Cooperatively Moving Minnesota Forward

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April 2011
# Table of Contents

Executive Summary ................................................................. 3

Findings ............................................................................. 6

Recommendations ................................................................. 6

Introduction ......................................................................... 7

  What are co-ops?
  Main advantages of cooperatives
  Some challenges
  Why co-ops are underutilized tools in Minnesota

Minnesota’s Cooperative History ............................................. 14

  New Generation Cooperatives (NGCs)
  Minnesota 308B cooperatives

Cooperatives in Minnesota: Flexible, Diverse, Evolving .............. 20

Worker Cooperatives and ESOPs .............................................. 22

  What we have: ESOPs.
  Worker Co-ops
  International models Minnesota should consider
  Implementing the worker-owned model
  Financial and business help for all types of Minnesota co-ops

Conclusion ............................................................................ 30

  Moving Minnesota Forward

Appendix ............................................................................... 33

References and Further Reading ............................................ 35
EXECUTIVE SUMMARY

It might sound strange, but Minnesota policymakers working to expand business growth should look to the countryside and the success of cooperatives. Some business leaders have and it’s paid off.

Cooperative businesses (co-ops) headquartered in Minnesota account for about $1.5 billion in wages on $33 billion in revenue, just shy of the state’s total biennial budget, according to the University of Wisconsin’s Center for Cooperatives’ research. The group identified at least 1,016 Minnesota-based co-ops, which employ nearly 42,000 people across 16 industrial sectors from farming and biofuels to insurance and banking to education and day care. They hold more than $91 billion in assets and have generated supplemental lines of income for their members.

In fact, Minnesota is the nation’s most cooperatively organized state and home to the country’s two largest co-ops, CHS Incorporated and Land O’Lakes. Despite cooperatives’ positive impact on Minnesota’s economy, they remain an underutilized Minnesota business tool.

Unfortunately, Minnesotans still tend to view cooperation as something “farmers do.” Business leaders and policymakers across diverse communities and diverse industry sectors must look at their market obstacles and ask themselves “What would farmers do?”

Co-ops began in the Midwest during the late 1800s as a defensive business strategy for individual farmers and other small producers looking to overcome market imperfections, such as lack of access to transportation routes, marketing tools, and cost efficient equipment and supplies. As a result, cooperative business structures provided small-scale producers with the resources to compete with larger more well-established companies. In the years since those frontier days, Minnesota in particular has evolved its cooperatives into more progressive business models that provide market advantages for members. That’s due in part to adapting successful models that Scandinavian, German and Dutch immigrants brought to Minnesota.
While there are formal business and tax code definitions, in short, cooperatives are democratically governed, member-owned enterprises buying and selling goods or services. They adhere to seven basic principles, including voluntary and open membership; a mission to educate, train and inform users; and a concern for community.

At a time when small business growth is critical to moving Minnesota’s economy forward, co-ops provide entrepreneurs a tremendous advantage in starting up and growing. For example, many of a business’ startup costs and initial risks are shared among multiple members. The group’s strength expands its individuals’ purchasing power and provides economies of scale. Users are members, giving the cooperative first-hand information about customer needs and buying behavior. One of the most successful and recognizable retail cooperatives is Ace Hardware. Stores are individually owned and operated, but wholesale supplying and other specialty business support is provided at the co-op’s headquarters.

Furthermore, one international research study shows co-ops having a 64 percent five-year survival rate compared to only 36 percent for other types of enterprises. Co-op experts estimate that upper-Midwest cooperatives would have an even higher survival rate.

This report examines how cooperatives have worked to move Minnesota forward and how they work in international economies. It provides strategies for entrepreneurs and communities, large and small, to implement successful cooperatives. The paper also takes a broader look at employee stock ownership plans (ESOPs), a variant close cousin of cooperatives, as an alternative option for development.

The 5-year survival rate for co-ops is 64% vs. only 36% for other types of enterprises.
This undertaking is based on three premises:

1) America’s problems with manufacturing and other middle class-sustaining enterprise didn’t come entirely from the 2008-2009 recession or from the slow recovery that has followed. About 6 million American manufacturing jobs have been lost since the year 2000, both by movement abroad in the global economy and from technological displacement.

2) Economic and business studies have found general agreement that younger firms (Haltiwanger et. al.) and small businesses generate real growth and job creation, not the large corporations with transitory factories that states are always chasing.

3) Throughout state history, Minnesotans have pooled resources and talents to overcome market problems—or “imperfect” markets—by forming cooperatives. Yet, as new market imperfections challenge Minnesota’s economy, we do little as a state to encourage entrepreneurs to revive and use our cooperative tools.

Minnesota’s current economic conditions have impacted almost everyone, from big city folks to countryside residents. A Minnesota Department of Employment and Economic Development labor report published in February 2011 showed that the Twin Cities metro area had five unemployed people for every job vacancy. Greater Minnesota, or rural Minnesota, had 6.9 unemployed people for every job vacancy.
FINDINGS

✓ Minnesota is the country’s most cooperatively organized state, with 1,016 Minnesota-based cooperative businesses and four of the nation’s top 10 largest co-ops.

✓ Minnesota’s cooperatives account for more than $33.3 billion in revenues, employ roughly 41,850 workers, and pay nearly $1.5 billion in wages.

✓ Co-ops aren’t just for farmers; they cross 16 active industrial sectors in Minnesota, including insurance, banking, biofuels, housing, utilities, child care, health care, transportation, and media.

✓ Cooperatives are member-owned and democratically controlled. They help members overcome market disadvantages, such as access to capital, equipment, marketing, and logistics. They provide members an advantage in raising startup capital, expand their individuals’ purchasing power, and provide economies of scale.

✓ While one of Minnesota’s strengths lies in its cooperative business structures, co-ops are still underutilized economic development models.

RECOMMENDATIONS

✓ Minnesota policymakers, business leaders and educators must expand knowledge of and access to cooperative opportunities.

✓ In conjunction with the universities, set up an Employee Ownership Center, similar to one at Ohio’s Kent State University. This allows current business owners to gradually sell their businesses to the workers, creating a succession plan that builds wealth and keeps a company locally owned and operated.

✓ State policymakers should work with private businesses to strengthen existing Small Business Development Centers, which are located in nine regions throughout Minnesota.

