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Know your COOPERATIVE ASSOCIATION

W. H. Dankers

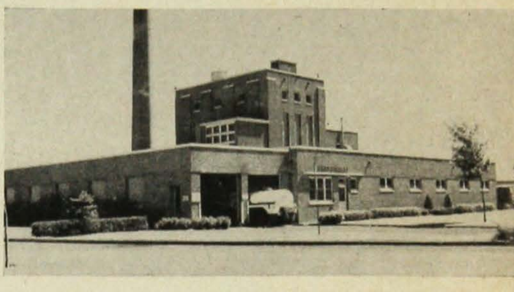
LET'S STUDY AND LEARN • THINK IT THROUGH AND ANALYZE • TALK IT OVER AND EXCHANGE IDEAS • MAKE INTELLIGENT DECISIONS

UNIVERSITY OF MINNESOTA
Agricultural Extension Service
U.S. DEPARTMENT OF AGRICULTURE

How A Cooperative Association Operates

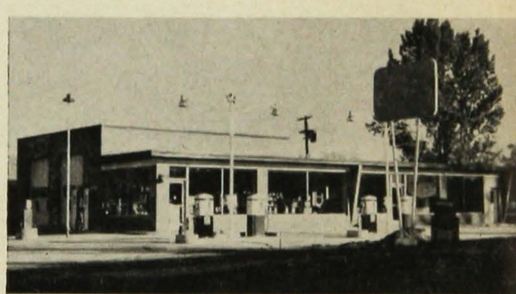
A cooperative is a *voluntary association,* owned, controlled, and operated by patrons. Generally, the members (common stockholders) are also the patrons. Therefore, they are correctly referred to as member-patrons. A cooperative business association is subject to the same economic forces that affect other businesses.

A **marketing** association aims to obtain the largest return for commodities produced by its patrons. The association takes the gross proceeds, deducts all operating expenses—including depreciation—and makes a cash advance to the patrons. Any balance remaining at the end of a fiscal year is credited to patrons on the basis of volume of products sold (patronage) through the association.



A cooperative marketing association.

A **purchasing** or **service** association aims to obtain the largest amount of high-quality goods or services for dollars spent by its patrons. The association collects money from its patrons for goods or services furnished them and pays the cost of the goods or services and all operating expenses. Any balance remaining at the end of a fiscal year (savings) is then credited to patrons on the basis of volume of purchases made (patronage) through the association.



A cooperative purchasing association.

Capital and operating funds in a cooperative association are partially built up through sale of capital stock to members. However, additional funds may be built up in a marketing association by retaining a part of the net balance (patron's credits), and in a purchasing or service association by retaining a part of the cash overpayments made by patrons for the goods and services received (patron's credits).

Capital funds represented by patrons' credits are returned to the patrons in cash when, in the judgment of the directors, operating capital requirements permit it, or when the association is dissolved.

A cooperative service association.

Know Your Cooperative Association

W. H. Dankers*

This bulletin is written to answer questions about cooperative associations. It offers practical suggestions for directors and management. These suggestions will help to understand and analyze the business operations and financial statements of a cooperative association. Directors and managers should pass the information on to association members.

Just because an association is a cooperative does not guarantee its success. Members are seldom so tied to their association that they will continue to patronize it when it fails to be competitive and is unable to meet competitive costs and prices. Therefore, cooperatives must stand on their own merits. They must be operated efficiently in order to serve the best interests of their patrons. Efficiency in plant operation, marketing, purchasing, and performing of service can be increased through a thorough study of the business and through an understanding of new developments and techniques.

Many cooperatives have failed because of inefficient plant operation, marketing, purchasing, and performing of service. Some cooperative associations can trace their failure to a lack of membership understanding and loyalty because their member-patrons were not properly informed. A continuous program of member-patron information and education is essential in a cooperative association. Such education should be based upon sound research and factual material that affects the group directly.

Articles of Incorporation and Bylaws

Cooperative members, directors, and employees should be well informed about the contents of their association's articles of incorporation and bylaws. These are the guidelines and rules that generally govern all meetings and activities in the association. They should, therefore, be carefully **studied** by directors, member-patrons, and employees.

