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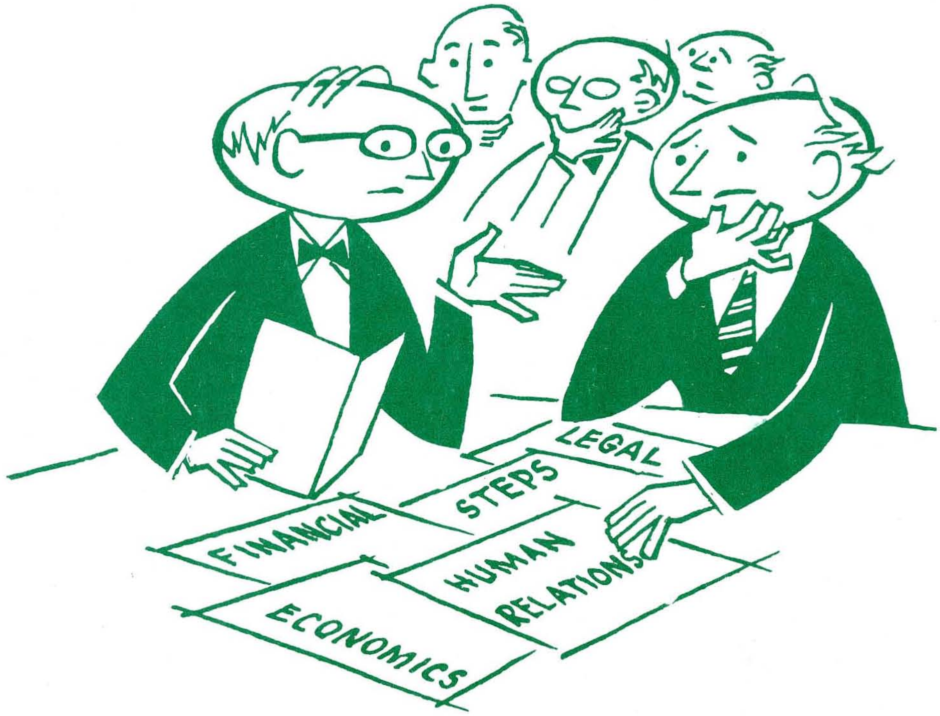
MERGERS for Stronger Cooperatives

USDA Farmer Cooperative Service



MERGERS

for Stronger Cooperatives

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Because of the interest in mergers by farmer cooperatives, this series of articles from the April and May 1961 News for Farmer Cooperatives on problems and possibilities of mergers have been collected into this publication.

It is hoped that cooperatives and others will find helpful the information in these articles written by staff members of Farmer Cooperative Service and the Office of the General Counsel, U. S. Department of Agriculture.

The articles are based upon experience in working directly with cooperatives involved in mergers and from related research studies.

Contents

Mergers for Stronger Cooperatives

by JOSEPH G. KNAPP
Administrator,
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TO MERGE—or not to merge. This is the problem confronting a number of farmer cooperatives today.

Times have changed since many existing farmer cooperatives were formed. We now have fewer and larger farms, better roads, better means of communication, and better transportation methods and equipment. It is possible for a cooperative to serve farmers effectively over a much wider territory than even a decade ago. Moreover, larger cooperatives serving larger areas can provide more extensive services and afford better management.

We have seen this same economic trend affecting general business firms. In the search for efficiency and lower overhead costs, they likewise have been expanding in size through merger or other methods of growth.

There is widespread use of the term merger to cover consolidations or acquisitions as well as mergers. We are here using the term in this broad sense. Under a true merger, two or more cooperatives are joined together with only one association continuing in existence. On the other hand, consolidation represents the creation of a new cooperative by two or more cooperatives who lose their identity in the process.

"Mergers" are not new in cooperative literature but they have been growing in importance due to the revolution in agriculture which calls for stronger, better integrated cooperative organizations.

Over 40 years ago the Cooperative Grange League Federation Exchange Ithaca, N. Y., was formed to combine the purchasing activities then being carried on by the New York State Grange, the Dairymen's League, and the New York State Farm Bureau Federation. In the intervening years it has extended and broadened its operations through acquisitions and consolidations.