✓ Look at successful cooperative models developed in countries with similar characteristics as Minnesota’s. The Finlandia and Northern Italian worker-owned co-op models take advantage of well-skilled workforces, existing multinational companies, and well-developed infrastructure. South American models provide low-skilled workers an opportunity to create wealth in small communities, as could be the case in many areas of Greater Minnesota and inner city neighborhoods that have high populations of immigrant workers.

✓ Ask “What would a farmer do?”
INTRODUCTION

While cooperatives aren’t the only solution to putting people back to work, they are a significant tool Minnesota’s business leaders and public policymakers should employ as part of a comprehensive plan to move Minnesota’s economy forward.

*In the past, co-ops have proven a viable option in reviving local economies, creating jobs and wealth, and stabilizing property values and job markets.*

In the past, co-ops have proven a viable option for Minnesota’s workers, farmers, entrepreneurs and communities in reviving local economies, creating jobs and wealth, and stabilizing property values and job markets. Some of the state’s most successful models center around farming, credit unions, mutual insurance agencies, utilities, food stores, and some health care enterprises—notably, HealthPartners Inc., the largest not-for-profit, consumer-governed health care system in the country.

Still, as this economic downturn has shown, Minnesota can’t rest on past success. It must continue innovating business models as well as new products and services. Evolving the cooperative model to other industries is one way to stay competitive, especially in the science and technology fields, where the co-op model is being underutilized. For example, the newly formed Minnesota Science and Technology Authority noted in its strategic plan that the state ranked seventh nationally in industry research and development, but only 42nd in new tech company entrepreneurship (p.23). Minnesota ranks eighth in workforce education, but only 21st in fast growing firms. In a companion table, the authors found Minnesota ranked 41st for new high-tech business formation in the most recent year states had been measured (p. 24).

There’s a great opportunity for research scientists, hobby inventors, prospective entrepreneurs, local developers and civic leaders to pursue the co-op model as an option to transform innovation potential into business success.

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**The First U.S. Cooperatives**

U.S. cooperatives pre-date the country’s official birth. In 1752, Benjamin Franklin founded the nation’s oldest, continuing cooperative, a Philadelphia fire insurance mutual. It had a rather long name: The Philadelphia Contributionship for the Insuring of Houses from Loss by Fire. It’s now simply known as The Philadelphia Contributionship, offering a multitude of insurance products and home security services.

The second oldest cooperative is the Associated Press. New York newspapers preparing to cover the Mexican-American War (1846-1848) formed the AP in 1846.
What are co-ops?

For those who think of co-ops only as farmer-owned businesses, let’s take a quick look at cooperatives and the reasoning for cooperation.

The National Cooperative Business Association (NCBA), the national umbrella organization for co-ops, uses the following internationally accepted points to define cooperatives:

• They are member-owned and democratically controlled (one member, one vote).
• Surplus revenues are returned to members proportionate to use, not by ownership share.
• They exist solely to serve their members, thus, they are motivated to meet members’ needs for affordable and high quality goods and services, and not just to produce profits.
• Co-ops pay taxes on income kept within the company for investment and reserves. Surplus revenues are returned to co-op members who pay taxes on that income. (See National Cooperative Business Association in References.)

Co-op models have been developed and widely used in the following industry sectors (NCBA):

**Agriculture:** These farmer-owned enterprises handle, process and market farm commodities; provide farm supplies; and provide credit and related financial services. Minnesota-based CHS Incorporated and Land O’Lakes are America’s two largest co-ops.

**Food Co-ops:** About two-dozen consumer-owned grocery and natural food stores exist in Minnesota, about half are in the Twin Cities metro area.

**Child Care and Preschool:** Compared to other industries, this is a relatively small part of Minnesota’s cooperative community with nine known units, but it’s showing great growth potential.

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**Seven Principles of Cooperation**

Principles of cooperation date to the Rochdale Pioneers consumer cooperative in northern England in 1844. These principles set standards for cooperatives worldwide, but have had minor adjustment by the International Cooperative Alliance (Geneva).

1st Principle: Voluntary and Open Membership
2nd Principle: Democratic Member Control (one member, one vote)
3rd Principle: Member Economic Participation
4th Principle: Autonomy and Independence
5th Principle: Education, Training and Information
6th Principle: Cooperation among Cooperatives
7th Principle: Concern for Community

Source: International Cooperative Alliance
http://www.ica.coop/coop/principles.html
Credit Unions: There are more than 8,000 credit unions nationwide serving more than 76 million members, according to the NCBA. About 150 are headquartered in Minnesota.

Financial Services: Co-op banks and cooperative development funds exist in addition to credit unions. One of the nation’s largest is AgriBank, headquartered in St. Paul.

Insurance: Mutual insurance companies are owned by their policyholder-members and are co-ops although incorporated under different legal codes.

Health Care: From Bloomington’s HeathPartners Inc. to lesser known medical providers, these cooperatives help provide access to health insurance for consumers and small businesses; better control prescription drug costs; help community-owned, nonprofit hospitals; improve quality of home-based health care and assisted living services; and help small, independent pharmacists.

Funeral & Memorial Societies: Some are consumer owned to help families with stressful moments in their lives, while other funeral home cooperatives help individuals survive industry consolidation.

Housing: While New York City is most well known for cooperative housing, Minnesota has a growing number of units—more than 6,000—especially in senior housing. Nationwide more than 1.5 million co-op housing units exist.

Marketing: These purchasing and shared service co-ops help local, small business owners survive against large competition. Ace Hardware Stores and Best Western International hotels and motels are among the best known brands of these co-ops.

Manufacturing: While a small number of worker-cooperatives exist, most worker-owned business structures are employee stock ownership plan programs (see later references to ESOPs).
Technology: This is currently a growth area for co-op development and is akin to worker co-ops in manufacturing. NCBA said these new high-tech service co-ops “are often organized as worker co-ops, but sometimes take looser forms in which independent programmers can find support while maintaining their independence.” In that regard, they are a combination of the marketing and manufacturing sectors cited above.

Utilities: These are primarily the rural electric and the telephone cooperatives that are commonplace throughout rural Minnesota.

Main advantages of cooperatives

The United Nations has dedicated 2012 as the year for promoting cooperatives worldwide. Guy Tchami with the UN’s International Labor Organization (ILO) in Geneva, has summarized co-ops advantages over other types of companies.