The articles of incorporation are a contract between a cooperative association and the state in which the association is incorporated. They serve as a guide to what the association, as a legal entity, can and cannot do for its members and patrons. Changes in the articles of incorporation cannot legally be made by the manager, directors, or members unless proper procedure is followed for amending them.

The bylaws supplement the articles of incorporation, and cover organizational and operating procedures of the association in greater detail. Bylaws can be changed only by amendment and cannot be suspended or disregarded at any meeting of the association.

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Distribute Statements and Reports

Printed financial statements, including a balance sheet and an operating statement, should be distributed to member-patrons at least once each year. Such reports are valuable only when they are clear and understandable. They are even more valuable when properly explained. Charts and slides frequently help to show and more clearly explain changes in such important items as volume of business, operating costs, amount of working capital, and changes in member and patron equities over a period of time.

Periodical letters and special reports are helpful and important in keeping member-patrons informed. Such reports may relate to progress of the association, special activities, seasonal price changes, effects of quality on price, need for attention to certain production practices, outlook information, and changes in the policies of the board of directors.

The annual meeting is one time in a year when all the members are called together. It should be made as effective as possible. Annual meetings offer good opportunity for member-patron education. A small attendance at the annual meetings is, in some cases, indication that previous meetings have not been sufficiently interesting or worthwhile.

Special meetings of the members should be called if they are necessary or desirable.

Arrangements for the Meetings

Good meetings don't just happen; they must be planned in advance. These details are important:

1. **Make plans and arrangements before the meetings.**
   - a. Send interesting notices. Call attention to various features of the program and each member's part, opportunity, and responsibility in it.
   - b. Select a meeting place neither too large or too small. Arrange it so that attendants will be comfortable. Provide adequate light, proper temperature, and chairs for all. For a fairly large meeting, provide adequate loud-speaking equipment.

Arrange for lunch to be served quickly at the meeting.

   - c. Arrange for lunch to be served quickly—people get restless if they have to wait.
   - d. Have blanks for balloting prepared. This saves time and avoids confusion.

2. **The chairman should not try to be a dictator at the annual meeting. He is very important as an engineer and as an expediter. He should:**
   - a. Have the entire program outlined so that he can keep things moving.
   - b. Bring the group close together at the front so that speakers can be heard by everyone.
   - c. Insist that all who speak must stand, face the group, and speak clearly.
   - d. Encourage all members to participate in the business, but insist that discussion be limited to business under consideration.
   - e. Repeat all motions and announce the results of each vote, so

everyone knows what takes place.

3. **Make the annual meeting program both educational and interesting.**

   a Distribute printed copies of the annual report and explain it thoroughly to the members.

   b. Present both the association's progress and problems to the members. This should include reports from the manager and from directors.

   c. Allot time for discussion of a marketing, purchasing, or servicing subject about which the members otherwise do not get information. Such subjects include variations in efficiency between cooperative associations, financing, legal and organizational requirements, and industry trends.

   d. Plan a wholesome entertainment program.

4. **Keep accurate minutes of annual and special membership meetings. Minutes have historical value and can be used in settling any possible disputes. Accurate minutes will show:**

   a. That proper notice or call for the meeting was given.

   b. That a member registration (roll call) was taken.

   c. That a quorum was present.

   d. What action was taken.

   e. The authority by which action was, or is, to be taken.

A successful annual meeting starts with the business session in the forenoon. Lunch is served at noon, supplemented by a brief entertainment program (preferably music). The meeting continues with an educational program in the afternoon. Such a meeting has proven more successful than meetings in which everything is crowded into a brief afternoon or evening program. A meeting started in the forenoon provides more time for consideration of business items and for the information and educational phase of the program, and still allows members to return home early enough in the afternoon.

Don't Let the Program Drag

The program should keep moving from the time the meeting is called to order until adjournment. Outside speakers are a part of many annual meetings. Carefully selected speakers can present information which members would not otherwise receive. However, speakers at annual meetings should be of the association's own choosing rather than speakers who want to get on the program in their own interest and who divert attention from the real interest and problems of the cooperative association. The county agricultural agent can usually suggest appropriate speakers.