Mergers Increasing

Our records in Farmer Cooperative Service indicate that over 170 cooperative consolidations occurred in the 4 years from January 1, 1957, to December 31, 1960. These mergers took place in 37 different States, although the highest proportion was in the North Central region. They included various kinds of marketing and farm supply purchasing associations with the majority in dairy cooperatives. Present indications suggest that the trend toward consolidations is increasing in intensity.

The desire of farmers to build strong efficient cooperatives has given a great impetus to mergers in recent years. In some cases it has been a case of merge or fail.

Yet it is not easy to merge. Cooperatives are like trees in that they have roots. Sometimes it is even difficult for them to make the changes essential to survival.

Farmer Cooperative Service has helped many groups of farmers on the problems involved in merger. In this work we have found that every merger must be a tailor made job. It's not easy to recreate an organization out of existing ones. Planning must precede agreement and arrangements that will give life to the new organization.

From our experience we have prepared five articles to help other farmers with like problems. This issue will examine the economic problems to be explored in contemplating merger, the financial problems and procedures involved, and the problems of human nature that can't be overlooked. In the May issue we will consider the legal problems and the steps involved in the actual process of merger.

Obviously, these five articles will not exhaust the subject, for each proposed merger involves a unique set of problems and circumstances. Rather, they will flag major items that should be considered. These articles are in reality guideposts for those who contemplate cooperative mergers — and not hitching posts.

Economic Explorations Into Mergers

by Martin A. Abrahamsen

Farmer Cooperative Service.

THE principal reasons cooperatives merge are economic in nature.

Merger becomes attractive whenever there appears to be an opportunity to: (1) Realize better prices, (2) increase bargaining power, (3) reduce operating costs, or (4) to provide farm business services not otherwise possible or feasible before.

But the cooperative member would do well to marshal facts to get a firm "yes" or "no" answer to the question: Would he be better off if his association merged? It is important for him to be constantly aware that this question relates to the basic objectives of cooperatives — namely economic benefits for members.

The many aspects of merger are interrelated because bringing about an effective merger depends on the attitude and ability of the people who are assigned responsibility for carrying it out. Even though members stand to gain economic advantages, there is no assurance that these can be realized if these persons are indifferent or incompetent. The economist can only go so far as to indicate whether dollars and cents advantages can be realized from mergers. He cannot guarantee their translation into actual benefits for members because so much depends on the individuals concerned.

Framework for Assumptions.—Any study of prospects for merger may well be approached through the framework of certain economic assumptions. Cooperative leaders and members should consider carefully the state of the economy in which they find themselves Then they will be in a better position to make the best decision on the most desirable course of action for their cooperative to follow.

Among the more useful areas in which assumptions might well be developed are:

1. *The Future of the Economy.* In looking ahead during the next 5 or 10 years, can cooperative leaders expect depression, economic growth, or maintenance of the status quo? If a depression, how severe? If economic growth, at what

rate? Can they expect continuation of the cold war? Will international tensions increase or decrease? What will be agriculture's role in the cold war? For example, are "Food for Peace" programs likely to be expanded or contracted and what role may cooperatives play in these programs? Will the trend toward bigness in industry continue and to what extent does this suggest the desirability of farmers taking further steps to achieve comparable bargaining power?

2. *Trends in Agricultural Production, Marketing Activities, Farm Supply Needs, and Business Service Requirements.* In this area, will the trend toward fewer but larger farms continue? Will technology result in increasing food production at a faster rate than total demand is increased? More specifically, an area may be going into or out of broiler production with the consequence that the demand for feed would increase or decrease greatly. Other areas may be going into or out of grain, tobacco, or livestock production. This would result in marked shifts in feed usage, in the demand for fertilizer, and in required business services.

In addition the cooperative is confronted with changing trends in market structure for the products the farmer has to sell; particularly larger but fewer processing and distributing firms, mass merchandising, specification buying, and increased processing and purchasing.

In actual practice the farmer needs to know what kinds of creameries, grain elevators, and cotton gins he should have to deal with changing market patterns that result from population trends, changes in consumer preference, and related considerations. From the production supply and service angle these trends are important: (1) Bypassing local assembly and distribution points, (2) bulk distribution of feed and fertilizer, and (3) improvements in a wide range of credit transportation, processing and manufacturing services.

