

COOPERATIVE HANDBOOK

This handbook has been prepared to help farmers become better acquainted with the cooperative way of doing business—how a cooperative can be organized and some of the ways to make it work. The question and answer format has been followed so as to break the subject down into small pieces that can be easily handled.

In 1921 when the first national year for the cooperative movement was observed, the following declaration of policy was made:

"In order to promote more and encourage the intelligently and wisely the production and distribution of goods and services, the cooperative movement should be encouraged and supported by the government and the people."

Farmers' **COOPERATIVE HANDBOOK**

Since 1911 we have seen the growth of the cooperative movement in this country. It has become a part of the life of the people and is now being carried on in many different forms.

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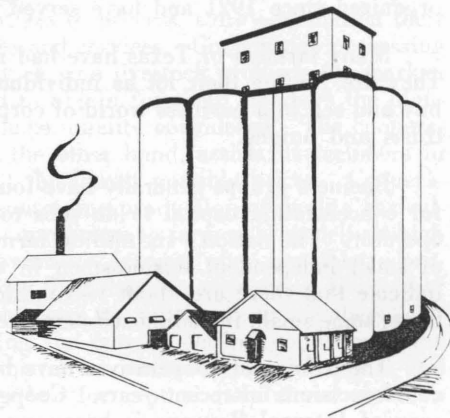
Issued by
The Agricultural Extension Service
The Texas A. & M. College System
The United States Department of Agriculture
G. G. Gibson, Director, College Station, Texas

FARMERS' COOPERATIVE HANDBOOK

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Issued by
THE AGRICULTURAL EXTENSION SERVICE
The Texas A. & M. College System and
The United States Department of Agriculture
G. G. Gibson, Director, College Station, Texas

FOREWORD

This handbook has been prepared to help farmers become better acquainted with the cooperative way of doing business—how a cooperative can be organized and some of the ways to make it work. The question and answer pattern has been followed so as to break the subject down into small pieces that can be easily handled.

In 1921 when the Texas Legislature passed the cooperative marketing act it made the following declaration of policy:

“In order to promote, foster and encourage the intelligent and orderly marketing of agricultural products through cooperation and to eliminate speculation and waste; and to make the distribution of agricultural products as direct as can be efficiently done between producer and consumer; and to stabilize the marketing problems of agricultural products, this law is passed.”

Several farmers' cooperatives in the state had been in existence ten or more years when this law was enacted and have continued in successful operation ever since. Hundreds of other cooperatives have been organized since 1921 and have served their members well.

Many farmers of Texas have had no experience with cooperatives. They are finding their lot as individuals increasingly difficult as they buy and sell in a business world of corporations, chainstores, combines, trusts and unions.

Business groups generally have found the corporation a useful tool for concentrating capital to do jobs too big for the small investor or operator. The nation's six million farmers are by far the largest group of small independent businessmen in the country. Business statistics indicate that there are about two million commercial businesses, some large, some small, including self-employed.

The affairs of cooperatives have been the subject of a number of court decisions in recent years. Cooperatives are finding that the Bureau of Internal Revenue is becoming more exacting before granting exemptions from federal income taxes. The language used in organization papers is important and the best counsel available should be used.

There are many questions which have not been included in this bulletin. The Extension Service invites any group of farmers to submit specific questions about the organization and operation of their own cooperative.

Farmers' COOPERATIVE HANDBOOK

By

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Texas A. & M. College System

QUESTIONS AND ANSWERS

1. Q. WHAT IS A FARMERS' COOPERATIVE?

A. It is an organization of agricultural producers chartered to transact collectively business pertaining to agricultural products, supplies or services. The Texas Cooperative Marketing Act gives such associations legal status and defines their purposes and powers. (Copies of this Act may be obtained from the State Commissioner of Agriculture, Austin, Texas, or from the Extension Service, College Station, Texas.)

2. Q. WHAT ARE SOME OF THE ADVANTAGES FARMERS HAVE FOUND FROM COOPERATIVE ACTION?

A. Farmers use cooperatives to process, store and market their produce and to purchase supplies and services. Cooperative processing plants prepare their crops, livestock, and livestock products for market. Marketing associations are used to obtain for their members the highest possible price for their products, quality considered. The cooperative purchasing association, on the other hand, assists its members in obtaining their farm supplies at the lowest possible prices. Cooperatives have the opportunity of encouraging production of quality agricultural products by returning premium prices to farmers who deliver high quality products. Through cooperatives, farmers often are able to provide themselves with better service than they were receiving from other agencies. Successful cooperatives save money for their members, giving service at cost. By reducing the cost of getting goods from the producer to the consumer, cooperatives encourage consumption and expand markets. Working together for mutual helpfulness makes a better citizenship.

3. Q. WHO MAY ORGANIZE A COOPERATIVE UNDER THE TEXAS COOPERATIVE MARKETING ACT?

A. A cooperative marketing or purchasing association may be formed by five or more persons engaged in the production of agricultural products. Three or more of these cooperative marketing or purchasing associations may form a federated cooperative association.

4. Q. WHAT IS THE FIRST STEP THAT SHOULD BE TAKEN BY A GROUP OF AGRICULTURAL PRODUCERS CONSIDERING THE ORGANIZATION OF A COOPERATIVE?

A. At a meeting of producers, cooperative marketing or purchasing should be thoroughly discussed as it applies to the commodities under consideration and to local conditions. The prospective members should determine whether: (1) there is a real need for a producer-owned and controlled association; (2) a cooperative can do the job better than it is now being done; (3) there is sufficient volume of business to assure savings to the members; (4) the members can be depended on for loyal support in bad times as well as good; (5) some outsider is encouraging the formation of the cooperative in order to sell property or equipment or get a job; (6) the producers are willing to put their own capital into a cooperative enterprise; and (7) competent and aggressive leadership is available. The answers to these and similar questions will have a direct bearing on the success or failure of a new association.

5. Q. WHAT IS THE NEXT STEP?

A. If the decision is to go ahead, the group then should elect at least five producers as incorporating or temporary directors. These directors may be instructed by the group to complete the organization, obtain a charter, prepare by-laws for the consideration of the new association, and to take such other action as may be desirable.