- Involvement by a significant group of participants can lead to greater innovation and collaboration within the enterprise.
- The users are members, meaning the cooperative has first-hand information about consumers’ needs, purchasing patterns, habits and expectations.
- A cooperative’s structure allows it to enjoy economies of scale.
- Worker cooperatives better motivate employees because of their ownership role.
- Members’ interests are better protected, resulting in better decision making on short-term economic issues and other financial problems.
- The democratic decision-making process means the general direction of the organization tends to be more sustainable and representative of members’ needs.

Applied economists studying cooperatives see Tchami’s list as providing economies of scale and factors reducing “transaction costs,” or the cost of doing business, and thus helping the enterprise survive in markets with well-developed competition.

Some challenges

Co-ops are still businesses. All the pressures brought to bear on individuals and other companies within industries and within markets don’t differentiate among ownership structures. The co-op advantages cited above can help an enterprise adapt, adjust and revamp strategies and products or services, but the never-ending change of marketplace pressures is real.
A cooperative faces two big challenges. One lies in its dual role. While a firm must be entrepreneurial and successful on its own to sustain itself, it must also make its members more entrepreneurial in their ventures, insists Dutch economist Gert van Dijk, a former agricultural cooperatives leader in the European Union (Van Dijk). This usually isn’t an issue for traditional business structures that have a single objective of maximizing profits for the owners.

A co-op also shares a common challenge with more traditional business models. Tensions often develop between “agents,” or managers, and the “principals,” the investors or bondholders whose capital the firm is using. Applied economists have adapted the theory to unique aspects of cooperatives, which will be discussed later, but they are always lingering behind the scenes and threaten cooperatives just like other ownership structures.

Harvard business professor Michael Jensen (a Minneapolis native and Macalester College graduate) and the late University of Rochester professor William Meckling identified this as “agency theory” problems (see Jensen).

If Minnesota business experience offers an accurate picture, however, advantages clearly outweigh disadvantages when good member governance teams with good management to achieve a co-op’s dual purposes.

### Why co-ops are underutilized tools in Minnesota

There is the talent, or human capital, walking around Minnesota that knows how to start, govern, and manage cooperatives. Development specialist Kevin Edberg, with Cooperative Development Services (CDS) in St. Paul, says knowing where to find appropriate expertise in the countryside may be as close as the nearest coffee shop where you’ll likely find two or three farmers with co-op experience. In the Twin Cities, Edberg says, entrepreneurs might find similar guidance at the nearest food co-op.

Ideally, such paths to co-op expertise will lead prospective entrepreneurs to groups such as his, or Northcountry Cooperative Foundation, the Latino Economic Development Center, the Agricultural Utilization and Research Institute (AURI), the joint Wisconsin-Minnesota trade association Cooperative Network, or the Minnesota Extension Service.

Those are starting points, Edberg notes. Meanwhile, major Twin Cities law firms and some rural-based firms have attorneys schooled in unique aspects of cooperative law, and the same applies to accounting firms with expertise in co-op business and tax accounting.

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Advantages clearly outweigh disadvantageous when good member governance teams with good management.

Entrepreneurs can find co-op expertise as near as a rural coffee shop or an urban food co-op.
The problem is these attorneys and accountants “look just like attorneys and accountants you see every day in the skyways,” according to Edberg. The prospective entrepreneur has to be rather knowledgeable about cooperatives to know who the experts are.

That leads us to a second problem. Outside of the cooperative community, co-op development isn’t widely taught at our business schools. Most current workers and leaders within Minnesota’s business community aren’t familiar with cooperatives’ development, operation, or strengths unless they’ve worked directly for or with a co-op.

Such divergence is rooted in business education’s compartmentalization in United States, Canada and Europe. Farmers have been big users of cooperative models; therefore, the U.S. Department of Agriculture and agriculture ministries have provided institutional support and research funding for cooperatives. Following that same money trail, most academic support for cooperatives has come from agricultural and applied economists over the years.

Business schools, meanwhile, turn to other government departments and ministries for support, and to large private and publicly traded stock corporations for private funding of research.

What this means is that graduate schools of business educate business leaders who must discover how member-owned businesses operate and their principal mission when they take jobs with cooperatives and ESOPs. That has also been the case for lawyers and accountants who end up having member-owned businesses as clients; on-the-job training becomes the final educational program for these professional service providers.

This is starting to change, however, observes CDS’s Edberg. While the University of Minnesota’s Department of Applied Economics has offered courses in cooperative theory and management over the years, the university’s Carlson School of Management, law school and public policy programs have now expanded the educational reach to people who might eventually work with co-ops.

Christopher Kopka, vice president of Minneapolis-based mutual Thrivent Financial for Lutherans, and applied economist Michael Boland taught this course during the fall 2010 semester.
“My desire to teach this course stems from many years as a co-op guy, but it also does stem from my work at Thrivent,” Kopka said. “Very few college campuses have classes or seminars on cooperative business models. I think that’s a real miss as this model has and can be used effectively for many types of economic development and business development.”

This represents movement in the right direction for helping Minnesota revive its economy and business opportunities for the 21st century. From an extremely pragmatic standpoint, cooperative development projects have access to capital to start or expand ventures while accessing capital can be extremely difficult for families or individual entrepreneurs.

Edberg and Mark Glaess, general manager of the Minnesota Rural Electric Cooperatives Association, said co-ops have access to capital through various co-op and government programs. Just like the existence of angel fund groups for high-tech and “the next best thing” risk investors in the business world, co-ops do have access to capital and usually at desirable rates of interest. What’s harder to find are business plans that merit investment and financing.

That circles back to proper planning and technical help in readying business plans and financing applications.
MINNESOTA’S COOPERATIVE HISTORY

The point has been made that cooperative enterprises and their various business models represent strengths in Minnesota that should be used, not ignored, or not even recognized. Historian Steven J. Keillor’s 2000 book, *Cooperative Commonwealth*, offers the most comprehensive look at Minnesotans’ early adaptations of cooperative models from 1859 to 1939 (Keillor). Cooperative commonwealth is a sociological term for a region that is heavily cooperatively organized.

Since that time frame, however, the use of cooperative models has come off the farm and spread to far more sectors of Minnesota’s economy as reflected by the following graphic from the University of Wisconsin Center for Cooperatives at Madison. It has found Minnesotans actively engaged in enterprises ranging from childcare service providers to housing co-ops to health care providers to media groups to water and waste management providers.