Select Suitable Speaker Topics

Speaker topics for the annual meetings should pertain to specific problems of the particular cooperative association. Changes and developments are so numerous that they can be only partially covered at annual meetings, and should be given first choice whenever possible. Of course, the topic will have to fit the speaker's background and experience.

Farm production problems and national and world economic and political problems are frequently timely and of considerable interest, but should be considered secondary to the discussion of specific marketing, purchasing, and service problems. A few topics that have proved of special interest at annual meetings of cooperative associations are:

1. Fundamental principles of cooperative associations.
2. Organizational and legal requirements of cooperative associations.
3. Responsibilities of the members, directors, and management.
4. Sound financing of a cooperative association.

Directors should meet often to discuss association progress and problems.

5. Procedures for improving the operating efficiency of cooperatives. How does your association compare with similar associations?
6. Analyzing statements and reports of cooperative associations.
7. Taxation and legislation.
8. Industry trends and special marketing, purchasing, and service problems.

Most cooperative associations have sufficient need for *regular* monthly directors' meetings. Arrangements for these meetings should be indicated in the bylaws. The bylaws should also provide that special directors' meetings may be called by the president, or demanded by a majority of the directors when they are deemed necessary and the president does not call them. *Special* directors' meetings are required for discussing and handling special and emergency matters of the association.

Directors' meetings are effective only when directors systematically "follow through" in discussing the association's problems and the work to be done. When a member accepts a directorship in his cooperative association he agrees, in effect, to accept responsibility for association activities. He should make every effort to attend all directors' meetings, and should arrive on time so as not to waste the time of the other directors. All directors should then give **immediate** attention to the association business.

Regular directors' meetings should be arranged so that the date will definitely be reserved and the board members will avoid conflict with other activities. Most associations arrange for directors' meetings within a specified short period of time. Each director must then be notified of the exact date as specified in the bylaws.

Although most boards of directors ask the manager of their cooperative association to meet with them, directors should make it clear that this is not a regular requirement. Discussion of management and director relationships, management problems, and manager's salary may require sessions at which attendance should be limited to the directors of the association.

Some directors find it advisable to invite their accountants or bookkeepers to attend some directors' meetings. In this way directors can obtain more detailed information about the association's affairs, and the office staff also develops greater interest and enthusiasm in the association.

A monthly operating statement is a must, and a monthly balance sheet also gives the directors necessary information. Directors have no basis for discussing the association's problems and making decisions unless they have necessary records and reports of the association before them. *Negligence* on the part of the directors could make them personally liable.

Records Are Important

Specific information about the business must be at hand if a cooperative association is to be operated efficiently. Such information can be obtained only from accurate records that are properly summarized and analyzed.

The primary purpose of accounting is to obtain financial information and to report it in an understandable manner; the most practical and workable form of accounts will vary for different kinds of businesses. A systematic record of all financial transactions must be kept. Physical volume records also are necessary. Summarized statements should be prepared periodically from detailed daily records; management may base decisions for future operations on these statements. This information should also be reported to the directors. *Operating costs data should be available for each department of the business.*

To obtain necessary and helpful data with minimum effort, certain office equipment, such as an electric calculator and an electric adding machine, should be available. Any association that does not have this equipment is wasting the time of its manager, secretary, and office employees who prepare the necessary records. More office equipment may be desirable, depending on the size and type of business.

The *balance sheet* (financial statement) and the *operating statement* (statement of income and expense) are the most frequently used summary statements. These statements should be prepared both at the end of each month and at the end of each fiscal year. The balance sheet provides a picture of the financial status of the business at a particular time (December 31, for example), while the operating statement provides a picture of income and expense, and operations through a given period of time, such as a month or a year.

The Balance Sheet

A properly prepared balance sheet shows the relationship between assets and liabilities. The difference between assets and liabilities is the members' and patrons' share in the association. The balance sheet also shows the association's financial condition and its debt-paying ability (solvency).

