriate remedy where the court can be induced to characterize the cooperative as an agent entrusted with the grower-principal's property for a specific purpose. Under these circumstances a court of equity will compel the agent to reveal the nature of the questioned transaction in order to demonstrate that his duties have been properly performed.[27] Even though title may have passed and no technical trust exists, the transactions may still be considered fiduciary in character. Regarded in this light, the cooperative, which assumed the duty of disposing of its patrons' property for the best price obtainable and returning the proceeds less specified deductions, possesses knowledge access to which plaintiff is entitled; and these facts may be ascertained in a proceeding for an accounting.[28] The same result has been achieved despite by-laws expressly denying the remedy.[29]

A more drastic remedy, appropriate only in cases of extreme mismanagement, would completely wrest control from the offending directors by means of appointment of a receiver.[30] In *McCauley v. Arkansas Rice Growers' Co-op. Ass'n*,[31] this relief was sought in a complaint alleging numerous abuses from negligence to outright fraud. It was ascertained, however, that the facts failed to sustain these allega-

27. See discussion of Rhodes v. Little Falls Dairy Co., 230 App. Div. 571, 245 N.Y. Supp. 432 (Sup. Ct. 1930), in note 18 *supra*.

28. Reinert v. California Almond Growers' Exchange, 63 P.2d 1114 (1937), *subsequent opinion*, 9 Cal.2d 181, 70 P.2d 190 (1937).

29. Reinert v. California Almond Growers' Exchange, 9 Cal.2d 181, 187, 90 P.2d 190, 193 (1937).

30. An even more extreme device, in view of the general tenor of judicial opinion with regard to specific enforcement of marketing contracts, was sustained in New Jersey Poultry Producers' Ass'n v. Tradelius, 96 N.J. Eq. 683, 126 Atl. 538 (Ct. Err. & App. 1924). An association sued a recalcitrant member to compel delivery and the latter invoked the unclean hands doctrine on the theory that the association had failed to grade the produce according to the contract. While acknowledging that violation of a collateral covenant would not discharge the member from his duty to deliver, the court felt that this substantial deviation should preclude the corporation from seeking redress in equity.

31. 171 Ark. 1155, 287 S.W. 419 (1926).

tions and that the demonstrated breaches of discretion, including unauthorized purchases of rice in derogation of the association agreement, could be rectified by a restatement of accounts. Two interesting sidelights in the opinion are worthy of note: a dictum suggested that an attempt to withhold superfluous reserves for contingencies might be thwarted by injunction;[32] and breach of the association agreement was urged by plaintiffs as justification for releasing them from their marketing contracts.[33] The latter contention was summarily rejected with the observation that such a step would cripple the cooperative to the serious detriment of its remaining members. In *Doss v. Farmers Union Cooperative Gin Co.*,[34] the device suggested by the *McCauley* dictum was unsuccessfully invoked. A shareholder's suit to enjoin a cooperative from allocating net profits to patronage dividends without first paying dividends on the common stock was defeated by applying a permissive construction to the language of a typical by-law provision.[35] This decision constitutes a formidable obstacle to efforts to compel payment of a share dividend where the articles and by-laws follow this pattern.[36]

32. *Id.* at 1173, 287 S.W. at 424.

33. *Id.* at 1168, 287 S.W. at 423.

34. 173 Okla. 70, 46 P.2d 950 (1935).

35. The provisions of the by-laws dealing with dividends and profits provided for distribution in this order: (1) not less than 10% to be set aside in reserve fund until fund equals 50% of the capital stock; (2) dividends not over 8% *may* be declared at the discretion of directors, 5% may be set aside for educational purposes; (3) the remainder of the net profits shall be apportioned to members ratably on the amounts sold to co-ops by members. *Id.* at 70, 46 P.2d at 950.

36. Plaintiff further contended that under this decision, though having invested money in the business, a stockholder has no legal right to demand or expect a share in the division of profits. The court replied that a cooperative is "a special and peculiar form of business enterprise which is not within the class of corporations designed purely and solely for money profit." To strengthen this conclusion, the court quoted from Justice Brandeis' decision in Frost v. Corporation Commission, 278 U.S. 517 (1929): "The act further discourages entrance of mere capitalists into the co-operative by provisions which permit 5 percent of profits to be set aside for educational purposes; which require 10 percent of the profits to be set aside as a reserve fund, until such fund shall equal at least 50 percent of the capital stock; which limit annual dividends on stock to 8 percent, and which require that the rest of the year's profits be distributed as patronage dividends to members, except so far as the directors may apportion them to nonmembers." *Id.* at 71, 46 P.2d at 951.

In Callaway v. Farmers' Union Cooperative Ass'n of Fairbury, 119 Neb. 1, 226 N.W. 802 (1929), directors had declared a dividend and plaintiff sued to compel its declaration. The court avoided issuing a mandatory injunction requiring payment by relying on a by-law providing for submission of any proposed measure to the shareholders for approval or rejection. Finding the declaration subject to revision or veto by such a referendum or initiative, the court held that it was not binding upon the co-op until a reasonable time for referendum and review had expired. Since the directors had rescinded within such time, no rights were created by the prior declaration. While the attempt to control the conduct of directors through injunctive relief was ineffective, the case also suggests referendum and initiative as conceivable instrumentalities of control by the shareholders.