<table>
<thead>
<tr>
<th>Economic Sector</th>
<th># of Coops</th>
<th>Wages (millions $)</th>
<th>Revenues (million $)</th>
<th>Members (thousands)</th>
<th>Employment (thousands)</th>
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**NOTES**
* Credit Union data is from Credit Union National Association (http://www.cuna.org/research/download/factsheet/Minnesota.pdf)
1. Housing information is incomplete. See (http://reic.uwcc.wisc.edu/house) for details.
2. The number of cooperatives given in the tables is the number of firms identified as cooperatives in the study.
3. The financial data is actual reported data from the portion of identified cooperatives that responded to phone calls and surveys. It does not represent the total activity of the number of identified coops.
It’s difficult to calculate exactly how many cooperatives operate in Minnesota but the University of Wisconsin Center for Cooperatives identifies at least 1,016 Minnesota-based co-ops, across 16 industry sectors. They employ roughly 41,850 workers accounting for $1.5 billion in wages and generate $33.4 billion in revenue.

While these numbers provide the most accurate picture to date, Minnesota cooperatives’ impact on the state’s overall economy is tough to determine exactly. A co-op headquartered in Minnesota generates economic activity from members in a variety of states. Another issue, according to Lynn Pittman with the Wisconsin Center, is the data was gathered through telephone calls and surveys, and as to be expected, not all cooperatives responded or were even identified and contacted.

Nonetheless, as the accompanying graphic on Wisconsin cooperatives shows, our neighboring state is also a cooperative commonwealth. The same can be said for North Dakota, Iowa, Texas, and to various extents, South Dakota, Nebraska, Kansas, Illinois, Missouri and California. (see Appendix for data on Dakotas) Cooperation is a business model strongly connected with the central U.S. states and the old frontier.

### WISCONSIN CO-OPS

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<th>Economic Sector</th>
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<th>Revenues (million $)</th>
<th>Members (thousands)</th>
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**Notes**
* Credit Union data is from Credit Union National Association (http://www.cuna.org/research/download/factsheet/Wisconsin.pdf)
1. Housing information is incomplete. See (http://reic.uwcc.wisc.edu/house) for details.
2. The number of cooperatives given in the tables is the number of firms identified as cooperatives in the study.
3. The financial data is actual reported data from the portion of identified cooperatives that responded to phone calls and surveys.
   It does not represent the total activity of the number of identified coops.
To understand the rise of co-ops in the Midwest, we must look at their role as a “defensive” business strategy in helping farmers and rural residents correct market imperfections threatening their livelihoods.

Agricultural cooperatives are stacked in states that were on the historical frontier, according to research conducted by the Illinois Institute for Rural Affairs (IIRA), Western Illinois University, and the Illinois Extension Service (Egerstrom, 2001). Two points of convergence are apparent. The states in which agricultural cooperatives are most organized are those most distant to population centers and markets, thus farmers sold everything at a discount and bought most farm supplies at a premium until they formed their own cooperatives. Second, they also had ethnic ties to Northern Europe where farmers had fought the same market problems and organized for market power. Our agricultural co-ops are based on the models that cousins, brothers, sisters, uncles and aunts used back in the ‘old country,’ but they’ve been adapted to address Midwesterners’ specific needs.

Since the frontier days, co-ops have gradually evolved from a defensive business model into offensive-oriented cooperatives that seek market advantages, instead of just overcoming market imperfections. Two such newer co-op business models are anchored in Minnesota.

**New Generation Cooperatives (NGCs)**

Starting with Minnesota’s sugarbeet cooperatives in the 1970s (and on the West Coast with other specialty crops) a newer model of cooperative business has been steadily evolving. These are closed-membership cooperatives designed not just to sell raw commodities but to develop a more complete user-ready product. Sugarbeet farmers, for example, started processing and manufacturing their crop and selling the sugar, rather than just selling the beet to a processor. This allows the original commodity producer to move up the food chain—literally and figuratively, capturing more of the consumer’s dollar from value-added processing.
Granted, dairy cooperatives were moving along the same path with branded food products, and forerunner cooperatives to CHS Inc. were doing the same in the grains and oilseed markets. What set the new cooperatives apart from the constantly evolving and progressing cooperatives was the offensive strategy to attack the market, right from the start.

Minnesota and North Dakota farmers were at the front gates of this new business model, creating such co-ops as American Crystal Sugar Co. at Moorhead, Minn-Dak Farmers Cooperative at Wahpeton, N.D., and Southern Minnesota Beet Sugar Co. at Renville. The farmer’s production is aligned with the interests of the company that he or she partly owns from the very start. Purchasing equity stakes in the company buys delivery rights to deliver production from a fixed number of acres of land, and with it, delivery obligations to supply the co-op.

By early 1994, this author had identified 67 such new ventures in the Upper Midwest. While they became known as New Generation Cooperatives, at the time, they didn’t have a name. That was quite a dilemma because in writing the St. Paul Pioneer Press article featuring these new businesses taking root in farm country, I didn’t know how to refer to them. This hasn’t been acknowledged in print before but the New Generation Cooperative title was arrived at during luncheon meetings with cooperative and rural affairs experts at the former Cedar Street Café in downtown St. Paul.

These included cooperative law specialists Richard Magnuson and Mark Hanson, former Minnesota Association of Cooperatives president Alan Gerber, then-president of Minnesota Farmers Union and now Minnesota Commissioner of Agriculture Dave Frederickson, current Humphrey Institute of Public Affairs educator Dr. Gary DeCramer, former North Dakota Governor and past president of the Independent Community Bankers of Minnesota Allen Olson, and Tom Sand, a former aide to Minnesota Congressman and U.S. Agriculture Secretary Bob Bergland.

The name New Generation Cooperatives was accepted because it recognized the new co-ops overcame a generational gap in which current co-op members didn’t seem to know or appreciate the intentions of their ancestor founders. Secondly, the NGCs seem to bind members more closely to the business of their cooperatives, making their co-op an extension of their farm.

This new model allowed the original commodity producer to move up the food chain, capturing more of the consumer’s dollar from value-added processing.
The co-ops overcame horizon problems and portfolio problems identified in Jensen and Meckling’s agency theory (Jensen).

While these structural changes contributed to cooperative business viability and sustainability over time, their greatest achievements were in stabilizing jobs and household incomes for members by opening second and sometimes third income streams for members.