6. Q. HOW CAN A CHARTER BE OBTAINED?

A. The incorporating directors must prepare articles of incorporation. These articles, after being signed by the incorporating directors and acknowledged before a notary public, are sent to the Secretary of State, Austin, Texas. (Suggested articles of incorporation which should be revised to fit local conditions, may be found in this bulletin.) Issuing and delivering the charter usually requires only a few days, if the articles of incorporation of the association are submitted in proper form.

7. Q. IS THERE ANY COST TO OBTAINING A CHARTER?

A. A fee of \$10 is required by the Secretary of State for issuing the Charter and making the necessary records. This fee should accompany the articles of incorporation when sent to the Secretary of State at Austin.

8. Q. WHEN SHOULD THE FIRST MEMBERSHIP MEETING BE HELD?

A. Not later than 30 days after filing the articles of incorporation the members of the association should hold their first meeting

and adopt appropriate by-laws. (Suggested by-laws, which should be adapted to local needs, may be found in this bulletin.) The directors should be elected at this meeting.

9. Q. WHAT RECORDS SHOULD BE KEPT?

A. Records of the action taken at early meetings of cooperatives are sometimes lost. These may later be very valuable. Minutes of all membership and director's meetings should be carefully preserved. Accurate records of all funds received and disbursed should be kept from the very beginning so that they will be understandable even years later. Nothing should be left to memory or to loose papers. Bound minute books and ledgers are much safer. The secretary, treasurer, or the secretary-treasurer is charged with the responsibility of preserving these important records.

10. Q. WHO MAY BECOME MEMBERS?

A. An association may admit as members all persons engaged in the production of agricultural products. One cooperative, as an organization, may hold membership in another association.

11. Q. WHAT IS REQUIRED OF A MEMBER?

A. The requirements for membership are determined by the members as set forth in the by-laws. Usually they specify that a member must be a producer of agricultural products and purchase a share of common stock or pay a membership fee. The association may require a member to execute a marketing contract binding the member to handle all or any specified part of certain agricultural products through the association.

12. Q. HOW MUCH STOCK MAY ONE MEMBER OWN?

A. The Texas laws states: "No stockholder of a cooperative association shall own more than one-twentieth of the issued common stock of the association." This may be further limited in the by-laws. Ownership of preferred, or non-voting stock, is not limited by law.

13. Q. DO STOCKHOLDERS VOTE ACCORDING TO THE SHARES OF STOCK OWNED?

A. No, the Texas law reads: "No member of the association is allowed more than one vote because of the stock or membership capital he may own therein."

14. Q. MUST STOCK PURCHASES OR MEMBERSHIP FEES BE PAID IN CASH?

A. A stock or membership certificate may not be issued to a member until it has been fully paid for. Promissory notes of the mem-

bers may be accepted as full or partial payments. However, associations with small paid-in capital are in a poor position either for operating or for obtaining credit.

15. Q. ARE MEMBERS OF COOPERATIVES LIABLE FOR DEBTS INCURRED BY THE ASSOCIATION?

A. No, except to the extent of any stock owned in the association or any unpaid balance on a promissory note given in payment for stock or membership fees.

16. Q. HOW DO COOPERATIVES ACQUIRE CAPITAL TO PAY FOR AND OPERATE GINS, GRAIN ELEVATORS, PACKING PLANTS, ETC?

A. If the cooperative is to belong to the members, these members must supply much of the capital used in their business. Some capital is usually raised in cash and notes at the time the cooperative is organized. In most instances, that is not enough. Additional capital may be acquired by retaining, or borrowing a small sum on each unit handled by the cooperative, on each bale of cotton ginned, each pound of butterfat processed, each box of fruit packed, each bushel of grain sold, each dollar's worth of goods supplied, etc. Members contribute this capital in exact proportion to the use they make of the facilities of the association and receive certificates of stock or equity accordingly.

17. Q. WHAT IS MEANT BY "REVOLVING CAPITAL"?

A. In time, these small amounts invested by the members from each unit of product they deliver to or purchase from their association will pay off indebtedness, pay for physical property, and also set up operating capital and reserves. By continuing to retain these small amounts each year, even after the indebtedness is paid, the cooperative can soon pay off the oldest certificates of stock or certificates of equity. In this way the members who actively use the association own and control it. Members who furnish capital in earlier years, but who have moved or for other reasons quit doing business with the association, are gradually paid off as the new capital become available. This plan has much to recommend it to groups forming new cooperatives or those reorganizing old associations.

18. Q. WHERE MAY COOPERATIVES OBTAIN CREDIT?

A. In addition to the usual lending agencies, the Houston Bank for Cooperatives, Houston, Texas, is a possible source of credit for Texas cooperative associations. The bank was established under the Farm Credit Act to furnish credit to farmers' cooperatives. Such loans are made in accordance with good banking practices, with adequate security and an acceptable plan for repayment. A booklet describing co-

operative credit and the services available from this bank may be had by writing the Houston Bank for Cooperatives, Houston, Texas.

19. Q. CAN A COOPERATIVE HANDLE PRODUCTS FOR PERSONS WHO ARE NOT MEMBERS?

A. Yes, a cooperative may do business with nonmember producers as long as the nonmember business does not exceed in value the business done with members. However, it is the policy of most cooperatives to keep the amount of nonmember business as low as possible. Regular patrons, if eligible, should become members.

20. Q. ON WHAT BASIS DOES A COOPERATIVE DEAL WITH ITS MEMBERS?

A. Different plans are followed. It is considered good practice among marketing associations to advance only a reasonable part of the market value at the time products are received from the producer. After the association has performed such marketing services as grading, processing, packing, shipping, selling, etc., the actual cost of these services is deducted, and dividends on capital paid, any sum remaining is returned to the producers as final payment. Many associations retain an amount of money on each unit of produce handled which becomes the member's investment to supply working capital and reserves.