An anticipatory technique which may effectively be used to forestall contemplated managerial undertakings which threaten to undermine the interests of members or patrons is the declaratory judgment.[37] Such a proceeding may prove particularly effective in unsnarling the complexities surrounding disposition of cooperative assets upon dissolution.[38] A further measure which may be useful to the dissatisfied member who is unable to document his complaints against the association's management is the right to inspect the organization's books. This right has been sustained at common law, in the case of a nonstock cooperative corporation, although statutory provisions relating to inspection were expressly limited to stock corporations.[39]

While the remedy has not been frequently invoked, there is no reason to believe a member may not enforce a right inuring to the entity, either through a derivative or a representative action. In *Olson v. Biola Cooperative Raisin Growers Ass'n,*[40] members of a cooperative demanded that directors enforce liquidated damages provisions of the marketing contract, on the theory that delivery of wet raisins by certain members violated this agreement. Their request having been rejected, the members initiated an action against offending producers, attributing the directors' nonaction to the fact that a majority of their number had been personally involved in the alleged breach. The court tacitly acknowledged their right to thus vindicate a right of the association under these circumstances.[41] This remedy, if not rendered cumbersome by the appendage of judicial or legislative prerequisites, such as approval by a majority of the shareholders, can constitute an effective deterrent to official abuses as well as a convenient means to enforce rights of the association over the opposition of unwilling directors.

The basic attributes of cooperation—democratic control,[42] limited return on capital, and sharing of benefits, savings and risks in pro-

37. Bogardus v. Santa Ana Walnut Growers Ass'n, 41 Cal. App.2d 939, 108 P.2d 52 (1940).

38. Attinson v. Consumer Farmer Milk Co-op, 197 Misc. 336, 94 N.Y.S.2d 891 (Sup. Ct. 1950). See note 60 *infra,* and accompanying text.

39. State *ex rel.* Boldt v. St. Cloud Milk Producers' Ass'n, 200 Minn. 1, 273 N.W. 603 (1937).

40. 184 P.2d 742 (Cal. App. 1947).

41. *Ibid.* It found, however, that the liquidated damages clause was inapplicable to qualitative breaches since the damages consequent upon such default were subject to precise ascertainment.

42. An almost inevitable characteristic of the farm co-op is the one vote per member formula which emphasizes the mutual benefit of producers on a patronage basis, as contrasted with the more familiar corporate scheme of control geared to capital contribution. See Part I, p. 360 *supra.* However, deviations from this principle are not entirely wanting. See *e.g.,* Alfalfa Growers of California v. Icardo, 82 Cal. App. 641, 645, 256 Pac. 287, 289 (1927), in which voting strength was based on units of interest in the

portion to patronage—have given rise to numerous organizational problems peculiar to farm cooperatives. Each of these attributes is but one aspect of the more fundamental principle of equality underlying the entire development of agricultural cooperation. This principle merits further discussion, first in the abstract and then in the context of the various concrete situations in which proprietary and creditor interests in cooperative assets are asserted.

The real significance of the doctrine of equality as a unique characteristic of cooperation is vividly illustrated in *Connecticut Milk Producers Ass'n v. Brock-Hall Dairy Co.*[43] Although all members of this association marketed milk of the same quality, the fluid milk commanded a higher price than that sold for processing. Under a program worked out by a cooperative selling agent to dispose of "homeless" milk in the surplus season, certain members, who sold exclusively to fluid milk dealers, were in effect subsidizing others who sold, also through the cooperative, to large dairies equipped to process the excess over their fluid requirements. This was true because continued operation of the program ultimately depended upon an equalizing membership assessment, which certain of the members in the former category resisted. Sustaining the association's position, the court observed that it was: ". . .within the powers of the co-op to deal with members as a group and to call upon certain of them to surrender something of their own individual advantage in order to improve marketing conditions for those less fortunately situated."[44] While this decision supports the right of the association to juggle, to a certain extent, the interests of its patrons in an attempt to equalize the advantage inuring to each from its operation, another court[45] has imposed the exacting requirement that the cooperative account to members for proceeds of its operations strictly according to pools, since the association, an almond growers' marketing exchange, conducted its business on a pool basis. While adopting widely differing approaches to the equality principle, the two decisions are not necessarily inconsistent. In the former, the quality of the produce of

property of the association with one additional vote for each ton of alfalfa produced by each grower; and Tapo Citrus Ass'n v. Casey, 45 Cal. App. 796, 797, 115 P.2d 203 (1941), in which the articles expressly provided that voting power be unequal.

43. 122 Com. 482, 191 Atl. 326 (1937).

44. *Id.* at page 495, 191 Atl. at 332. In Tobriner, *Legal Aspect of the Provisions of Cooperative Marketing Contracts,* 12 A.B.A.J. 23 (1926), the author points out that the method of conducting co-op marketing transactions has an important bearing on this question. Use of the sale and re-sale contract permits the association greater latitude in adjustment of losses among its members than does the agency contract. For further analysis of the various marketing arrangements see Part III, *infra, passim.*

45. Reinert v. California Almond Growers' Exchange, 9 Cal.2d 181, 70 P.2d 190 (1937).

each member was identical, whereas in the latter, the almonds were classified according to size and quality.

The fundamental objective of cooperation under discussion prohibits a cooperative from deliberately favoring certain of its patrons by discontinuing its dealings with others because surplus supply threatens to deflate the market. This position has been upheld against the contention that the marketing contract of the dismissed members merely constituted the association a selling agent and that it had discharged its duty by exercising good faith in attempting to procure a buyer.[46] In this case, the court reiterated the now familiar principle of cooperative law that a marketing organization is bound to exercise the same diligence and good faith to sell the produce of one member which it exercises in behalf of any other. Under this theory, each grower has an interest in the proceeds from the sale of every other grower's crop. Hence, when a patron sells through another channel, the association is entitled to receive any benefit accruing to the recalcitrant member.[47] A perspective which frequently recurs in the cases dealing with the equality problem and which strengthens the theoretical foundation of this doctrine is the idea that the marketing contract constitutes a covenant "running to and with every other member of the association."[48]

46. 208 Wis. 40, 242 N.W. 486 (1932).

47. In California Peach Growers v. Harvey, 69 P.2d 915 (1937), *subsequent opinion*, 11 Cal.2d 188, 78 P.2d 1137 (1938), the court observed that "all members have an interest in the proceeds from the sale of defendant's peaches and are entitled to share in the sum defendant received by reason of a sale made outside of his dealings with the association." For a direct holding to the same effect see California Canning Peach Growers v. Downey, 76 Cal. App. 1, 243 Pac. 679 (1925).