A balance sheet is more easily understood if you think of it as the statement of a business (the cooperative association) and not the statement of an individual owner of that business. To an individual member a share of stock is an asset, but to the association itself the stock is a corporate obligation. Other obligations are the net margins that have accumulated to patrons' credit and are recorded as allocated equities (capital contributions).

The balance sheet has three distinct sections: (1) assets ("what we have"), (2) liabilities ("what we owe"), and (3) member and patron equities ("what we own"). The term "balance sheet" implies that there is a blance. Assets are always equal to the total of liabilities and member and patron equities.

What Are Assets?

Assets are the property and resources of an association. Listing assets is the same as taking an inventory. All assets which are cash or which could be converted into cash during normal operations of a year's business are **current assets.**

Accounts receivable are current assets. They are frequently overrated on the balance sheet when collectibility of some accounts is questionable and the association has failed to make proper allowance for such accounts. Ordinarily, accounts receivable which are more than 1 year old are questionable. Associations doing considerable credit business should watch this item carefully and should have a firm and virgorous credit policy. Losses on bad accounts are operating costs and should be shown as expenses in the operating statement.

Fixed assets are such items as land and buildings, machinery and equipment, and furniture and fixtures.

Investment assets include investments in other cooperatives, government bonds, and other investments.

Prepaid expenses represent expenses which have been paid in advance. A part of the material or service for which payment has been made has not yet been utilized, and to that extent it is still an asset. Prepaid insurance is a good example.

Although not a cash expense, depreciation of buildings and equipment is part of the operating cost of an association. Therefore, the allowance (valuation reserves) for depreciation of buildings and equipment (and also for bad debts) are direct deductions from such assets and should be shown as such in the assets section of the balance sheet.

What Are Liabilities?

Liabilities represent debts or obligations of the association. Most common among the liabilities are accounts payable, notes payable, and mortages.

Liabilities are either current or long term, depending on when the obligation must be met. Ordinarily, any liabilities which will mature during a year's operation are considered current.

Cooperative associations frequently omit such liabilities as accrued taxes and accrued interest from the balance sheet. Accrued liabilities represent that part of an expense not yet paid but actually chargeable to the current period of operation. For example, real estate taxes and interest which are paid only twice each year should be proportionally charged to each month's operation. These accruals are definite liabilities and should be shown as such on the balance sheet to present a true picture of the association's financial condition at a given time.

What Are Member and Patron Equities?

Member and patron equity items are paid-in membership money (capital stock and stock credits), and patrons' capital contributions accumulated from past and current net margins which have been allocated to patrons (parton's equities) but retained in the business. Member and patron equities are actually the excess of assets over liabilities. These equities represent the claims that members and patrons have on the assocition's assets.

A cooperative association that is properly organized and operated has no corporate income. Members can receive only a limited market rate of dividends on money which they have invested in the form of capital stock. The balance of any net margins then belongs to patrons of the association. If money that belongs to the patrons (member or nonmember) is retained in the association it is then listed as patron's capital credits (patron's equities) in the balance sheets.

Patron's capital credits (patron's equities) should always be allocated to patrons on the basis of volume of business done with the association, because they have been retained in that way. Association records for each fiscal year should be kept in such a manner that the amount of each patron's capital credit can be ascertained. The amount of each patron's capital credit should be reported to him within a reasonable time after the end of each fiscal year.

Balance Sheet

December 31, 19__

________________ Cooperative Association

ASSETS (What the association has)

Current Assets:

Cash on hand			$ 408.20	
Cash in bank			5,250.00	
Accounts receivable—patrons	$ 1,466.10			
Accounts receivable—general	20,376.92	$ 21,843.02		
(Less: allowance for bad accounts)		856.85	20,986.17	
Notes receivable			3,468.53	
Inventory—merchandise			7,651.30	
Inventory—supplies			7,303.85	
Prepaid expense			1,193.72	
Total current assets				**$ 46,261.77**

Investments:

Stock and equities in other cooperatives				**20,500.00**

Fixed Assets:

Land			2,516.68	
Buildings		108,343.32		
Less: allowance for depreciation		31,941.37	76,401.95	
Machinery and equipment		47,451.12		
Less: allowance for depreciation		10,295.62	37,155.50	
Office equipment		3,116.22		
Less: allowance for depreciation		298.65	2,817.57	
Trucks and delivery equipment		2,900.00		
Less: allowance for depreciation		1,250.00	1,650.00	
Total fixed assets				**$120,541.70**
Total, all assets				**187,303.47**

LIABILITIES (What the association owes)

Current Liabilities:

Short-term notes payable		$ 1,497.93		
Accounts payable—patrons		33,884.70		
Accounts payable—general		1,254.62		
Accrued taxes and interest payable		1,413.00		
Total current liabilities				**$ 38,050.25**

Long-term Liabilities:

Mortagage or long-term notes payable				**$ 48,875.00**
Total Liabilities				**86,925.25**

MEMBER AND PATRON EQUITIES

(What the association owns—the members' and patrons' share)

Capital stock—authorized		37,500.00		
Less: unissued stock		10,250.00		
Capital stock outstanding			$27,250.00	
Capital stock credits			1,025.50	
Patrons equity credits—prior years		57,597.57		
Patrons equity credits—curent year		14,505.15	72,102.72	
Total member and patron equities				**$100,378.22**
Total liabilities and member and patron equities				**187,303.47**

Financial Ratios

Current Ratio

To stay in business an association must pay its debts as they come due. It must also have enough cash on hand to meet current operating expenses. One measure of an association's ability to do this is the ratio of current assets to current liabilities. The desirable ratio depends on the type of association and its method of operation.

Generally, an association should aim to have $2 of current assets for each $1 of current liabilities, or a ratio of 2 to 1.

The balance sheet on page 9 shows $1.22 in current assets for each $1 of current liabilities, or a ratio of about 1.2 to 1. If the ratio is less than 2 to 1 an association may have difficulty meeting its current obligations and retaining sufficient operating capital to take advantage of cash discounts and to make money-saving quantity purchases.

If the ratio is less than 1 to 1, the association may have to delay payments on some current obligations. Such a condition may mean lost discounts, additional interest charges, and difficulty in borrowing money at a reasonable rate.

Member and Patron Equity-Debt Ratio

The ratio of member and patron equities to total liabilities is an important business indicator.

Total member and patron equities should equal or exceed total liabilities; this indicates more owner than creditor capital in the business.

The balance sheet on page 9 indicates $1.15 of member and patron equities (owner capital) for each $1 of creditor or borrowed capital. This is a fairly desirable situation, but should be improved. Capital loans should be held to a reasonably low level, because fixed interest charges and debt payments can sometimes require cash outlays to a point where it is difficult to meet competition. It is desirable to finance all fixed assets from member and patron capital. This is generally accomplished by selling stock to patrons or retaining more of the net operating margins in the business.

Intensive, Efficient Use of Fixed Assets

A third ratio of importance for consideration by management, directors, and members of cooperative associations is the ratio of the total units of business (such as pounds, tons, or dollars) to the investment in fixed assets. This ratio is calculated by dividing the total units of the business by the total number of dollars of fixed assets. The result shows the number of units handled per dollar invested in fixed assets.

It is necessary to handle as many units as possible per dollar invested. The more units handled per dollar of fixed assets the lower the per unit overhead cost, and the more efficient the cooperative association is in serving its member-patrons.

All of the financial ratios referred to are more helpful to directors and managers of an association when compared with ratios of other associations with a similar business and of similar size. Ratios favorable in comparison with those of other associations give some assurance of the efficiency and effectiveness of the business.

Reserves

Allowance for Depreciation

(Valuation Reserve)

Buildings and equipment wear out with time and use. New buildings and equipment must at some time replace those used in current operations. "Wear and tear" are definite operating costs which should be charged to the current year's business.

Funds obtained from the allowance for depreciation may be applied on mortgage and note payments in associations where such obligations exist. In other associations these funds are applied to expansion of the business. When the funds are not used for these purposes they help to increase the amount of cash on hand or in the bank. Such funds are then available later when buildings and equipment are worn out, when it is desirable to improve them, or when it is desirable to replace them with newer and more efficient facilities.