As a case in point, a Minnesota 2020 report (Bhasin) looked at the biofuel co-ops and limited liability companies Minnesota farmers helped start. The report found that by creating nearby markets for their corn, the farmers added about $1.2 billion annually to Minnesota farm incomes, directly and from secondary sources of income.

**Minnesota 308B cooperatives**

By 2003, a new law governing cooperatives made it easier for community residents to team with local co-op members to develop new or expanded ventures, according Amy Fredregill, Minnesota vice president of the Cooperative Network trade association for Wisconsin and Minnesota. It opened a path for more non-agricultural co-ops and bolstered the model’s value as an economic development tool in Minnesota.

In designing the law, Minnesota cooperative officials polled co-ops in 2002 to learn about problems in raising capital and searched for ways to allow community investors and others to invest in existing and expanding co-ops, and to help start new co-op ventures. The new law, 308B, expands on the basic cooperative business code, Chapter 308A.

In this case, Minnesota looked to an earlier Wyoming law allowing outside, non-patron investment in a new agricultural cooperative. Cooperative law specialists then with Lindquist & Venom, Dorsey and Whitney and what is now the Minneapolis office of Stoel Rives, worked with co-op officials in drafting a variant to suit Minnesota needs. On August 1, 2003, Chapter 308B became operative.
It’s a complex statute, but in simple terms, the new co-op law allowed outside investors to gain a stake in co-ops and spelled out their rights as non-patron investors.

As a result of 308B’s success, Wisconsin and Iowa have both adapted variations of the Minnesota law that’s now being used to start a diverse group of specialty food and wine production companies and stores, health cooperatives for physicians and in-home care providers, and a variety of other ventures.

In materials Fredregill has provided for a class at the University of Minnesota’s Department of Applied Economics, she cites Canadian research showing Quebec province has gone even farther in making co-op structures flexible. A 1997 Quebec law allows for solidarity co-operatives patterned after some European models. These are multi-stakeholder businesses where two classes of members are allowed—formed from user-members, employee-members and community supporter-members.
COOPERATIVES IN MINNESOTA: FLEXIBLE, DIVERSE, EVOLVING

Cooperative business models are flexible and enterprises can be structured differently to meet member-owner needs. Consider these Minnesota examples:

**CHS Inc.**—Based in Inver Grove Heights, CHS is the nation’s largest farmer-owned co-op. It had revenue from agricultural marketing, farm supplies, petroleum operations and convenient store operations of $25.3 billion in its 2010 fiscal year.

More than 300,000 Midwest and Northwest farmers own the company, both directly and indirectly through local grain marketing cooperatives and Cenex co-ops. The name comes from the 1998 merger of Cenex, which was founded as Farmers Union Central Exchange in St. Paul in 1931, with Harvest States Cooperatives, formerly of Falcon Heights.

Harvest States was created in 1983 with the merger of North Pacific Grain Growers, founded in Lewiston, Id., in 1929, and Farmers Union Grain Terminal Association (GTA), founded in St. Paul in 1938.

From a series of local co-ops merging, CHS has grown into a multinational force. Its web site offers information for customers, clients, business partners and friends in English, Spanish, Portuguese, Japanese, Chinese and Russian.

**Minnesota Winegrowers Cooperative**—Fanciers of locally grown and produced foods and beverages know this co-op by its brand and Stillwater store name, Northern Vineyards Winery. The grape growers, who were mostly from the St. Croix Valley area east of St. Paul, started this co-op in 1983 when the private winery they were supplying stopped buying grapes.

Nearly three decades later, Northern Vineyards Winery has been studied for its use of Minnesota-developed grapes, for its cooperative business structure (Horsthemke), and its usefulness in restoring private property in former Eastern European countries after the collapse of communism. Meanwhile, it continues to provide economic reasons for people to hold onto private land (“green space”) when private vineyards might otherwise give way to commercial and residential property development.

**Park Plaza Cooperative**—This Fridley manufactured home community, known as Park Plaza Estates, might be Minnesota’s newest co-op. About 50 residents of the park became members and took control of their 90-unit community on February 15th.

Technical assistance for forming the cooperative and arranging financing came from the Minneapolis nonprofit Northcountry Cooperative Foundation. It, in turn, is affiliated with the financing provider, a national partner—ROC USA (Resident Owned Communities).

Park Plaza Estates became the fifth resident-owned manufactured home community in Minnesota.
**Northwest Minnesota Housing Cooperative**—Working from offices in Thief River Falls and Detroit Lakes, this co-op is actually a construction company owned by northwest Minnesota contractors and material suppliers. It was formed after the severe 1997 Red River Valley floods when there was property restoration and rebuilding to do, but individual electricians, carpenters plumbers and local lumber yards didn’t get work with general contractors.

This co-op, headquartered in Thief River Falls, has business services through Midwest Minnesota Community Development Corp. in Detroit Lakes and serves as a general contractor for its members.

At last count, this co-op had built 130 new homes in and around Thief River Falls and Crookston.

**Common Properties Management Cooperative**—This property management co-op based in Minneapolis provides management services, analysis and planning for housing co-ops, condominium, single family homes, commercial property owners and town homes.

The stated mission is to: “deliver professional and responsive property management and maintenance services to its member-owners.”
WORKER COOPERATIVES AND ESOPS

When talking about worker-owned co-ops, it is important to discuss employee stock ownership plans (ESOPs), which are far more common than outright worker co-ops here in Minnesota. ESOP’s are cooperatives’ close cousins even though they are structured under different business models and may be incorporated in different ways.

These employee-invested equity holdings achieve many of the same objectives of a cooperative, and many of them undoubtedly operate using most if not all cooperative principles.

In the following subsections, let’s look first at common employee stock ownership plans and then look at cooperative alternatives.

What we have: ESOPs.

Business literature has encouraged at least partial ESOP participation in corporate ownership structures in recent decades on the theory that employee-owners would be more productive than mere employees. An unintended benefit for other stakeholders, such as suppliers (vendors) and communities, is that these businesses tend to stay put. They don’t export large numbers of jobs abroad, although some successful firms may expand into new markets and create jobs elsewhere.

ESOP companies in Minnesota and the Dakotas have a regional chapter of The ESOP Association and represent better than 10 percent of the national organization’s membership.

Nationwide, there are approximately 11,000 ESOP companies of which about 10 percent are totally employee-owned. The national association’s Minnesota/Dakotas Chapter has about 100 member companies out of an estimated 300 to 350 total ESOP firms. A 2005 survey of its members found these characteristics:

- Three times as many — 29 percent — of M/D firms are totally employee-owned compared with national statistics.
- The average employee ownership of these firms is 65 percent.