A refinement of this position is to the effect that a general managing agent of a co-op, or even a director, has no apparent authority to release an individual grower from his contract. Patrons, by virtue of their contractual relation with the association, are affected with knowledge that any ostentibly official act which violates the principle of equality is unauthorized. California Canning Peach Growers v. Harris, 91 Cal. App. 654, 267 Pac. 572 (1928).

48. California Peach Growers' Ass'n v. Williams, 69 P.2d 893 (1937), *subsequent opinion*, 11 Cal.2d 221, 78 P.2d 1154 (1937); Noble v. California Prune & Apricot Growers' Ass'n, 98 Cal. App. 230, 276 Pac. 636 (1929).

The peculiar development of the law with regard to marketing contracts sometimes characterized as a lack of mutuality of remedies is perhaps best explained by this theory. If a breach on the co-op's part entitled a grower to a release, the rule of equality would be undermined and remaining members would suffer from diminished market control. McCauley v. Arkansas Rice Growers' Co-operative Ass'n, 171 Ark. 1155, 287 S.W. 419 (1926).

But see Staple Cotton Cooperative Ass'n v. Borodofsky, 143 Miss. 558, 108 So. 802 (1926), to the effect that an improper release of certain members from a marketing agreement, entitled remaining participants to release. This decision seems contra to the vast weight of authority in cases involving growers' remedies for the co-op's breach of the marketing agreement. However, when the improper releases have been so numerous as to cripple the effectiveness of the association, replacement of directors, recovery of money damages from them, and other remedies short of absolute discharge may be inadequate reparation.

An important implication of cooperative equality is the subordination of the traditional profit motive for investment to the objective of furthering the mutual interests of growers on a patronage basis. Hence, in *Doss v. Farmers Union Cooperative Gin Co.*,[49] a shareholder objected to a construction of the association's by-laws which he contended deprived him of any legal right to demand a share in the division of profits on the basis of his invested capital. Accepting the accuracy of the predicted consequences of their ruling, the court pointed out, ". . . that a co-op is a special and peculiar form of business enterprise which is not within the class of corporations designed purely and solely for money profits." This position was substantiated by reference to the epic *Frost Case*[50] in which Justice Brandeis observed that cooperative by-laws are designed to discourage investment of capital with the primary objective of earning a return.[51]

Cooperation is calculated to benefit participants personally only in so far as their interests as patrons are advanced through the operation of the enterprise.[52] A member in affiliating himself with a cooperative is primarily interested in securing access to more efficient marketing and other facilities and only in a secondary sense in acquiring a property interest which will yield monetary returns. By the same token, all contributors to a reserve fund made available for distribution have been deemed entitled to share in the proceeds despite the fact that the membership of some has terminated and their sole claim is founded upon their prior contributions. A contrary result would prefer existing members *as such* and would defeat the objective of patronage-equality.[53]

Basically, classification of members and disparity of treatment accorded them violates the equality theory. A California court frustrated efforts of a cooperative to market the crops of certain peach growers, classified as "renters" on a more favorable basis than peaches grown by

49. 173 Okla. 70, 46 P.2d 950 (1935).

50. Frost v. Corporation Commission, 278 U.S. 517 (1929).

51. See note 36 *supra.*

52. Driscoll v. East West Dairymen's Ass'n, 52 Cal. App. 468, 126 P.2d 467 (1942).

53. Consistent with the theory here enunciated, the court in Avon Gin Co. v. Bond, 198 Mis. 197, 22 So.2d 362 (1945), refused to grant an ineligible withdrawing shareholder more than par value for his stock. Since non-shareholders were entitled to participate in the assets on dissolution, granting the plaintiff the full book value of his shares upon his retirement would detract from the rights of such nonmember patrons. See also Ozona Citrus Growers' Ass'n v. McLean, 122 Fla. 188, 189, 165 So. 625, 626 (1935), in which a withdrawing member was permitted to recover his pro rata part of the existing surplus arising from "retains" attributable to the handling of crops during his period of membership. This result was achieved in spite of a charter provision for forfeiture of "all rights and privileges in the association" upon cessation of membership.

the majority of its members.[54] The principle of equality dictates that every one delivering produce to a cooperative, even in pursuance of an agreement purporting to accord preferential status, must have his rights determined by the same criteria which fix the rights of others. Reasonable classifications necessitated by the nature of the organization or the circumstances will be upheld if such devices are not inherently discriminatory.[55] A recent decision sharply emphasizes the view that no violation of equality is inherent in special treatment accorded only to a select group of members where this is the result of factors entirely beyond the control of the cooperative.[56] However, so deeply is the concept of equality rooted in the law of farm cooperatives that some courts have by indirection repudiated classification devices apparently not discriminatory as between members similarly situated.[57]

Questions involving the rights of individual members in the assets of a cooperative arise primarily in situations in which the member has severed relations with the association. When such controversies have been litigated, it will be observed that a predominant consideration has been the desire to effect a disposition fair to the individual asserting the right while at the same time adhering to the principle of equality essential to the preservation of the cooperative effort. While few clear indicia of the proper resolution of disputes concerning dissolution or consolidation of farm cooperatives are to be found, the courts will presumably adhere to the established rules governing ordinary corporations in solving such problems. Deviations can be expected in situations where existing corporation rules cannot be reconciled with the philosophy of cooperation. In such instances the doctrine of patronage-equality is likely to emerge as the guiding consideration.