21. Q. HOW WOULD THIS PLAN WORK IN THE CASE OF A COOPERATIVE COTTON GIN?

A. Each producer will pay to his cooperative gin at the time of ginning a rate sufficiently high to cover the expense. At the end of the season, after all expenses, such as salaries, labor, fuel, repairs, depreciation, insurance and taxes, are paid, the amount of the net saving for the season can be determined. The directors will then provide for the distribution of this net margin or saving. If the association is in debt, a portion of the cash payment to members may be withheld for payment of principal and interest installments. For these amounts withheld, each member will receive stock, certificates of equity, or book credit. In this way the capital of the association is built up. From any cash remaining, the directors will provide for payment of limited dividend on the capital invested in the association. They also will set up reserves and the remainder shall be paid to the members as a cash patronage refund based on the amount of business each has done with his association.

22. Q. HOW WOULD A PURCHASING ASSOCIATION OPERATE UNDER THIS PLAN?

A. Supplies are sold to members at cost plus a safe and substantial margin, but usually at prevailing prices. Periodically, savings

above operating costs and necessary retains for capital and reserves are returned to members in proportion to their purchases. Price cutting at the time supplies are delivered disturbs business and had led to disastrous price wars. Selling at regular market price enables associations to return larger patronage refunds.

(22-A) Q. WHAT KINDS OF RESERVES MAY DIRECTORS SET UP?

A. Directors may set up capital reserves, as reserves for contingencies, and valuation reserves, as reserves for bad debts and depreciation. Capital reserves must be allocated and disclosed to patrons, if an association is to be permitted to exclude such reserves from income. Cooperatives are subject to the same rules with respect to setting up valuation reserves as are commercial corporations.

23. Q. DO COOPERATIVES EXTEND CREDIT TO MEMBERS?

A. "All business for cash" was one principle of the early cooperatives. Time has proved the soundness of this rule. Cooperatives should treat all members alike and if credit is given one, others will demand it. Few cooperatives can operate on a 100 per cent cash basis, yet many are so careful in handling accounts that they have practically no loss. Supply cooperatives have a serious problem, for example, when they deliver fuel oil to the farms or when a hired hand hauls out a load of feed. Cash payments, if required, would work a hardship on the patrons. Directors often instruct the manager to extend credit in such cases, but to require payment for the last purchase before making another credit sale to those particular patrons. In that way, accounts are prevented from getting out of control.

24. Q. DO COOPERATIVES PAY DIVIDENDS ON CAPITAL STOCK?

A. Most of them pay reasonable dividends on the capital stock invested by members or others. This rate may not exceed 8 per cent per annum under the Texas law. Often the rate is 3, 4, or 5 per cent. This dividend payment must first be earned, then declared by the board of directors. The dividend rate set in the by-laws should be the rate which the association may reasonably expect to pay. There are some disadvantages to authorizing a rate of dividend higher than the one paid, particularly if an association should find itself on a non-"exempt" basis.

25. Q. DO ALL COOPERATIVES PAY CASH PATRONAGE REFUNDS?

A. It is the ultimate aim of cooperatives to return cash refunds to patrons, however this is not always possible during the early life of

an association when it is paying off its capital investments. When funds are available cooperatives revolve out the oldest outstanding certificates or pay a part of the current margins as a cash refund.

26. Q. IS THE PRACTICE OF LEAVING MARGINS IN A BUSINESS PECULIAR TO FARMERS' COOPERATIVES?

A. By no means. Most of the large and successful commercial businesses in the country started with small investments. Year after year, a part of the profits are "plowed back" into the business. Cooperatives, in following this practice, are acting in good American business tradition.

27. Q. ARE THERE BENEFITS OTHER THAN PATRONAGE REFUNDS TO BE OBTAINED FROM A COOPERATIVE?

A. Yes, farmers can often improve the quality of service they receive. By mixing their own feed or fertilizer, they can be sure that the formulas used meet their requirements. It is not practical for large manufacturers that distribute over many sections to do this. Keeping ownership and control of marketing, processing and distributive facilities in the hands of a large group of citizens reduces the concentration of economic power.

28. Q. WHO DETERMINES THE BUSINESS POLICIES OF A COOPERATIVE?

A. The affairs of the association are managed by the directors, elected by the members from their own number. The directors give general supervision and control to the business. Provision is made in the law for referring certain important matters to the membership for its consideration and action. Members may influence the business policies to be followed by attending membership meetings, expressing their views and by helping to elect directors who share their ideas as to how the business should be operated. Since the members own the cooperative, they should feel free to let their wishes be known.

29. Q. WHAT PROTECTION HAVE MEMBERS FROM DISHONEST EMPLOYEES?

A. The Texas law requires that all officers or employees handling funds or property be adequately bonded. Directors who fail in this responsibility may be held personally liable, under the law, for all losses which may occur because of their failure to require proper bonds.

30. Q. WHAT PROTECTION HAVE MEMBERS AGAINST INEFFICIENT MANAGEMENT?

A. Managers of cooperatives are selected by the board of directors. The best interests of the members demand that they elect di-

rectors who have courage and sound judgment and who are willing to work at the job if they would guard against inefficient management. Active participation of the members in elections and membership meetings is necessary to prevent an unhealthy condition of the cooperative. No relative of a member of the board of directors or of the manager should be employed by the association.

31. Q. WHAT OTHER QUALIFICATIONS SHOULD MEMBERS EXPECT IN DIRECTORS?

A. Members might well raise the following questions when considering the fitness of a nominee for the important responsibility of director:

Will he give the necessary time and attention to the business of the cooperative? Has he conflicting interests? Has he a near relative engaged in a competing business? Has he shown sound judgment in handling his own business? Will he require a strict accounting for all funds and property handled by employees? Has he the qualities of leadership that will attract members—and beget public confidence? Is he progressive enough to keep the association moving ahead?—yet conservative enough to avoid unwise expansion?

32. Q. DO COOPERATIVES PAY TAXES?

A. Yes, cooperatives pay the usual state, county, city and school taxes on their property. They also pay excise, transportation, communication, unemployment taxes, social security, occupational license taxes and a special annual license fee collected from farmers' cooperatives only. In fact, cooperatives pay taxes on the same basis as comparable businesses owned by partnerships or individuals. Cooperatives meeting the strict requirements of the statutes may obtain exemption from federal income tax. Margins distributed to the patrons of a tax exempt cooperative do not escape income tax as they become taxable income to the recipient. Approximately one-half of the farmers' cooperatives in the nation have obtained exemption from federal income tax.