The depreciation rate to be used for buildings and equipment varies with different kinds of facilities. Generally the life of buildings and equipment can be estimated quite accurately and a rate of depreciation can be calculated. For example, if an association has a new piece of equipment which is expected to last 10 years, it is logical to include 10 percent of the original cost in each year's operating costs. If the estimated life of such equipment is not correct the depreciation rate must be adjusted at the time such error becomes apparent.

Sometimes it is also necessary to use other methods of calculating depreciation when a certain percentage of the original cost might be too low. For example the cost of replacement equipment is sometimes much higher than the cost of original and the earlier purchased equipment.

The balance sheet should show the **allowance for depreciation** as a deduction from the original value of the property (fixed assets). Allowances for depreciation are set up to show the proportion of the original value that has been used and to indicate the present net value of fixed assets.

The amount of annual allowance for depreciation should be included as an item of expense in the *operating statement*. If no depreciation charge is made or the charge is too small, operating costs are understated. As a result, net margins will be overstated. An inflated patrons' equity account—which is incorrect and undesirable—will then be recorded on the books of the association.

Capital Equities

(Owner and Patron Reserves)

Capital equities represent member (owner) and patron claims on the assets. Capital equities are increased by retaining the net margin funds in the business.

Funds from capital equity reserves are needed and used: (1) to provide for and meet obligations such as the payment of a mortgage or note, (2) for increasing the operating capital of the association, (3) as insurance against possible future losses, or (4) for expansion of the business in the form of either fixed or current assets.

There is no specific relationship between the amount of total equities and cash on hand. For these reasons, a cooperative association may have a large total equity with only a small item of cash.

A cooperative association can have sufficient capital equities (reserve funds) only when net margins are sufficiently large. Some cooperative marketing associations tend to pay too much cash for products marketed. Some purchasing or service cooperatives tend to charge too little for products purchased. As a result, net margins are small and capital equities remain far too limited.

Many cooperative associations have a substantial proportion of their capital equities listed as **patrons' equity credits—prior years,** and **patrons' equity credits—current year.** When capital equities are so recorded it indicates that they have been allocated and credited to patrons from whom they were retained on the basis of each patron's volume of business with the association.

Such credits belong to the patrons, as their capital investment in their cooperative association, in proportion to service they have received.

Allocation of net margins to patrons on the basis of volume of business done with the association is also an absolute requirement if a cooperative association is to obtain and retain a proper income tax status.

Stock Credits

Frequently the item **capital stock credits** appears in the member and patron equities section of the balance sheet. So that all patrons may become members (stockholders) and the voting control of the association may be kept in the hands of those who use it, many associations have a provision for applying credits of patrons who are not already stockholders toward the purchase of a share of stock. Such credits are listed as stock credits, they accumulate until they reach an amount equal to the purchase price of a share of stock. A certificate of stock is then issued, usually at the end of the fiscal year.

Revolving Capital

The most effective way of financing cooperatives is to have a substantial part of the funds supplied from **patron's capital credits.** These are accumulated net margins allocated on the basis of patronage (volume of business done by individual patrons) and credited to patrons (patron's equities) as their capital contribution and investment in their cooperative association. However, this method of financing is much more effective and favorable if funds in the patron's capital credits are handled on a revolving capital basis.

Provisions for a revolving plan are included in the articles of incorporation and bylaws of many cooperatives. If parton's capital credits are revolved with the requirement that the oldest patron's equity credits are paid in cash, the more current patrons furnish a larger share of the funds and have a larger investment in their cooperative.

Sufficient net margins at the end of each fiscal year are necessary to have sufficient funds for paying older patron's equity reserves (patrons' credits) in cash. Thereby patrons currently operating through their cooperative association are replacing funds supplied over a period of time by patrons of earlier years.

In many cooperative associations, more emphasis should be placed on having an adequate net margin at the end of each fiscal year so that they can operate on a logical revolving fund basis. This involves the need for keeping patrons informed that the total price received in a cooperative marketing association is the cash advance (cash price) plus the credit in the net margin, and that the actual net price paid by patrons in a cooperative purchasing and service association is less than the cash price they paid, to the extent of the credit (refund) in the net margin.