In the event that the cooperative movement undergoes a decline in popularity in the future, the question of dissolution is likely to become a

54. California Peach Growers v. Harkey, 69 P.2d 915 (1937), *subsequent opinion* 11 Cal.2d 188, 78 P.2d 1137 (1937).

55. HULBERT, LEGAL PHASES OF COOPERATIVE ASSOCIATIONS 169 (F.C.A. BULL. No. 50, 1942).

56. Cooperative Milk Service v. Hepner, 81 A.2d 219 (Md. 1951).

57. In Matanuska Valley Farmers Cooperative Ass'n v. Monaghan, 188 F.2d 906 (9th Cir. 1951), a cooperative handled several different crops and agreed to pay each producer his share of the profits realized on resale of his particular crop. Actually, only a very crude allocation of profits and losses among the various crops was ever made. When this discrepancy was finally challenged, the court held that plaintiffs, by their long acquiescence in the cooperative's operations, had consented to a modification of the contract. Similarly, in Alfalfa Growers of California v. Icardo, 82 Cal. App. 641, 256 Pac. 287 (1927), the court rigorously condemned a scheme whereby control was geared to tonnage, membership fees were based on acreage planted to alfalfa, and assessments were founded upon tonnage. Refusal to enforce an assessment was attributed to the inequities which would ensue since non-owners and non-growers were entitled to membership in the association.

storm center of controversy. The problem will be magnified in intensity by one of the most startling phenomena of the agricultural cooperative development—the tremendous reserves accumulated by numerous associations through the device of deducting "retains" in excess of the association's actual expenses. At common law, disposition of assets upon dissolution was a relatively simple matter. Only members of a nonstock cooperative or shareholders of a stock company at the time of the dissolution were entitled to participate in the distribution of assets remaining after payment of creditors.[58] The method of disposition can be substantially modified by statute or by the articles or by-laws of the organization. For example, one model charter stipulates that upon dissolution, assets remaining after payment of debts and retirement of outstanding stock are to be distributed ratably to patrons "on an equitable basis."[59] Whether to define "patrons" to include former and existing growers or only those doing business with the association at the time of its demise is a latent source of controversy under this proposed article.

In a recent dissolution case,[60] the court seemingly despaired of achieving any satisfactory disposition of assets among potential claimants and announced that, in the absence of any applicable provision in the article or by-laws, the members had no rights whatsoever. The task with which the court was confronted, of unscrambling the assets and devising an equitable plan for their distribution, was indeed a formidable one. Cooperation had been inaugurated in order to organize farmers and consumers into a cooperative enterprise the announced purposes of which included the marketing of milk and furtherance of economic and cultural welfare of the members and the public. While producer-members had claimed surplus earnings attributable to their phase of the cooperative's activities, a vast number of patronage dividend vouchers printed on milk containers remained unclaimed. Referring to the fact that the association carried on an extensive public education program relating to production and distribution of milk products, the court concluded that it was primarily a civic enterprise and, broadly speaking, constituted a "charitable corporation." Hence, the court concluded that the assets were distributable, in the event of dissolution, according to

58. Clearwater Citrus Growers' Ass'n v. Andrews, 81 Fla. 299, 87 So. 903 (1921); HULBERT, *op. cit. supra* note 55, at 76. In the *Clearwater* case, the court rejected claims of withdrawn members of a cooperative, deciding, by analogy to the rule governing lodges and fraternal organizations, that a withdrawing member forfeits his interest in the association and cannot invoke the rule against enforceability of forfeitures in equity.

59. HULBERT, *op. cit. supra* note 55, at 403, 411.

60. Attinson v. Consumer Farmer Milk Corp., 197 Misc. 336, 96 N.Y.S.2d 891 (Sup. Ct. 1950).

the doctrine of *cy pres*. The case suggests the aura of confusion surrounding the problem and the difficulty of the task of delineating the rights of competing claimants which lies ahead.[61]

Although consolidation likewise poses many problems as yet unsolved, proponents of cooperation may claim a major victory in *Pearson v. Clam Falls Co-op Dairy Ass'n*.[62] Minority shareholders objecting to a proposed consolidation were required to accept shares in the newly created entity in exchange for their interests in the predecessors of the merged cooperative. In reaching this result, the court recognized that most consolidation statutes provide for optional appraisal and cash payments to dissenters, but held that the absence of such a provision in the Wisconsin statute did not render it unconstitutional. Significantly, the omission was attributed to legislative awareness of the difficulties encountered by small cooperatives in attracting new capital to finance proposed consolidations. The interests of remaining participants would be seriously jeopardized by a contrary holding. The decision is consistent with the oft-repeated view that the property interests acquired by a cooperative member are of secondary importance.[63]

Most frequent assertions of an individual interest in cooperative assets have been pressed by the withdrawing member. *Clearwater Citrus Growers' Ass'n v. Andrews*[64] has long been regarded as representative of the common law on the subject of voluntary withdrawal. It was there decided that forfeiture of all interest in the cooperative's assets was an incident of such withdrawal.[65] Carefully drawn articles and by-laws today expressly provide for voluntary withdrawal.[66] A by-law provision for payment, within twelve months, of the face value of shares of a member who dies or moves away has been upheld.[67] In *Driscoll v.*

61. In Burley Tobacco Growers' Ass'n v. Tipton, 227 Ky. 297, 11 S.W.2d 119 (1928), it was held that the fact that a cooperative association was temporarily inactive presented no ground for dissolution or distribution of assets.

62. 243 Wis. 369, 10 N.W.2d 132 (1943).

63. See note 36 *supra*.

A further issue in the *Pearson* case was whether dissenting minority shareholders must accept patronage dividends from the old corporation in the form of stock in the new. An affirmative decision was founded on the view that since patrons have no right to insist on being paid such a dividend, the form of payment is a matter within directors' discretion. Pearson v. Clam Falls Co-op Dairy Ass'n, 243 Wis. 369, 373, 10 N.W.2d 132, 134 (1943).

64. 81 Fla. 299, 87 So. 903 (1921).

65. Actually, this case did not directly involve an application of the common law since it was decided under a statute and by-law authorizing forfeiture. Clearwater Citrus Growers' Ass'n v. Andrews, 81 Fla. 299, 206, 87 So. 903, 905 (1921).