(32-A) "Exemption" from Federal income tax is of small consequence since the enactment of the Revenue Act of 1951. The principal advantages of "exemption" are: (1) Such associations do not pay a capital stock issuance and transfer tax, (2) they do not pay excess profit tax and (3) the amount paid in dividends on stock may be deducted from taxable income. Any business may deduct patronage refunds from taxable income to the same extent that cooperatives may do so if they are paid pursuant to a binding contract between the business and the patron.

33. Q. WHAT REQUIREMENTS MUST AN ASSOCIATION MEET TO BE "EXEMPT" FROM FEDERAL INCOME TAXES UNDER SECTION 101 (12) A OF THE CODE?

A. Briefly stated, a cooperative must meet the following requirements to qualify for a letter of exemption from federal income tax:

1. The association must be owned by producers of agriculture commodities. Substantially all voting rights must be owned by actual producers who patronize the association.
2. The association must not do more business with nonmembers than with members.
3. The rate of dividends (or interest) on capital shares must not exceed 8 per cent or the legal interest rate of the state, whichever is greater.
4. Operations must be of a mutual nature with nonmembers treated equally with members in business dealing and in the distribution of savings.
5. Patronage records must be maintained and permanently preserved.
6. Purchasing associations must not make purchases for nonmembers who are also nonproducers (not farmers) in excess of 15 per cent of the total volume of business.
7. Financial reserves must have a necessary purpose and must be reasonable in amount. To be deductible from taxable income capital reserves shall be allocated to the respective patrons. (See question 22-A)
8. The legal structure of the association must be cooperative in principle.
9. Patronage refunds must be allocated and distributed to patrons under a binding obligation to do so.
10. Notice of the allocations and distribution must be given to the patrons in writing.

Many of the difficulties between cooperatives and the Bureau of Internal Revenue come from failure to answer correspondence and make prompt reports. When farmers go into business, they must be business-like. Officers and employees should be instructed to reply to all important mail.

34. Q. HOW MAY A COOPERATIVE CLAIM "EXEMPTION" FROM FEDERAL INCOME TAXES?

A. While cooperatives meeting these requirements are eligible for exemption from federal income taxes, this exemption must in all cases be sought. The Treasury Department has ruled that: "Every corporation, unless expressly held exempt by this Bureau, is required to file a federal income tax return for each taxable year or period of its existence, regardless of the amount of net income." Application for this exemption is made on Treasury Department Form 1028, a copy of which may be obtained from the Collector of Internal Revenue, Dallas or Austin, Texas. Form 1028 is a questionnaire which should be completed and sent to the nearest Collector of Internal Revenue. Determination will then be made whether the association is exempt.

35. Q. CAN PATRONAGE REFUNDS TO NONMEMBERS BE MADE IN THE FORM OF BOOK CREDIT TOWARD THE PURCHASE OF VOTING STOCK OR ACQUIRING MEMBERSHIP?

A. Yes, the Treasury Department has ruled that patronage refunds may be credited to the nonmember until he pays for voting stock or pays his membership dues, and still meet the requirement that the association deal with members and nonmembers alike.

36. Q. WHAT IS THE REASON FOR "EXEMPTING" COOPERATIVES FROM THE FEDERAL INCOME TAXES PAID BY MANY OTHER CORPORATIONS?

A. A cooperative acts for and in the interest of its patron. Produce is processed or marketed or supplies are purchased for the member. The association deliberately under-pays the farmer for his produce or over-charges him for his supplies and services. The cooperative contracts with its patrons to refund the amounts withheld, after paying the costs of doing business and setting up necessary business reserves. Amounts so withheld by the association are for the account of the patron, held temporarily in the business and eventually returned to the rightful owner as final settlements of business transactions. It is a well established principle of law that an agent, as such, is not liable for tax on funds he temporarily holds in trust for the principal. It is difficult to see how a non-profit business could be liable for a tax on profits which it does not make. The difference between the savings dollar of a cooperative and the profit dollar of a commercial business is that the savings dollar goes back to the patron whose business made the saving possible, while the profit dollar of the commercial enterprise very properly goes to those who invested their capital in the business.

37. Q. IS THE COOPERATIVE MOVEMENT ANTAGONISTIC TO DEMOCRATIC GOVERNMENT?

A. A cooperative is simply a democratic way of doing business and thrives best in democratic soil. If the aims, objectives, and practices of cooperatives were not entirely American and wholesome, one-third of the farmers and ranchmen in Texas would not own and use them.

38. Q. WHAT IS THE ATTITUDE OF THE FEDERAL GOVERNMENT TOWARD FARMERS' COOPERATIVES?

A. The Congress has recognized that farmers need a special type of business organization. The Capper-Volstead Act set forth the purposes for which cooperatives may be organized and the powers they may exercise. The Farm Credit Administration, created by Act of Congress, provides credit to meet the various needs of cooperatives and set up a research service to develop facts and information helpful to cooperatives. There are many evidences that the Federal Government is sympathetic with farmers in their efforts to help themselves.

The report of the Committee on Small Business of the House of Representatives contains the following paragraph:

"The enactment and reenactment of section 101 (12) and (13) of the Internal Revenue Act appears to represent a continuing attitude on the part of the Congress that the maintenance of a sound agricultural economy is necessary for the preservation of the national well-being. It has now become an established national policy co-existent with all other policies designed to extend all possible support and assistance to agriculture. This policy apparently is further reflected in state legislation and the combined policy has been affirmed enumerable times by the Supreme Court."

Both of the major political parties have repeatedly endorsed the principles of cooperation among farmers and have pledged their support to farmers in their business organizations.

39. Q. ARE FARMERS THE ONLY ONES WHO USE COOPERATIVES TO SERVE THEIR INTERESTS?

A. No. The business world has found cooperative principles useful in many ways. Newspapers have their large news gathering cooperative; retail merchants have their cooperative wholesale establishments; other merchants have their mutual insurance service; banks have their cooperative clearing house arrangements; railroads have cooperative provisions for operating union stations and the interchange of cars. Many other examples could be listed. A congressional committee found there are in the United States some 300,000 non-profit and mutual businesses. About 6000 of these, or 2 per cent, are farmers cooperatives.