Minnesota’s ESOPs of note

**SJE-Rhombus, Detroit Lakes** — This 35-year-old company has grown from a few employees who began buying equity in their workplace to a 400-employee, multinational manufacturer of waste and water management equipment. It is now 100 percent employee owned.

While the company is still based in Detroit Lakes, it has grown and diversified operations to be closer to customers. It now has four plants in the U.S. and one new site in China.

**Walman Optical, Minneapolis** — Since 1915, Walman Optical has become the largest independent optical manufacturing company in the nation. Along the way, Walman employees started buying shares from the founder and eventually turned it into a 100-percent employee company.

Walman now has 820 employee-owners, with 40 locations in 19 states. It generated more than $200 million in 2008 revenue, the last year for which data are available.
• Approximately 99 percent of member firms are privately held.
• While ESOP firms are both large and small, 80 percent have fewer than 250 employees.
• The average number of ESOP employees in Minnesota and the Dakotas is 159 employees.
• ESOPs are proving sustainable; 55 percent report having ESOP plans in place for more than 10 years.

The 99 percent of companies cited above are as close to being cooperatives as companies can be without being incorporated as such or without adhering to the ICA’s cooperative principles. What the data show, however, are that hundreds or thousands of Minnesotans already use equity stakes in their companies. This gives them the benefit of profits made from their labor, talents and, to various extents, a voice in management or governance.

Five million American workers own their businesses through ESOPs. Chicago-based United Airlines is probably the country’s best known ESOP, with 54,000 employee owners. The Iowa-based Hy-Vee grocery chain, with stores in southern Minnesota, is also partially owned by employees.

Sue Crocket, executive director of the Minnesota/Dakotas Chapter of ESOP, said almost all of the Minnesota ESOP companies started out as closely-held private companies. As owners began looking at succession plans, they started bringing employees into the ownership structure.

The companies that are 100 percent employee-owned today usually started with employees making gradual acquisitions of equity in the company. In some cases, former owners had a social agenda in which they wanted the employees to succeed them as owners, or they wanted to do it for the good of the community, and oftentimes both, she said.

The 100 percent employee-owned companies are mostly S-Corp businesses today, she said. Partial employee-owned are a mix of C-Corp and LLC business structures. But unlike cooperatives, Crockett added, few of the ESOP companies operated like co-ops where they influence management from boards even though their equity holdings would give them a voice in board selections and management hiring.
**Worker Co-ops**

A few genuine worker cooperatives do exist in Minnesota, such as the Hub Bicycle Cooperative in Minneapolis and Seward Childcare Cooperative, also in Minneapolis. More can be found in Wisconsin, such as the Union Cab of Madison taxi company and a co-op for rural in-home healthcare workers.

Across the nation, worker co-ops prove to be flexible in enterprise and most are comparatively small. Among diverse examples are Massachusetts-based Dollars and Sense magazine and the mechanics-owned Pelham Auto Parts; the Black Star Co-op brewpub and restaurant in Austin, Texas; the Blue Scorcher Bakery & Deli in Astoria, Oregon; Ronin Tech Collective web developers in Vermont; and in California, the Pedal Express bicycle courier service in Berkeley and the Mandela Foods Cooperative in an underserved Oakland community.

“I think [worker co-ops] are the most exciting sector right now,” said Audrey Malan, a Wyoming-based cooperative development specialist. Many newer co-ops are empowering people who were otherwise blocked from careers and employment by the recession and slow national recovery, she said. New groups and new ventures are forming all over the country.

Major research universities, from Berkeley and Davis in the University of California system to Massachusetts Institute of Technology (MIT) have helped develop programs and curricula for people wanting to learn how to start, manage and govern worker co-ops.

**Minnesota Worker Co-ops**

**The Hub Bicycle Cooperative, Minneapolis**—Founded in 2002, 13 employee own and operate this bike shop dedicated to providing “sustainable transportation products and services” with bikes, clothing and equipment from two south Minneapolis locations.

Benjamin Tsai, development coordinator, said the 2009 recession “was tough for all of us,” but 2010 bounced back. The 2010-2011 winter’s heavy snow was a nuisance “but Minnesota bikers are a hardy bunch,” he says. Business has recovered.

The Hub is one of only a handful of bicycle sales and service cooperatives in the country.

**Seward Child Care Cooperative, Minneapolis**—This is a dual membership co-op in south Minneapolis. The name comes from the neighborhood; however, it is not an adjunct co-op of the well-known Seward Food Cooperative.

The child care co-op was started 37 years ago by parents who would take turns providing child care services. It’s evolved into a patron-member co-op of parents along with the seven worker “collective” members as co-owners, said Sasha Bloomquist, a member of the latter.

In many regards, it is a professional worker co-op. Most of the seven teacher-worker members have master’s degrees in various disciplines or are working on graduate degrees.
In 2004, a national organization was formed at a meeting hosted by the University of Minnesota’s Humphrey Institute of Public Affairs to encourage and mutually aid co-ops. However, only two Minnesota-based enterprises are current members among the organization’s North region—the Seward Childcare Cooperative and Hub Bicycle Co-op (U.S. Federation of Worker Cooperatives).

**International models Minnesota should consider**

Just as Minnesota adapted Northern European models for early cooperative success, state policymakers and business leaders should again look oversees for more diverse modern-day examples. All of the following show potential usefulness in either rebuilding or building from scratch new 21st Century economies.

**Finlandia Cooperatives** — Minnesota 2020 has written about the explosion of Finland’s new cooperatives. They best represent what a Minnesota model could look like because they’re based on a highly skilled workforce, using some of the world’s most modern infrastructure.

The Soviet Union collapsed in 1991 and effectively ended Finland’s trade with its neighbor at precisely the same time Finland was removing social safety net programs to qualify for European Union membership (1995). The little Nordic country was thrown into depression. Unemployment soared.

Within a few short years, Finland’s well-educated populace had created more than 2,000 cooperative ventures. Finnish architects, engineers and designers, for example, are now helping build projects in new wealth regions of the Middle East, parts of Asia and South America—and much of this work is done on computers from lake and beachfront homes using Finland’s state of the art telecommunications.