3. *The Competency of Management (Directors and the Manager and his Top Staff) and the Understanding of Members.* Do the cooperatives concerned with merger now have or can they attract individuals capable of managing the new associations that assume the larger responsibilities merger involves? Not only do larger cooperatives offer opportunities for more effective business performance; they also may involve greater risk and the danger of more spectacular failure.

Having made the best possible appraisal as to economic climate that will prevail in the immediate years ahead, cooperative leaders are now ready to assemble and interpret facts that have a bearing on the desirability of merger in their particular situation.

SPECIALISTS IN EACH JOB RATHER THAN JACK-OF-ALL-TRADES

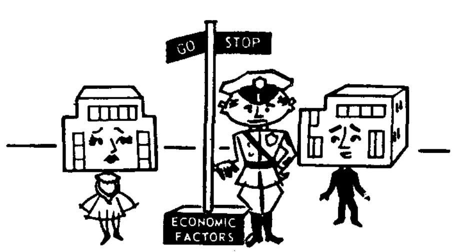
Economic Exploration—In exploring economic consequences of merger, cooperative leaders may want to consider these consequences from the standpoint of: (1) Use of facilities, (2) use of personnel, and (3) operating practices.

These should be looked at mainly from the standpoint of benefits or advantages to members. Unfavorable consequences also should be examined, even though they may be temporary. For example, these may result from acquiring obsolete facilities, doubtful accounts receivable, and a financial structure out of balance because of unfavorable operating conditions.

1. *Use of Facilities.* To a considerable degree, "economies of scale" show up in the use of cooperative facilities. To illustrate: Cotton gins, dairy plants, and fertilizer mixing plants usually have lower fixed costs per unit of output as the size of their operations increase. If a merger of small cooperatives results in the use of fewer but larger plants, the per unit costs for farmers should be reduced.

Any exploration of merger, therefore, should include careful examination as to how strategically facilities are located, and whether it would be possible to serve the combined membership of the various associations through joint use of fewer facilities. If a given facility is favorably located and fully utilized, it often may be possible to reduce total operating costs by as much as one-third by merger.

An objective look at existing facilities is also needed. Can some plants be closed and either reconverted to other uses or sold for other than competing uses? In some instances all plants may be obsolete and it should be determined if merger would enable cooperatives to join in the construction of modern facilities that might be the only way to achieve maximum benefits for members.



Another aspect in the use of facilities is determining if the combined volume of the cooperatives involved is such that together they can undertake new or additional services that none of them acting individually are in a position to provide. For example, in many cases individual associations might not be able to efficiently construct and maintain fruit or vegetable processing facilities, egg breaking facilities, insecticide and paint manufacturing plants, or grain storage—to mention just a few. Cooperatives should ascertain if merger could result in construction and maintenance of these plants and if such action is a further service to members.

2. *Use of Personnel.* Opportunities for a reduction in personnel costs resulting from merger should be explored by cooperative leaders contemplating such action. Is it possible, for example, to achieve economies in plant and warehouse labor costs? If two cooperatives merge, there is need for only one general manager instead of two; and when the associations are small, one or two bookkeepers instead of two or more, one office manager instead of two, one warehouse supervisor instead of two, and so on down the line.

However, it cannot be emphasized too strongly that success is only achieved if managers and directors have the ability to grow as the cooperatives grow.

Likewise, it ought to be determined to what extent these reductions may be partially offset by higher salaries needed for more competent personnel.

There is another side, however, that needs to be considered. To what degree do opportunities prevail for more effective use of personnel when cooperatives join forces through merger. For instance, the merged cooperative, because it is a larger and perhaps a stronger organization, may more readily obtain and retain competent personnel. It should be considered that personnel may find responsibilities greater and opportunities more challenging in such associations and that salaries should be increased accordingly.

Opportunities that merger may provide for developing and holding a second echelon or middle management group that would be ready to step into top management positions when needed should be examined.

Persons responsible for obtaining facts on merger should find out if additional services can be provided when cooperatives merge. This has special application to larger cooperatives. It may relate to a wide range of activities—for instance, specialists in membership and public relations; more effective accounting services, including opportunities for mechanized accounting; specialists in employee training, credit control, and personnel; and a research staff.