40. Q. DO MANY COOPERATIVES FAIL?

A. Some do, as a matter of course. Some should never have been organized. Others are launched with insufficient educational work among the members. Taken as a group, cooperatives have a much better record of survival than have businesses in general. A survey made by the Farm Credit Administration inquired into the cause of the failure of a number of cooperatives. Briefly summarized, the reason assigned for cooperative failures were as follows:

- (a) Difficulties in management—high overhead, inadequate accounting, speculation, friction among board members, etc.
- (b) Difficulties in membership—lack of necessary information among members, inexperience of farmers in cooperating, promises of big refunds unfulfilled, etc.
- (c) Financial difficulties—under-financed by members, too liberal credit, over-borrowing, fire loss with insufficient insurance, insistence of members on refunds when cash is needed in business, operating with too small margins, lack of financial reserves, etc.
- (d) Insufficient volume of business—failure to check carefully on volume available before organization, failure of members to patronize the business, over-expansion of facilities, changes in production of crops and livestock, etc.
- (e) Defective legal organization—failure to incorporate, neglect in observing the terms of the charter, by-laws and contracts, etc.

ARTICLES OF INCORPORATION

(Specimen Form)

We, the undersigned, all of whom are residents and citizens of the State of Texas, engaged in the production of agricultural products, do hereby voluntarily associate ourselves together for the purpose of forming a non-profit cooperative marketing association with capital stock, under the Cooperative Marketing Act of the State of Texas.

Article I

The name of this cooperation shall be _____

Article II

The purpose of the association shall be to engage in any activity in connection with the marketing or selling of agricultural products of

its members, or with the harvesting, preserving, drying, processing, canning, packing, storing, handling, shipping or utilization thereof, or the manufacturing or marketing of the by-products thereof; or in connection with the manufacturing, selling or supplying to its members of machinery, equipment or supplies; or in the financing of the above enumerated activities; or any one or more of the activities specified herein. The association, however, may extend any one of the foregoing activities to the products of and supplies for nonmembers to an amount not greater in value than such as are handled by it for its members.

Article III

The association shall have all the powers permitted and granted to associations organized under the cooperative marketing act of the State of Texas, as amended or as the same may be hereafter amended, it being intended hereby to embrace all of the powers enumerated in Article 5742, Revised Civil Statutes of Texas, 1925, as amended or as the same may be hereafter amended.

Article IV

The term for which the association is to exist from date hereof is fifty (50) years.

Article V

The principal place of business of the association shall be _____
 _____ in _____ County, Texas,
 but the association may establish other places of business from time to time.

Article VI

The business of the association shall be under the management, direction, and control of a Board of five (5) directors, and the names and post office addresses of those selected for the first year, and who shall serve until their successors are selected at a stockholders meeting to be held in accordance with the by-laws of the association, are:

Names

Post Office Addresses

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Article VII

The authorized capital of the association is \$100,000.00 of which the sum of \$95,000.00 shall be designated "preferred stock" which shall be divided into 95,000 shares of a par value of \$1.00 per share, and the sum of \$5,000.00 shall be designated as "common stock" which shall be divided into 5000 shares of a par value of \$1.00 per share, all of which stock shall be issued in the manner provided in the by-laws. The holders of preferred stock shall have no preference as to dividends, but in the event of liquidation of the association, the holders of such stock shall be preferred up to the par value thereof plus any declared dividends then remaining unpaid thereon. Dividends on all stock shall be non-cumulative and shall be payable as provided in the by-laws. The preferred stock may be retired upon call of the Board of directors, subject only to the restrictions and provisions of the by-laws.

Article VIII

All margins or earnings, shall be distributed annually in the manner provided in the by-laws.

IN TESTIMONY WHEREOF, we hereunto sign our names this _____ day of _____, 19_____.

THE STATE OF TEXAS }
COUNTY OF _____ } ss.

BEFORE ME, the undersigned authority on this day personally appeared _____, known to me to be one of the persons whose names are subscribed to the foregoing instrument, and acknowledge to me that he executed the same for the purposes and consideration therein expressed.

Given under my hand and seal of office, this the _____ day of _____ 19_____.

Notary Public in and for
----- County, Texas.

erative Marketing Act of the State of Texas with a capital stock of \$50,000.00 divided into 5,000 shares of Common Stock of a par value of \$1.00 per share and 45,000 shares of Preferred Stock of a par value of \$1.00 per share. Dividends on the stock evidenced hereby may be paid in the sole discretion of the board of directors in an amount not to exceed six per cent per annum, as provided in the by-laws and as authorized by law.

The stock evidenced by this certificate may not be transferred to any persons not engaged in the production of agricultural products handled by the Association, and no transfer of this certificate in violation hereof or of the by-laws shall be valid for any purpose.

Secretary

President

PAR VALUE

\$1.00

PER SHARE

**SPECIMEN FORM OF BY-LAWS WHICH MAY BE
ADAPTED TO THE NEEDS OF COOPERATIVES
HAVING A CAPITAL STOCK STRUCTURE**

ARTICLE I

Purposes

The purposes for which this association is incorporated are those set forth in the Articles of Incorporation.

ARTICLE II

Place of Business

The place where the principal business of the association will be transacted is _____,
County, Texas.

ARTICLE III

Board of Directors

Section 1. Number and Qualifications of Directors. The corporate powers, business and property of the association shall be conducted, controlled and managed to the extent authorized by law and by the

Articles of Incorporation and these By-Laws, by a board of _____ directors, each of whom shall be a member of this association or an authorized representative of an incorporated member.

Section 2. Election of Directors. At the first annual meeting of the members of this association, directors shall be elected to succeed the incorporating directors. At such meeting _____ directors shall be elected for one (1) year, _____ directors for two (2) years and _____ directors for three (3) years. Thereafter each director shall be elected for a term of three (3) years. At least two members shall be nominated for each directorship. All directors shall be elected by secret ballot, and the nominees receiving the greatest number of votes shall be elected. Directors shall hold office until their successors have been duly elected and qualified.

Section 3. Vacancies. Whenever a vacancy occurs in the board of directors, other than from the expiration of a term of office, the remaining directors shall appoint a member of the association to fill the vacancy until the next regular meeting of the members.