66. See contract of CALIFORNIA WALNUT GROWERS' ASSOCIATION (1940).

67. Loch v. Paola Farmers' Union Cooperative Creamery & Store Ass'n, 130 Kan. 136, 285 Pac. 523, *rehearing denied*, 130 Kan. 522, 287 Pac. 269 (1930).

East West Dairymen's Ass'n,[68] an erstwhile member demanded her pro rata share of the reserves deducted from proceeds of milk sold by the association during her term of membership. Conceding the validity of her claim to an interest in the fund, the cooperative was sustained in the contention that, pursuant to the applicable statute and by-laws, this claim could not be realized until such time as the association was liquidated. Such a result was deemed the only alternative consistent with the continued welfare of the enterprise. Enactments or by-laws providing for compensation of retiring shareholders will probably be construed to authorize payment of par value only. Since the non-shareholder commonly is entitled to participate in the assets upon distribution, payments to withdrawing shareholders in excess of par would undermine the interests of those patrons who possess no shares in the organization.[69]

By-laws and statutes providing for forfeiture upon voluntary disassociation from a cooperative have no application to unpaid or undistributed proceeds received from the sale of crops contributed by the member prior to his withdrawal.[70] Such amounts are ordinarily considered to be a debt owed to the patron and not "property or assets" of the cooperative to which forfeiture provisions apply. Here again careful distinction must be drawn between rights founded upon the association agreement and those stemming from the marketing contract.[71] The former are vitiated by a separation from the association, if statute or by-laws so provide, but the latter are subsisting rights based upon a separate and enforceable relationship.[72]

The revolving fund, an increasingly significant method of capitalization of agricultural cooperatives, presents a convenient solution to the withdrawal problem. Under the revolving fund system, reserves are accumulated through deduction of "retains" from the proceeds derived from marketing of members' crops. These retains are refunded periodically on a chronological basis. The members of longest standing are

68. 52 Cal. App. 468, 126 P.2d 467 (1942).

69. Two further incidental aspects of voluntary withdrawal are worthy of note: In California Bean Growers' Ass'n v. Rindge Land & Navigation Co., 199 Cal. 168, 248 Pac. 658 (1926), it was held that a by-law providing that failure to deliver terminated membership could only be invoked at the instance of the co-op and did not relieve the defaulting member from compliance with his agreement in succeeding seasons; a Kentucky court, in Carpenter v. Dummit, 221 Ky. 67, 297 S.W. 695 (1927), sustained the validity of a restriction on alienation of stock. The provision had a legitimate purpose, to retain control of the cooperative in friendly hands, and since the membership of the association was large it was not an undue restraint.

70. According to Bogardus v. Santa Ana Walnut Growers' Ass'n, 41 Cal. App.2d 939, 108 P.2d 52 (1940), a withdrawing member's interest in the revolving fund is in this category.

71. Hood River Orchard Co. v. Stone, 97 Ore. 158, 168, 191 Pac. 662, 666 (1920).

72. HULBERT, *op. cit. supra* note 55, at 74, 75.

repaid first with retains subtracted currently from proceeds belonging to members presently using the cooperative's facilities. The by-laws may appropriately provide that funds so withheld and credited to individual accounts will be repaid to disaffiliated members in the same manner they would have been refunded had such members continued to participate in the cooperative enterprise. Thus, the withdrawing member is entitled only to receive the balance of the proceeds of his crop less expenses, when such proceeds become available, and to be repaid his contributions to reserves when the cooperative sees fit to make like payments to nonwithdrawing members with similar tenure.[73]

Withdrawal may also be involuntary, as in the case of expulsion or ineligibility to continue as a member of the association. In *Adams v. Sanford Growers' Credit Corp.*[74] the by-laws provided that marketing privileges could be denied to a shareholder for sufficient cause and, in such an event, his equity in the organization should be adjusted as in the case of voluntary withdrawal. The by-laws pertaining to voluntary separation authorized disposition of stock only with unanimous consent of the directors. Failing to procure an acceptable buyer, the departing member could require the directors to provide for the purchase of his stock. The court frustrated an attempt by directors to effect a forfeiture through their refusal to retire the offending member's stock. A member of an association who for varied reasons becomes ineligible to continue to participate in the enterprise is entitled to enforce rights still in existence under his marketing contract[75] and also to receive the par value of his stock in the organization.[76]

A cooperative, like any other business enterprise, must display some basis of financial responsibility to induce the extension of credit upon which successful conduct of any commercial venture is predicated. The problem differs with the character of the organization, *i.e.*, whether it is an unincorporated or a stock or non-stock corporation. Moreover, the variety of approaches to the task of securing protection to creditors is limited only by the ingenuity of state legislatures and the drafters of

73. Reinert v. California Almond Growers' Exchange, 63 P.2d 1114 (1937), *subsequent opinion*, 9 Cal.2d 181, 70 P.2d 190 (1937).

74. 135 Fla. 513, 186 So. 239 (1938).

75. HULBERT, *op. cit. supra* note 55, at 75 (1942).

76. Avon Gin Co. v. Bond, 198 Miss. 197, 22 So.2d 362 (1945). See also Snyder v. Colwell Cooperative Grain Exchange, 231 Iowa 1210, 3 N.W.2d 507 (1942), in which plaintiff, a shareholder in the old corporation, was ineligible for membership in a reorganized cooperative. It was held that a fiduciary duty existed between prior holders and the managing officers seeking to purchase such ineligible shareholders' stock. Thus the officers were obligated to make full disclosure to plaintiff of all facts bearing upon the value of the redeemed stock.

articles and by-laws for farm cooperatives.[77] In keeping with the trend toward insulating the agricultural cooperative from the impact of many burdensome regulatory measures applicable to corporations generally, there may be a strong tendency to provide only a minimal margin of security to those extending credit to the cooperative. But the long run effect of such a policy may be to subvert the very goals sought to be advanced, by discouraging extension of credit.