The Operating Statement

The operating statement is a statement of income and expense. It provides information about the operations during a given period of time—1 year, for example. It also includes information on how the net margin (balance due patrons) is determined.

A *simplified operating statement form* is given on page 14. Most items included are self-explanatory. When preparing an operating statement, it is necessary to check carefully that all expense items are included. **The amount allowed for depreciation of buildings and equipment should be included.** If any expense items are omitted the net margin is overstated.

The operating statement prepared for stockholders and patrons is often too brief and too general and provides little information about actual operations of the association. Good accountants and auditors will properly classify various expense items, such as actual operating costs and general administrative costs. This makes it possible to compare each type of expense with figures from statements of other cooperatives.

Detailed Analysis Necessary

The operating statement shown on page 14 is merely an illustration. An operating statement will vary with the type of association for which it is prepared, such as marketing, purchasing, or service associations. It will also vary with the type of business for which it is prepared, such as creameries, grain elevators, and oil associations. In this sample statement the gross margin is on the product marketed. In creameries, on the other hand, items (1) and (2) in the operating statement would be reversed so that the gross margin would be on the product manufactured.

Helpful Comparisons

To determine the success of an association, one must consider both balance sheets and operating statements. For measures of business efficiency it is necessary to obtain further information on cost per dollar of sales, cost per unit of product manufactured, changes in gross and net margins, and other cost items. This information can be obtained from the balance sheet and the operating statements through a few simple calculations. Such calculations should be made for a period of years to determine changes in an association's efficiency of operation and financial structure. Such measures of efficiency also have much value for comparison with other similar associations.

Best Measures of Success

Net margins at the end of a year are a good measure of a cooperative association's efficiency and effectiveness. However, the most effective measures are: (1) cost per unit of handling and processing, (2) prices received for products marketed and the net price received by patrons in a marketing association, and (3) prices paid for goods and service bought and prices paid by partons in a purchasing and service association. Changes in volume of products handled are significant indicators of progress. These changes usually affect the per unit cost of handling and the resulting price paid to patrons in a marketing association, or savings made for patrons in a purchasing or service association.

Operating Statement

____________ Cooperative Marketing Association

January 1, 19___, to December 31, 19___

Returns from Products Handled			**$480,275.69**
Cash advance to patrons	$412,534.20		
(1) Inventory, beginning of year	10,453.47	$422,987.67	
Less (2) inventory, end of year		6,974.20	416,013.47
Gross margin			**64,262.22**
Operating Expenses:			
Labor and wages		22,800.00	
General supplies		5,321.40	
Fuel		3,867.07	
Light and power		3,311.40	
General repairs		1,390.23	
Other plant expenses		713.19	
Depreciation: buildings	833.57		
Depreciation: machinery and equipment	2,245.13		
Depreciation: delivery equipment	725.00	3,803.70	41,206.99
General and Administrative Expenses:			
Office salaries		1,850.00	
Directors' fees		1,185.00	
Payroll taxes		928.00	
Local taxes		1,527.30	
Insurance		684.65	
Office supplies		723.00	
Advertising and printing		504.60	
Telephone and telegraph		123.20	
Auditing		352.65	
Annual meeting expense		359.05	
Depreciation: office equipment		61.62	
Bank service charges		51.50	
Miscellaneous items		199.50	8,550.07
Total Expenses			**$ 49,757.06**
Balance Due Patrons-Net Margin			**$ 14,505.16**

A combined income and expense statement is not sufficient by itself. An operating statement of income and expense should be prepared for each major department. From such statements the per unit operating cost for each enterprise can be determined. Per unit costs are significant in indicating the efficiency of a business. Inefficiency and small "leaks" in some departments, if not discovered at an early stage, may soon drain off all savings from efficient operation in other departments and cause real difficulty to the association.