Section 4. Board Meetings. The board of directors shall meet at least once each month in the principal office of the association at a time to be set by the board of directors.

Section 5. Special Board Meetings. Special meetings of the board shall be held upon call of the President or upon the written request of at least three members of the board. Such written requests shall be signed by the members making the same, shall state the purpose of such meeting, the time and place where it is to be held and shall be addressed and delivered to the Secretary of the Association. Written notice of all special meetings shall be given to all members of the board at least two (2) days prior to the date of such meeting, provided, however, that such written notice of any meeting may be waived by the directors, by unanimous consent.

Section 6. Quorum. A majority of the board of directors shall constitute a quorum at any meeting of the board.

Section 7. Depository. The board of directors shall have the power from time to time to select one or more banks to act as depositories of the funds of the Association, to determine the manner of receiving, depositing, and disbursing the funds of the Association, the form of checks to be used and the person or persons who shall be authorized to sign such checks.

Section 8. Employees. The board of directors shall have power to employ or to authorize the employment of a manager and such other employees as may be deemed necessary, to prescribe the duties thereof and to fix their compensation. No director or member of a director's immediate family shall serve as a manager or employee of the Associa-

tion, nor shall a member of the manager's family be employed by the Association.

Section 9. Bonds.— The board of directors shall require all officers, employees and agents of the Association handling funds or property belonging to, or in the possession or under the control of the Association, to furnish the Association with a satisfactory bond of indemnity, indemnifying the Association and its members against any fraudulent, dishonest or unlawful act on the part of such officers and employees. Such bonds shall be furnished by a responsible bonding company and shall be approved by the board of directors.

Section 10. Executive Committee. The board of directors shall be empowered to appoint from its own membership an Executive Committee of three members, determine their tenure of office and their powers and duties. Such Committee shall keep accurate minutes of its proceedings and shall submit a report thereof to all directors within seven days following each such meeting of the Executive Committee. Such minutes shall be considered and approved by the board of directors at the next succeeding meeting of the board.

Section 11. Removal. Any member may bring charges against an officer, director or member of the Association by filing the same in writing with the secretary of the Association together with a petition signed by at least ten per cent (10%) of the members of the Association, requesting the removal of the officer, director or member in question. The secretary of the Association shall give such officer, director or member written notice of the charges, at least ten (10) days prior to the date of the meeting at which the charges will be considered and voted upon. At the next regular or special meeting of the Association a hearing shall be held and such charges shall be considered. The person charged and the person or persons bringing the charges against him shall be given an opportunity to be heard in person or through counsel and to present witnesses. At the conclusion of such a hearing a majority vote of the members shall decide the issue.

ARTICLE IV

Officers

Section 1. Manner of Election. The board of directors shall elect from their number a president and a vice president. They shall also elect a secretary and a treasurer, who need not be directors. The offices of secretary and treasurer may be combined by the board of directors, and the combined office shall be designated as "secretary-treasurer."

Section 2. Tenure of Office. The officers shall hold office at the discretion of the board of directors, subject to the power of removal by stockholders as provided in these by-laws and as authorized and allowed by law.

Section 3. Duties.

(a) The president shall:

- (1) Preside over all meetings of the association and of the board of directors.
- (2) Call special meetings of the board of directors and of the stockholders.
- (3) Perform all acts and duties usually performed by an executive officer of a corporation.
- (4) Serve as an ex-officio member of all committees of the association.
- (5) Sign all stock certificates and such other papers and documents as he may be authorized or directed to sign by the board of directors.

(b) *The vice president* shall perform the duties of the president at such time or times as the president shall be absent or disabled. In case of the death, resignation, or total disability of the president to perform the duties of his office, the board of directors may declare the office vacant and elect his successor.

(c) *The secretary* shall keep a complete record of all meetings of the stockholders of the association and of all meetings of the board of directors. He shall have general charge and supervision of the books and records of the association. He shall attest or sign as secretary all stock certificates and such other papers pertaining to the association as he may be authorized or directed to do by the board of directors. The secretary shall serve all notices required by law and by these by-laws and shall make a full report of all matters and business pertaining to the association to the stockholders at their annual meeting. He shall keep a proper stock record showing the name and address of each stockholder of the association, the number of his stock certificate(s) and the date of issuance, surrender, cancellation or forfeiture thereof. He shall make all reports required by law and shall perform such other duties as may be required of him by the association or the board of directors. Upon the election of his successor, the secretary shall deliver to him all books and other property in his possession belonging to the association.

(d) *The treasurer* shall keep a complete record of all financial transactions of the association and perform such other duties and exercise such other powers as the board of directors may authorize or direct.

ARTICLE V

Members

Section 1. Qualification of Membership. Any person, firm, partnership, corporation, or association, including landlords and tenants,

who is a bona fide producer of products handled by this association, or a producer of agricultural products who is a purchaser of supplies and/or services provided by this association, may become a member of this association if found acceptable by the board of directors, by purchasing one share of common stock, signing such marketing or purchasing agreements as the board may prescribe from time to time, and by agreeing to comply with the requirements of the Articles of Incorporation and this code of by-laws.

Section 2. Termination of Membership. In the event of the death of a member, or, if the board of directors shall find, following a hearing, that a member has ceased to be a producer of agricultural products or a patron of the association, or has moved out of the territory in which the association is operating, the board of directors may suspend or terminate his membership without prejudice to any of his property rights or equities in the association, and give notice of such action to such member, his heirs or legal representatives, and call for the surrender of his common stock. When such membership is terminated, the board shall call and cancel such common stock in the association owned by such former member, and, in its discretion, pay therefor the par value of such stock in cash, and/or in preferred stock of the association.

Section 3. Annual Membership Review. The board of directors shall review annually its official membership record, and shall determine the membership eligibility status of all persons holding common stock of the association. Such stockholders who are found to be ineligible for membership in the association as provided for in these by-laws shall be notified thereof and given an opportunity to show cause why their common stock should not be called in by the association.

Section 4. NonMember Business. The association, if it elects to do business with nonmembers, shall deal with nonmember patrons in all respects on the same basis as with members, but the association may not do over 50 per cent of its marketing business with or for nonmember producers, and the amount of business which it may do with or for patrons who are neither members nor producers, in farm business services or in the furnishing of supplies and equipment, may not exceed 15 per cent of all such business.