Members of an unincorporated agricultural association assume full financial responsibility for the obligations incurred by it. Hence, members of an association organized to market a pickle crop were jointly liable not only for excess advances, but also for debts contracted by the managing trustees in connection with the marketing operation.[78] In an incorporated cooperative having capital stock, shareholders whose subscriptions are paid in full ordinarily are subjected to no further liability for the debts of the corporation in the event of insolvency.[79] However, there is no legal impediment to an agreement among all shareholders binding them to deliver to the cooperative their individual promissory notes whether for the purpose of strengthening its credit or of protecting directors from personal liability when they have found it necessary to pledge their own credit to obtain needed funds. Such agreements have been upheld against the contention that they were mere unenforceable unilateral promises wanting consideration.[80] Consideration for the promise of each shareholder is found in the execution by the others of similar agreements for their mutual benefit.[81]

The range of variety in approach to the problem of members' liability for debts of a nonstock cooperative corporation is broad; strained judicial constructions of exculpatory statutory and by-law provisions in order to protect creditors have not been infrequent.[82] In *Lockport Cooperative Dairy Ass'n, Inc. v. Buchner*,[83] plaintiff cooperative became

77. KY. REV. STAT. § 272.190(3) (1946). "No member shall be liable for the debts of the association to an amount exceeding the sum remaining unpaid on his membership fee or his subscription to the capital stock, including any unpaid balance on any promissory notes given in payment thereof."

78. Tomlin v. Petty, 244 Ky. 542, 51 S.W.2d 663 (1932).

79. IND. STAT. ANN. § 15-1613 (Burns' Repl. Vol. 1950); KY. REV. STAT. § 272.190 (1946).

80. Farmers' Coop. Union of Lyons v. Reynolds, 127 Kan. 16, 262 Pac. 108 (1928).

81. Farmers' Equity Co-op. Ass'n of Dresden v. Tice, 122 Kan. 127, 251 Pac. 421 (1926).

82. For example, the court in Lewis v. Monmouth County Farmers' Co-op. Ass'n, 105 N.J. Eq. 257, 147 Atl. 550 (Ch. 1929), found that a by-law provision expressly negating personal liability for debts of the co-op in excess of a certain amount was an ineffectual attempt to limit such responsibility.

83. 129 Misc. 73, 221 N.Y. Supp. 433 (Sup. Ct. 1925).

unable to meet its maturing obligations and the directors, pursuant to statutory authorization, levied a per capita assessment to secure funds with which to accommodate creditors pressing for payment. Defendant resisted collection on the ground that the articles of incorporation limited individual liability to one dollar. Relying on a provision of the Membership Corporations Act under which plaintiff was incorporated, which imposed liability on members for the debts of the association, the court rejected this defense and condemned the charter provision as one in derogation of the legislative purpose.[84] In another jurisdiction the statutory device developed for the protection of creditors of a non-stock corporation limits the liability of individual members to the amounts due them under their marketing contracts. When the association has satisfied all claims of its members growing out of the marketing contract for a given year, the potential liability of such members to creditors is extinguished. Until such time as the proceeds are turned over to the growers, creditors have an equitable lien upon the funds in the hands of the cooperative.[85] Another scheme adopted in a few states renders each member initially liable for his proportionate share of the cooperative's debts and obligations. In addition, the shares of defaulting members are distributed per capita among remaining members, with the qualification that no member's ultimate liability shall exceed twice his initial share of the total debt.[86]

Not infrequently cooperative charters authorize and articles or by-laws adopt a debt limitation.[87] In this event, members of a non-stock corporation are absolved from liability for obligations incurred in excess of this restriction. Legislation may impose personal responsibility on directors for such excesses, thus providing some modicum of protection to unwary creditors while limiting the risks assumed by the association's patrons.[88]

84. While the applicable statute authorized establishment of a debt limitation beyond which the cooperative could not contract obligations, the provision in question purported to fix a limitation on individual liability, even for debts within an established debt limitation, in contravention of an express provision fixing liability on members individually.

85. Bank of Aurora v. Aurora Cooperative Fruit G. & M. Ass'n, 91 S.W.2d 177 (Mo. App. 1936).

86. Mandell v. Cole, 244 N.Y. 221, 155 N.E. 106 (1926); Lewis v. Monmouth County Farmers' Coop. Ass'n, 105 N.J. Eq. 257, 147 Atl. 550 (Ch. 1929).

87. Federal Chemical Co. v. Paddock, 264 Ky. 338, 340, 94 S.W.2d 645, 647 (1936); Lockport Coop. Dairy Ass'n, Inc. v. Buchner, 129 Misc. 73, 74, 221 N.Y. Supp. 433, 434 (Sup. Ct. 1925).

88. Federal Chemical Co. v. Paddock, 264 Ky. 338, 94 S.W.2d 645 (1936). This decision also emphasizes the significance of protection of creditors by revealing that the co-op involved had no capital and conducted its business entirely on borrowed money.

A perennial difficulty not peculiar to cooperative concerns preferential treatment of certain favored creditors to the serious detriment of others, by a cooperative approaching insolvency. The dual status enjoyed by the patron-member makes this problem a perplexing one in the cooperative context. While "insiders" are commonly the recipients of the preference, such members also usually constitute the largest single group of creditors, since a large proportion of the association's business is conducted with its own proprietors.