Audits Are A Must

Audits, by competent professional accountants, should be made **at least once each year** in all cooperative associations. Audits help avoid errors in accounts and provide a good basis for financial analysis. An auditor who is familiar with the particular line of business and well versed in cooperative association organization and operating procedures, can also give much valuable assistance (1) in setting up a satisfactory accounting system, (2) in explanation of income tax record requirements and reports, (3) in suggesting desirable financial and management policies, and (4) in more efficient methods of operation.

A thorough audit, explained and openly and frankly discussed before all members at the annual meeting, is the best means of creating a sense of security and of promoting members' confidence and goodwill. In any discussion there is no substitute for accounting data as a source of accurate and reliable information.

The cost of an audit depends largely on the condition of records and on the type of audit made. The cost is less if audits are made regularly and if the association follows the auditor's suggestions for improving accounting methods than if audits are irregular and if records are poorly kept.

Special Considerations

Responsibilities of Directors

To elect well qualified directors is a major responsibility of cooperative members. A well qualified director will:

1. Place the interest of the association above his own personal interest and represent the association in its entirety, and not just the member-patrons from his own community.

2. Strive to keep general and overall control with a well informed membership. He must not let his cooperative become just a directors' or managers' association.

3. Give careful and continuous attention to the business affairs of the association and strive for continued and increased efficiency.

4. Do careful and independent thinking and then express himself, but remain an openminded teamworker who realizes that views of individual directors cannot always prevail.

5. Give necessary time to directors' meetings and to other deliberations, and apply good reason and common sense to all problems.

Responsibilities of Management

A major responsibility of cooperative directors is to arrange for good management and employ a well qualified general manager. A well qualified manager will:

1. Study the association's business and problems and continuously strive for up-to-date efficient and effective methods and procedures.

2. Keep directors informed about association business, operating affairs, and needs as an aid in improving the policies of the association; then accept and carry out business and management policies laid down by the board of directors.

3. Give directors, members, and patrons complete and accurate accounting of the association's operating affairs and financial condition as a means of keeping them well informed and interested.

4. Be courteous and tactful with patrons, members, directors, employees, and others dealing with the association, but grant no special privileges or favors.

5. Assume responsibility in community affairs, in the interest of good citizenship and to acquaint the community with his association's program and value.

How Income Taxation Applies to Cooperative Associations

All cooperative associations pay real estate, personal property, excise, and all other regular taxes.

As the term implies, an income tax applies only where there is income. Cooperative associations that carry on their operations at cost have no corporate income of their own to which corporate income tax can be applied.

Cooperative marketing associations that distribute any financial balances remaining at the end of the year to their patrons, in cash or credits, in proportion to the amount of business handled per patron are, in effect, allocating final payments for goods delivered. Such amounts are income to the patrons; therefore there is no corporate income to the association.

Similarly, cooperative purchasing and service associations that distribute balances at the end of the year to their patrons, in cash or credits in proportion to the amount of business handled per patron, are refunding the overpayments. Such refunds represent savings to patrons; therefore there is no corporate income to the association.

The principle applies to all cooperative associations. It recognizes the basic fact that net margins handled in the manner indicated do not constitute corporate income to the association. Any business association that follows this principle of operation—even though it is not called a cooperative association—would be accorded similar treatment. On the other hand, if a cooperative association does not allocate net margins on the basis of patronage, the undistributed amount is subject to corporate income tax.

Proper handling of net margins (net balances due patrons) in line with income tax requirements is a complex matter, and is in a rather continuous state of change. It is the result of changes in tax laws and regulations, both Federal and state, and through interpretations of these statutes and resulting regulations by the courts. Therefore, it is essential that directors of cooperative associations keep fully informed and up-to-date about tax matters, and seek the advice of competent professional advisors at frequent intervals.

Does Your Cooperative Measure Up?

A cooperative association that is properly located, has sufficient volume, keeps accurate and complete records, and has sound management and well informed directors, is in a position to serve its member-patrons efficiently and effectively. However, it is important to keep members well informed of the progress made and of obstacles to more rapid progress. Directors must carry out this responsibility; it can be accomplished with the help of accurate, complete records and thorough audits. However, records are of value only insofar as the management and directors understand them and make use of them in improving the business of the association.

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