ARTICLE VI

Capital Structure

Section 1. Capital Stock. The authorized capital of the association shall be in amounts of common and preferred stock as set forth in the association's charter and any amendments thereto. Each share of such stock shall be issued and held subject to the terms, condition and limitations of the Cooperative Marketing Act of Texas, as amended, the

Charter of the Association, these By-Laws and any amendments hereafter made thereto.

Section 2. Transfer of Stock. No stock of this association shall be transferred except on the books of the association, and in no event shall common stock be transferred to or owned by any person not engaged in the production of agricultural products except a bona fide Farmers' Cooperative Association. These restrictions shall be printed on every stock certificate subject thereto.

Section 3. Voting Rights. All voting rights shall be vested in the holders of common stock. No common stockholder shall have more than one vote in the affairs of the association or in the election of its directors, regardless of the amount of common stock owned by him.

Section 4. Stock Subscriptions. The Association shall not issue common or preferred stock to any person until the same shall be paid for in full, in cash or credits on the books of the Association; provided, however, that the board of directors may, in its discretion, accept promissory notes for subscribers for such stock, which notes shall be in such form and amounts as the board of directors may prescribe. In no event shall any stock be issued to any such subscriber before such stock has been paid for in full, nor shall such subscriber exercise or have any rights of ownership therein or receive any dividends thereon until said stock has been fully paid for.

Section 5. Dividends. Non-cumulative dividends of not to exceed _____ per cent (___%) per annum are to be paid on the outstanding common and preferred stock of the Association, if, as and when declared by the board of directors. Such dividends may be paid in cash and/or preferred stock of the association in the discretion of the board of directors.

Section 6. Retirement of Common Stock. In the event of the death or expulsion or termination of the membership of a member, the board shall call and cancel all common stock in the association owned by such former member, and, in its discretion, pay therefor the par value of such stock in cash, and/or in preferred stock of the association.

Section 7. Retirement of Preferred Stock. The board of directors is authorized at any time and in its sole discretion to call for the retirement at par of the oldest outstanding shares of preferred stock theretofore issued by the association, as determined from the date of original issue. Payment at par shall be made for called shares immediately on delivery, and failure of the owners or holders to deliver certificates called for shall entitle the association as the owner's agent or otherwise, to cancel the shares called for retirement at the expiration of thirty (30) days after the call has been made. In the event of such cancellation and failure of the stockholder to surrender the call certificate(s), the proceeds of such cancelled stock shall be placed to the credit of such

stockholder in a special account and shall be held by the association for the owner's account in accordance with the laws of the State of Texas. The method herein provided for the revolving of capital shall constitute the sole and exclusive method whereby a patron or other stockholder of the association shall be entitled to convert into cash his equities (property interests) in the association, either prior to or after his withdrawal or expulsion from the association, and shall be in lieu of any right or power any such patron or stockholder might have or be entitled to assert to have his equities appraised by the board of directors or otherwise and be paid therefor on the basis of such appraisal within any given period of time.

Section 8. Stock Retirement in the Event of Death. Notwithstanding the provisions of Section 7 of this article, in the event of the death of a member of the association, the board of directors may, in its discretion, retire common and/or preferred stock owned by such deceased member, having an aggregate par value of not to exceed One Hundred Dollars (\$100), and pay the par value thereof, plus any declared and unpaid dividends thereon in cash to the heirs or legal representatives of the deceased, upon surrender of the stock certificate or certificates so cancelled and retired and upon the submission of satisfactory evidence that such heirs or legal representatives are the sole persons entitled to receive the funds. Such stock, up to the amounts specified, may be so called, cancelled and retired, regardless of the date of issue thereof.

Section 9. Liquidation. Neither common nor preferred stock shall have a preference over the other as to dividends, but in the event of liquidation of the association, the outstanding preferred stock shall be first retired and the holders thereof shall be entitled to payment therefor at par plus any declared and unpaid dividends thereon, before any payments are made to retire the outstanding common stock.

ARTICLE VII

Meetings of Stockholders

Section 1. Annual Meeting. The regular annual meeting of the member-common stockholders of the association shall be held in the offices of the association at 10 o'clock a. m. on the ___ day of the month of _____ of each year. If such day falls on a Sunday or holiday, the annual meeting shall be held on the first business day thereafter.

Section 2. Special Meetings. Special meetings of the members may be called by the president or by a majority of the board of directors. Each such call shall be in writing and shall state the time, place, and purpose of such meeting. No business shall be transacted at any special meeting other than that stated in the purpose for the call.

Section 3. Notice of Meeting. The secretary shall cause a notice of each special meeting to be mailed to each common stockholder of the

association according to his address as it appears on the association's books, at least ten (10) days prior to the date of such meeting. The notice shall state the time, place and purpose for which the meeting was called.

Notice of regular annual meetings shall be given likewise by the secretary, stating the time and place of the meeting.

Section 4. Quorum. Twenty-five per cent (25%) of the common stockholders shall constitute a quorum for the transaction of business at any meeting. If on first call twenty-five per cent (25%) of common stockholders fail to attend, then a second meeting shall be called at which the common stockholders present shall constitute a quorum.

Section 5. Voting. No votes by proxy or power of attorney shall be permitted. All ballots in connection with the election of directors shall be cast by members in person in attendance at the stockholders' meeting at which such election is being held. It shall be permissible, however, in connection with any other matter of business of the association, except the election of directors, for the board of directors to cause to be prepared ballots in writing to be cast by the members and transmit such ballots to the members by mail for their further handling. Ballots so transmitted shall contain a clear and concise statement of each issue to be voted upon and shall provide a place where the members may indicate his vote in favor of or against each such issue. Such ballots must be signed by the member casting the ballot and may be transmitted by him through the United States mail to the Secretary of the association, or delivered to such Secretary in person, to be by him placed in the ballot box in the office of the association prior to the date of the regular or special stockholders' meeting at which such issues are to be voted upon. The envelopes containing the ballots so cast shall not be opened until the vote is counted, at which time such envelopes containing such ballots shall be opened by the counters appointed by the chairman of the meeting. No ballot shall be counted if the envelope containing the same has been opened prior to the time such envelope is delivered to the counters. All eligible ballots cast in the manner aforesaid shall constitute the appearance of the member casting such ballots at the meeting, in determining whether a quorum is present.