One reason advanced for invalidating an attempted preference of shareholder-creditors is that they occupy a favorable vantage point from which to perceive the first symptoms of insolvency.[89] Under this theory a Kansas court vitiated a preference granted to ten shareholders in the form of an assignment of promissory notes which were the obligations of eight of the favored group. The court buttressed its position that shareholder-creditors cannot be favored to the exclusion of outsiders who also have extended credit to the association with the arguments that: a) the notes had originally been contributed to make up an impairment of capital and hence constituted a trust fund to which all creditors were entitled to look for the satisfaction of their claims; b) the shareholders in question not only had the advantages of the usual incidents of stock ownership, such as the right of inspection, but also were active in the management of the affairs of the cooperative.[90]

Directors of an insolvent cooperative corporation clearly cannot satisfy their claims against the corporation in preference to the demands of general creditors.[91] This result can be substantiated on the trust fund theory[92] or on the ground that the director occupies a fiduciary relationship to others interested in the assets of the organization and is forbidden to plunder its resources to satisfy personal claims when he foresees financial embarrassment.[93] However, a recent Minnesota decision has adopted a singularly narrow construction of the rule, upholding

89. Leyden v. Calhoun Cooperative Creamery Co., 223 Ala. 289, 135 So. 317 (1931).

90. Clark v. Pargeter, 142 Kan. 781, 52 P.2d 617 (1935).

91. In Darling & Co. v. Petri, 138 Kan. 666, 27 P.2d 255 (1933), plaintiff supplied fertilizer to a cooperative on a consignment basis. Defendant, a director of the cooperative, had loaned it money and taken a note in return. He surrendered his note and claim in exchange for fertilizer immediately prior to the co-op's insolvency. Recovery against defendant was sustained on the theory that he was in effect a trustee, with notice of the terms of the contract and that as against creditors of the consignee, the consignor's rights are protected.

92. Clark v. Pargeter, 142 Kan. 781, 786, 52 P.2d 617, 620 (1935).

93. Farmers' Co-op Ass'n of Bertha, Minn., v. Kotz, 222 Minn. 153, 158, 23 N.W.2d 576, 579 (1946).

a preference conferred upon a director and officer just one month after he had resigned.[94] If his knowledge of impending financial difficulties is the basis for rendering a director ineligible to receive a preference, as the Minnesota case indicates, it is difficult to understand in what manner this factor becomes insignificant upon resignation of the director on the very eve of insolvency.[95]

Numerous regulatory measures have potential application to agricultural cooperatives because of the nature of the activities they engage in and the corporate form under which they most frequently operate. Review of the courts' delineation of cooperatives' immunities from and obligations under these statutes reveals a crazy-quilt pattern indicative of an incessant conflict among major governmental policies. On the one hand, the courts are besieged with reminders of the depressed status of farming in this country before the advent of cooperation, while on the other the argument is urged that uniform achievement of a particular social objective outweighs the slight inconvenience incident upon its application to the farm cooperative. Judicial solicitude for agricultural cooperatives has resulted in their exclusion from the coverage of legislation regulating warehousemen,[96] imposing a license tax on the privilege of conducting various commercial activities,[97] prescribing standards and conditions precedent to the transportation of goods in interstate com-

94. This court recognized a split of authority on the question whether an insolvent corporation can confer a preference and took the position that it can when it has control of all its assets and such action will not prevent its continued operation. Farmers' Co-op. Ass'n of Bertha, Minn. v. Kotz, 222 Minn. 153, 23 N.W.2d 576 (1946).

95. A related problem concerns liability of a cooperative for negligent injuries arising out of its operations. It seems clear that the cooperative entity should assume the risks incident to its undertakings. This was the conclusion reached in Lichty v. Carbon County Agriculture Ass'n, 31 F. Supp. 809 (M.D. Pa. 1940). However, in Arkansas Valley Co-operative Rural Electric Co. v. Elkins, 200 Ark. 883, 141 S.W.2d 538 (1940), a cooperative electric power company successfully resisted liability on the two-fold theory that defendant was a public *quasi* corporation having no obligations not specifically provided by statute and that it was entitled to the immunity with which some states still clothe charitable corporations.

The liability of a central cooperative for torts of its inadequately capitalized local presents an interesting contrast with the rule ordinarily invoked in the parent-subsidiary context. Since, under the theory of cooperation, control moves upward from the base of the pyramid, members of the local organization presumably direct the activities of the central. Thus, the pattern of control which enables a court to disregard the corporate entity of a subsidiary corporation and impose tort liability on the parent cannot be found in the cooperative superstructure. An opinion emphasizing lack of control as a reason for its refusal to impose liability on a central for a tort of the local is Farmers' Educational and Cooperative Union of America v. Eakins, 188 Okla. 324, 108 P.2d 182 (1940).

96. Lexington Mill & Elevator Co. v. Browne, 116 Neb. 753, 219 N.W. 12 (1928).

97. Forrester v. Georgia Milk Producers' Confederation, 66 Ga. 696, 19 S.E.2d 183 (1942); Yakima Fruit Growers' Ass'n v. Henneford, 182 Wash. 437, 47 P.2d 831 (1935).

merce,[98] conferring upon creditors the right to institute involuntary bankruptcy proceedings,[99] forbidding commission merchants from purchasing on their own account,[100] imposing emergency price ceilings,[101] and defining prohibited speculative future transactions,[102] to name only a few. In addition, several courts have engrafted unusually broad constructions upon the authorized powers provisions of cooperative charters. For example, in *State v. Consumers Cooperative Ass'n*,[103] a charter provision entitling the association to furnish its members with machinery, equipment and supplies was deemed to justify its entrance into the oil refining business and ownership of oil wells and pipe lines, and, in addition, the operation of canning plants, lumber mills, printing plants, paint factories, and insurance and auditing enterprises.[104] On the other hand, decisions inimical to the cooperative movement can be found which impose upon these organizations the restrictions embodied in state license taxes,[105] legislation governing public markets,[106] the federal bankruptcy act,[107] and several others.[108]

A context in which the problem of cooperative immunity from burdensome statutory requirements is brought into sharp focus is presented by the cases defining exemptive provisions employing the termi-

98. I.C.C. v. Jamestown Farmers' Union Federated Co-op. Transp. Ass'n, 57 F. Supp. 749 (D. Minn. 1944), *aff'd*, 151 F.2d 403 (8th Cir. 1945).

99. *In re* Wisconsin Co-op. Milk Pool, 35 F. Supp. 787 (E.D. Wis. 1940), *rev'd*, 119 F.2d 999 (7th Cir. 1941).