While these new co-ops are essentially modern versions of the historic marketing and purchasing cooperatives of years gone by, they are also worker co-ops. It’s just that Finland’s professionals and highly skilled people of today are the workers of the Developed World’s 21st Century economy (Newsweek).

**Emilia-Romagna** — This region is northern Italy’s “cooperative commonwealth.” It is best known for fashions, gourmet cuisine, food companies such as the Barilla Group, specialty wines such as Lambrusco, and auto and motorcycle makers such as Ferrari, Ducati, Lamborghini, Maserati and Pagani.
Aside from providing the world with good food and fast cars, this region provides Minnesota with a model for small scale technology manufacturers and bio-tech entrepreneurs to form worker-owned cooperatives. Many of the Emilia-Romagna’s 8,100 worker-owned cooperatives supply the country’s well established international businesses with parts, helping make it Italy’s third wealthiest region and one of the wealthiest in all of Europe.

**Biobusiness is an emerging Minnesota strength**

Similarly Minnesota has many highly-skilled engineers and tech-savvy workers that could join forces to supply the state’s bio-tech firms in much the same way farmers came together to supply giants like General Mills, Cargill and the nation’s food processors.

There are conflicting reports of the bio-tech fields’ strengths to Minnesota’s overall growth potential. On the high-tech side, Minnesota Public Radio has noted that Minnesota may be falling behind other states that have made commitments to developing new sciences and companies. Another report from the BioBusiness Alliance of Minnesota found that biobusiness jobs increased by 20 percent between 2002 and 2007, and that growth continued in 2008 and 2009. Biobusiness is an emerging Minnesota strength. The challenge going forward will be to encourage business development of all levels of advanced technologies. Worker-owned co-ops can help provide Minnesota with advantages in these fields.

**Mondragon** — This community and region in the Basque country of northern Spain is everyone’s favorite example of worker co-ops. The National Center for Employee Ownership in Oakland, California, credits the umbrella Mondragon Cooperative Corporation (MCC) as having 85,000 employees at about 250 federated companies, and it has 7,500 students at its Mondragon University. Business activities include four sectors ranging from finance/banking to industrial manufacturing to retail stores to education.

While all of these activities are co-ops adhering to cooperative principles, what anchors them as worker co-ops is the industry sector where 90 percent of industrial employees are co-op members.

Using co-op terminology cited elsewhere, the Basque minority in northern Spain suffered what cooperators would call complete market failure. The Basque were on the losing side of the Spanish Civil War (1936-1939). Generalissimo Franco retaliated and went so far as forbidding Spanish banks from doing business in the region.
The people around the community of Mondragon sent a young priest, Jose M. Arizmendiarieta, to the London School of Economics to study economic development and cooperatives. When he returned, he set about establishing a technical college in 1943 to train managers, engineers and skilled workers; and the growth of automotive parts and household appliance manufacturing, credit union-like banking and retail store developments spread from there.

Simply put, what markets failed to provide, the people of Mondragon created.

**Mercosur Cooperatives**—Cooperative building in South America is in a rapid state of development, closely linked with general economic growth being experienced throughout the continent.

The name for these cooperatives shown above has no legitimacy in political recognition or in academic studies. Rather, it is mostly slang used here because it encompasses the Mercosur countries, and they have an international organization that uses the identifying mantle of “cooperatives of Mercosur.”

Mercosur is the name of the common market trade region involving Argentina, Brazil, Paraguay and Uruguay formed in 1991 that has expanded, both formally and through common practice, to other countries. The co-op organization, translated into English, is the Specialized Reunion of Cooperatives of Mercosur.

Some South American national laws allow former factory workers to become squatters. Quirks in some South American national laws allow former factory workers to become squatters, taking over abandoned factories and then starting new businesses—often with machinery that was left behind. Two such movements include Brazil’s Landless Workers’ Movement and Argentina’s National Movement of Recuperated Businesses.

Far more common, however, are groups of women or other workers starting businesses from scratch, much like the farmers in the Upper Midwest a century ago, and then use their pooled resources, volume of production and talents to contract with other companies or reach markets on their own.

Again, Internet search engines reveal plenty of reading in English, Spanish and Portuguese about these organizations and cooperative development in South America. But one especially interesting piece is Michael Fox’s “South America: Mercosur’s Cooperatives in an Age of Integration” (Fox).

One co-op of three-dozen women in Porto Alegre, Brazil, that he profiles is Univens, which is the “We Will Overcome Cooperative of United Seamstresses.” It is now one of 15,000 co-ops that account for nearly 22 million members in the Mercosur region.
Such cooperative models may prove as useful to Minnesota as the previously mentioned Finlandia cooperatives. The Latino Economic Development Center, based in Minneapolis, is currently working with women to start cooperatives that can utilize their skills. CDS’s Edberg said this is especially so in southwestern Minnesota counties that can use startup enterprises and where third- and fourth-generation residents are well aware of cooperatives.

Implementing the worker-owned model

While it’s critical to examine successful worker-owned models for Minnesota to follow, business leaders must have a practical way of actually starting or turning over ownership to employees. Kent State University’s Ohio Employee Ownership Center provides many practical examples for implementing this strategy. Founded in 1987, the center began helping business owners with succession planning.

“We’d spend maybe eight hours going over succession plans. And then we’d say, ‘Oh, by the way, you could do this by selling to your employees,’” said Bill McIntyre, the center’s program director.

Initially, almost all companies that brought employees into ownership used employee stock ownership plans (ESOPs), McIntyre said. Now, about 50 percent of assisted companies go the ESOP route and the other half become cooperatives.

Differences in tax laws tend to make companies with more than 30 employees better candidates for ESOP stock ownership, he said. Smaller, startup companies and firms with 20 or fewer employees can be more easily converted into co-ops.

To this point, the OEOC can point to 14,700 jobs it has helped to save, stabilize or create in Ohio. Those workers now have equity totaling $344 million in their businesses.

It has also helped start companies or convert privately owned companies to employee ownership in Pennsylvania, New York and a few other states.
Financial and business help for all types of Minnesota co-ops

Minnesota does have an extensive network of Small Business Development Centers (SBDC) throughout nine regions of the state that are licensed by the Minnesota Department of Employment and Economic Development (DEED). State efforts are supported with federal funding and programs such as those offered through the Small Business Administration (SBA).