ARTICLE VIII

Reserves and Patronage Refunds

Section 1. Margins. It is the ultimate aim of this association to render services to its patrons at cost. In order to operate on a non-profit and cooperative basis and at the same time to insure the solvency and financial stability of the association, adequate margins shall be withheld by the association on all transactions. Such margins shall at all times be subject to allocation to the patrons entitled thereto in the

manner provided by law in accordance with these by-laws, and shall be so allocated within the period of time provided in the Internal Revenue Code in which such allocations are permitted.

Section 2. Reserves. From the aforesaid margins retained by the association, the board of directors in its discretion, may create and authorize the establishment of reasonable reserves for necessary purposes. All capital reserves so established shall be allocated on the books of the association to the accounts of the various patrons on the basis of the amounts contributed by them to such reserves, and each patron to whom such allocation is made shall be given notice thereof. While the valuation reserves which are established need not be allocated, the records and accounts of the association shall be so kept as to afford a means of making accurate allocations of such reserves on the basis of the contributions thereto, if such reserves are not needed for the purposes for which they were created.

Section 3. Allocation of Reserves. Amounts of savings or margins retained by the association in capital reserves, as aforesaid, and allocated to the individual patrons, shall have the same status as though they had been paid to the patrons in cash pursuant to a legal obligation to do so and the patrons had then furnished corresponding amounts of capital for the association. The association acknowledges its legal liability to repay such capital advances to the patrons making the same, pursuant to the terms and conditions of these by-laws.

Section 4. Annual Study of Reserve Accounts. The Board of Directors shall make a study of all reserve accounts, following each annual audit and shall determine whether any of such reserves shall be retained, increased reduced and/or revolved. Following such study the board shall direct the disposition to be made of such reserves, make a record of such action in the minutes of such board meetings, and shall issue proper and necessary instructions pursuant thereto.

Section 5. Revolving Reserve Accounts. Whenever it shall appear to the board of directors that an established reserve is adequate for its designated purpose, the board may direct that said reserve be revolved in whole or in part by taking out of such reserve whatever amount the board may direct and pay the same to the patrons according to their allocated equities in the reserve. Such equities shall be revolved out of such reserve in the date order in which they were allocated. The amounts so revolved out of such reserve account shall be replenished from margins retained during the current year's operations and shall be allocated on a patronage basis.

Section 6. Reducing Established Reserves. Whenever in the discretion of the board of directors conditions justify reducing an established reserve in whole or in part, the board shall order such reduction and direct that the amount of such reduction be disbursed to patrons

according to their equities therein in the date order in which such equities were allocated.

Section 7. Patronage Refunds. The annual net savings or margins resulting from the transaction of the business of the association in excess of the reserve fund requirements as provided above, and after the payment of dividend on the common and preferred stock outstanding, shall be apportioned to and distributed among the patrons as a cooperative refund for the respective year, on a percentage basis, as the same appears upon the books and accounts of the association. Said cooperative refund shall be paid or credited to the account of the patron entitled thereto at least once each year.

At the discretion of the board of directors, funds revolved out of reserves and/or the patronage refunds provided in the preceding paragraph shall be paid to the patrons entitled thereto, in whole or in part, in cash, in certificates of preferred stock, or in book credit; provided however, that in the distribution of such patronage refunds, all patrons shall be treated alike, and there shall be no discrimination between member and nonmember patrons. Following the end of each fiscal year, the association shall notify each patron and stockholder of the association of all amounts allocated to him as a result of the operations of the association during such year, and of all amounts paid or to be paid to him as a dividend on his capital stock for such year. In the event of the payment or allocation of patronage refunds during such year of amounts earned in previous years but not theretofore allocated, the patron shall be given notice of in like manner.

Section 8. Refunds to Nonmembers. In order to provide a mutuality of risk, as well as benefit, the board of directors shall cause to be deducted from patronage refunds due nonmember patrons who are eligible for membership in the association, an amount equivalent to one share of common stock in the association. Such patron, if approved by the board of directors, shall become a member and a share of common stock shall be issued to him.

Section 9. Undeliverable Refunds. In the event that the association is unable to make payment to any patron of patronage refunds or other sums due such patron because of inability to locate the patron or incapacity of the patron to receive the same, or other cause beyond the control of the association, such unpaid amounts shall be placed to the credit of such patron in a special account and held by the association subject to the owner's order, in accordance with the laws of the state of Texas.

ARTICLE IX

Miscellaneous

Section 1. Cooperative Association. This corporation shall be operated in all respects within the limitations of the Texas Cooperative

Marketing Act as amended or as hereafter amended, for the mutual benefit of its members as producers of agricultural products. The value of business conducted with members shall always be in excess of that conducted with nonmembers, and each member shall be limited to one vote.

Section 2. Reports and Audits. It shall be the duty of the treasurer and the manager to furnish the board of directors at least once each month during the operating season with a statement of assets and liabilities as of the end of the preceding month, and with a statement of income and expense covering the period from the end of the last fiscal year to the end of the preceding month. Immediately after the end of each fiscal year the board of directors shall employ a practicing public accountant who shall make a complete audit of the association's records and furnish the board of directors with a report thereof.

Section 3. Contract with Patrons. The patrons of the association, by dealing with the association, acknowledge that the terms and provisions of the Articles of incorporation and this code of by-laws shall constitute a contract between the association and the patrons, and both the association and the patrons are bound by said contract, as fully as though each patron had individually signed a separate instrument containing said terms and conditions.

ARTICLE X

Corporate Seal

Section 1. The *corporate seal* of this association shall consist of two concentric circles surrounding a star. The name of the association shall be included therein.

ARTICLE XI

Amendments

These by-laws may be altered or amended at any regular or special meeting of the members by the affirmative vote of a majority of the holders of the common stock present and voting. No amendment to the by-laws shall be passed, however, unless notice in writing to the effect that the same will be voted upon has been mailed to the address of each holder of common stock of the association.