100. Clinton Co-op. Farmers' Elevator Ass'n v. Farmers' Union G.T.A., 223 Minn. 253, 26 N.W.2d 117 (1947).

101. Bowles v. Inland Dairy Ass'n, 53 F. Supp. 210 (E.D. Wash. 1943).

102. Clark v. Murphy, 142 Kan. 426, 49 P.2d 973 (1935).

103. 163 Kan. 324, 183 P.2d 423 (1947).

104. In this connection, see Note, 36 CALIF. L. REV. 122-124 (1948).

See also American Cotton Co-operative Ass'n v. U.S. Warehouse Co., 193 Miss. 43, 7 So.2d 537 (1942), in which agents of a warehouse and a cooperative entered into a scheme to defraud their principals by negotiating warehouse receipts which should have been cancelled when the goods they represented were withdrawn. Since a statute regulating warehouse receipts imposed a nondelegable duty upon the warehouse company to cancel such receipts, the cooperative was able to evade the detriment of its agent's fraudulent activity by invoking the rule that the conduct of an agent acting adversely to his principal's interests is not imputable to the principal.

105. Rockingham Co-operative Farm Bureau, Inc. v. City of Harrisonburg, 171 Va. 339, 198 S.E. 908 (1938); Irvine Co. v. McColgan, 26 Cal.2d 160, 157 P.2d 847 (1945).

106. West Central Producers' Co-op. Ass'n v. Com'r of Agriculture, 124 W.Va. 81, 20 S.E.2d 797 (1942).

107. For a comprehensive discussion, see Comment, 10 WIS. L. REV. 516 (1935).

108. *E.g.*, in State v. Sho Me Power Co-operative, 354 Mo. 892, 191 S.W.2d 971 (1946), the court construed the word "including" in a statute prescribing powers of cooperatives as restrictive rather than all-inclusive. An electric utility business conducted by the cooperative was not a mercantile business within the purview of the statute.

HULBERT, *op. cit. supra* note 55, § 302 *et seq.* contains an exhaustive discussion of the impact of numerous regulatory statutes upon farm cooperation.

nology "agricultural labor." The lines of controversy have been sharply drawn by the appearance of diametrically opposed decisions in California and Arizona. In the former state,[109] cooperatives have been accorded the benefit of the "agricultural labor" exemption to the Unemployment Insurance Act on the theory that the association is merely an instrumentality of each individual participant. Since farm hands conducting identical activities on the farm would not be embraced within the scope of the act, the court reasoned that the performance of these functions "incidental to ordinary farming operations" by a cooperative marketing association at the central establishment was within the spirit of the exemption. To comply with the literal terms of the statute the court was forced to indulge the obvious fiction that the cooperative's activities were conducted "on the farm."[110] The Arizona court, conversely, assumed the position that employees of a marketing association engaged in grading, sorting, cleaning, and wrapping fruits in the association's packing plant were not "agricultural laborers."[111] The Arizona decision was founded upon recognition of the cooperative as a corporate entity and refusal to "pierce the veil" to impute to the member-cooperative relationship an agency or trust character.

Neither approach is to be advocated,[112] nor is either result necessarily incorrect. Rather, doctrinaire application of unmeaningful legal formulae should be supplanted by a realistic evaluation of relevant policy considerations. When there are no real indicia of legislative intent, the court is at liberty to achieve a result most consistent with the welfare of all interest groups affected by their decision. Much, of course, depends upon the severity of the burden which the act would impose upon cooperation and the prevailing economic status of agriculture and of the marketing associations themselves. Such factors may indicate the necessity of shielding cooperatives from any additional financial burden. On

109. California Employment Commission v. Butte County Rice Growers' Ass'n, 146 P.2d 908 (1944), *subsequent opinion*, 25 Cal.2d 624, 154 P.2d 892 (1944). See also Industrial Commission v. United Fruit Growers' Ass'n, 106 Colo. 223, 103 P.2d 15 (1940), in which a cooperative successfully claimed exemption from an Unemployment Compensation Act of Colorado.

110. While the court in the California Employment Commission Case was entirely correct in rejecting the separate entity theory as a basis for application of the statute, the agency or instrumentality argument it adopted is equally questionable. California Employment Commission v. Butte County Rice Growers' Ass'n, 146 P.2d 908 (1944), *subsequent opinion*, 25 Cal.2d 624, 154 P.2d 892 (1944).

111. Employment Security Commission v. Arizona Citrus Growers, 61 Ariz. 96, 144 P.2d 682 (1944).

112. A similarly mechanical means of reaching a result was adopted in North Whittier Heights Citrus Ass'n v. N.L.R.B., 109 F.2d 76 (9th Cir. 1940). The court contrasted the means of accomplishing identical functions on the farm and in the co-op warehouse. On the basis of apparent differences, they concluded that the latter was not entitled to benefit from an exemption intended to cover agricultural labor.

the other hand, a policy strongly embedded in modern legal thinking, and embodied in the legislative enactments under discussion, is that a commercial entity should assume a portion of the risk of injury and unemployment incident to its business. Another circumstance which may be significant is the fact that administrative aspects of unemployment compensation render it particularly inadaptable to the small business such as the average farm unit. The agricultural labor exemption may stem from the latter consideration rather than from any legislative desire to exempt the farmer from the responsibilities growing out of the conduct of his business.

In the past, legislative and judicial attitudes have been extremely favorable to the farm cooperative, perhaps in response to the serious need to inject new vigor into our farm economy. With the advent of improved agricultural conditions and enhanced farm prosperity, some courts and legislatures have adopted a more critical approach to continuing cooperative demands for preferential treatment. Exact equilibrium among competing economic and social goals is, of course, unattainable. However, a continuing attitude of critical scrutiny of the claims of all organized groups is the only satisfactory means of adjusting governmental policy to the demands of changing economic conditions.