The metro area SBDC is housed at the University of St. Thomas, the West-Central region is housed at Concordia College in Moorhead, and most of the other centers and satellite offices are based at campuses for either the University of Minnesota system (Duluth) or Minnesota State Colleges and Universities (MnSCU) system.

An informal check with SBDC offices found most assistance is given to private individuals wanting to start or expand a business. From opposite sides of the state, SBDC specialists at International Falls and Marshall said they haven’t been queried about cooperatives or ESOPs.

Regional director Cathy Lindquist at Moorhead hasn’t fielded such questions, either. But given the huge cooperative business presence in west central Minnesota and the Fargo-Moorhead area, “I would know where to turn when it happens,” she said.

Such centers help businesses, she noted, and it helps future economic development by engaging students on work projects. “Business isn’t just IBM and Apple. You don’t need to leave here and go to Minneapolis or San Diego to have a business career,” she said.

As noted, Minnesota has a strong base of employee-owned and employee-participating ESOP companies. This might partly explain why Minnesota, with its deep cooperative roots, has so few actual worker co-ops. But as examples cited from South America and Europe suggest, there is enormous potential for worker co-ops to become a vibrant source of entrepreneurship here in Minnesota.
CONCLUSION

No matter how one defines business success and failure rates, cooperatives and their ESOP cousins prove to be sustainable, keep businesses anchored in communities, and provide secondary benefits for stakeholders that aren’t easily measured.

For instance, the International Labor Organization (ILO) cites Canadian research that shows 64 percent survival rates for co-ops after five years, compared with only 36 percent for other types of enterprises. Nonscientific assessments of cooperatives in the Upper Midwest states would suggest higher survival rates for co-ops.

Cooperative development and ESOP ownership ventures have scored great successes in Minnesota. By pooling resources, ideas and capital—as the ILO summarizes cooperative action—new Minnesota ventures have succeeded where individuals might have failed or never got off the ground. But that work is far from complete.

We must also look at impacts on communities when co-ops consolidate, which sometimes comes as a result of co-ops’ success, especially in New Generation Cooperatives’ case.

The University of North Dakota and Oklahoma State University have studied economic impacts of NGCs on counties and communities in their states, but “survival” endurance hasn’t been fully studied. Since farmers have been the most aggressive in starting NGCs in the past 20 years, questions arise whether the co-op “failed” or “survived” when ventures are merged or sold into larger, non-cooperative companies.

Success and failure get interpreted differently between cooperative organizers and community and regional economic developers. The latter would still consider a co-op that “demutualized,” or sold to different owners, a success when a local plant remains in business; it continues to provide local employment, it generates local economic activity, and, in the case of agricultural cooperatives, it continues to add value to area resources or products.

What factors researchers use to determine a NGC’s community impact doesn’t negate their overall success in creating wealth in the countryside. Rural communities are well versed in the use and success of cooperatives. The problem comes when we try to transfer this model to the broader economy.

Universities have compartmentalized business education in the United States, Canada and Europe that makes getting cooperative information difficult for some potential entrepreneurs. As noted earlier, business schools tend to ignore co-op business options.
What this means is that graduate schools of business educate business leaders who must discover what member-owned businesses are about when they take jobs with cooperatives and ESOPs. That has also been the case for lawyers and accountants who end up having member-owned businesses as clients; on-the-job training becomes the final educational program for these professional service providers.

While the University of Minnesota’s Department of Applied Economics has offered courses in cooperative theory and management over the years, the university’s Carlson School of Management, law school and public policy programs have only begun to reach other students.

This represents movement in the right direction for helping Minnesota revive its economy and business opportunities for the 21st Century, and needs to be encouraged.

**Moving Minnesota Forward**

Minnesota needs to make knowledge of cooperative options, multiple stakeholder options and ESOPs more readily available to prospective entrepreneurs and their friends and backers. There are two principal ways to make this happen:

- Minnesota needs a “cooperative, ESOP and community-based enterprise center” similar in objectives to the Ohio Employee Ownership Center at Kent State University. This new center would need to be a public/private undertaking. It would also need to be structured in a way to allow the center access to federal funding support from multiple departments and agencies, breaking the rigid lines of support cited above. It must also be centrally administered to provide access and service to Minnesota’s metropolitan and rural regions.

- Clearly, it would need collaboration and intellectual access to University of Minnesota researchers and the University Extension Service; and it would equally need access to MnSCU campuses and the Continuing Education and regional economic development services provided by those universities and colleges that are located strategically throughout the state.

- Finally, partners in such a venture would need to offer appropriate resources and technical expertise. These should include Cooperative Network (Wisconsin and Minnesota), the Minnesota/Dakotas Chapter of the ESOP Association, Minnesota Rural Electric Association, Cooperative Development Services (CDS), Agricultural Utilization Research Institute (AURI), professional associations involved with succession planning and economic development, and nonprofit organizations committed to aiding statewide, regional or local economic development.
Minnesota business leaders and policymakers must also work to strengthen the already extensive network of Small Business Development Centers (SBDC), which are located in nine regions across the state and licensed by the Minnesota Department of Employment and Economic Development (DEED). This should happen through increased collaboration and support from DEED and other state departments and agencies; with Minnesota academic institutions; with federal agencies and with private and nonprofit partners.

These centers are ideally located to be of even greater service in making Minnesotans aware of business structure, ownership and governance options for local economic development.

Such steps would help Minnesotans build on what have been great strengths for the past 150 years—our ability to work cooperatively and collaboratively. Positioning us for the years ahead would also be timely. The United Nations has designated 2012 as the “International Year of Cooperatives,” with the theme: “Cooperative enterprises build a better world.” It will encourage ground-up economic development through cooperative actions. That makes a great platform for building from Minnesota’s strength.
## APPENDIX

### NORTH DAKOTA CO-OPS

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### SOUTH DAKOTA CO-OPS

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<th>Economic Sector</th>
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<th>Wages (millions $)</th>
<th>Revenues (million $)</th>
<th>Members (thousands)</th>
<th>Employment (thousands)</th>
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<td>Members (thousands)</td>
<td>Employment (thousands)</td>
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NOTES

1. Housing information is incomplete. See (http://reic.uwcc.wisc.edu/house) for details.
2. The number of cooperatives given in the tables is the number of firms identified as cooperatives in the study.
3. The financial data is actual reported data from the portion of identified cooperatives that responded to phone calls and surveys. It does not represent the total activity of the number of identified coops.
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www.mn2020.org