3. *Operating Practices.* Basic in evaluating any plan for merger is the influence such action may have on business operations. The following questions, while far from all inclusive, are suggested as illustrating those cooperative personnel will want to consider in appraising the desirability of merger.

a. If joint action is contemplated, which of the various forms—merger, consolidation, or acquisition — is the most feasible? For example, to what extent will such matters as the nature of the various economic forces bearing on a proposed merger, the objectiveness of directors and managers, the understanding of members, and the availability or lack of availability of competent personnel and adequate facilities dictate which course of action may be taken to greatest advantage?

b. To what extent do differences in methods of operation influence possibilities for merger or improve opportunities for such action by introducing flexibilities in operating business practices? Possible differences in pooling and pricing practices serve as a case in point.

When the farmer of tomorrow considers merger of his cooperative, he will want to know whether or not it would be more effective in providing at lower cost the various basic production supplies and services these farmer members need.

c. What will merger mean in terms of serving both large and small farmers

as well as farmers engaged in varying types of operations?

d. Will merger contribute to increased bargaining power? This might well involve consideration of questions about the influence of larger volumes on new and more lucrative market outlets for associations handling farm products. Will merger enable an association to more effectively provide the kind and quality of farm products desired by new and changing markets? To what extent would merger enable a cooperative to take advantage of the interest of some larger buyers who want to establish business relations with a firm known for its dependable products?

e. Closely related to bargaining is the desirability of determining the impacts of merger on opportunities to more effectively integrate operations in the interests of farmers.

For marketing cooperatives, this may well mean exploring opportunities for performing additional business functions—assembling, storing, standardizing, financing, and the establishment of central sales agencies.

For farm supply cooperatives, it relates to determining whether or not they could go back toward the sources of raw materials—for example, to providing a mine-to-farm fertilizer program and to exploring for crude petroleum and refining petroleum products.

Likewise it should be determined if merger would enable cooperatives to meet the growing needs for farmers for such services as insurance, credit, transportation, and a wide range of related farm business services.

f. Will merger offer opportunities for greater diversification of operations? Is the cooperative prepared to face up to these changes and can their impacts be dealt with to benefit members? Is greater diversification urgently needed if cooperatives are to serve members effectively in the area concerned?

g. Merger also may considerably influence transportation charges as well as location of facilities. Farmers, for example, will want to determine what effect merger may have on how and where processing, warehouse, or farm supply distributing units will operate. Similarly they will want to examine the possible effects of merger on such items as hauling and delivery charges.

In summary, the final test is: Will well planned and carefully worked out merger arrangements provide farmers with an opportunity to increase their income through more effective business performance on the part of their cooperatives?

Findings of Farmer Cooperative Service suggest that in most instances merger is in accord with the needs and trends of the time. Businesses are much larger, operating technology has changed, and improved techniques and procedures on management are available to cooperatives.

It cannot be too strongly emphasized, however, that each individual merger presents a separate and special situation. In arriving at the right decision it will be useful for cooperative leaders to approach their decision by getting all the facts possible to help them answer the many and varied questions dealing with the likely impacts of merger on: (1) Use of facilities, (2) use of personnel, and (3) operating practices.

Merging Cooperatives –The Human Equation

by IRWIN W. RUST

Farmer Cooperative Service.

JOINING together two or more firms involves an effort to make the best possible use of three classes of resources—physical, financial, and human. Human resources, the focus of this particular article, include the farmer members, the employees and directors of the firm, and the community in which the firm operates — in essence, the general public.

The human resources of a farmer cooperative may be considered "publics." Among these are many special groups such as members, employees, customers, firms which supply or serve the cooperative, competitors, and other groups in the community, all of them affected by the cooperative in some way.

All of these publics are—or *should be* —part of the human resources of a cooperative. Success in dealing with them is a major key to success in joining together two or more firms by merger, consolidation, or acquisition.

Achieving the greatest effectiveness in the use of human resources calls for knowledge of laws governing human behavior and application of that knowledge through all available channels of communication.

This poses problems. What are some of these problems, and how may they be solved? Answers to some of these questions will be considered under three main headings: Member relations, employee relations, and public relations.

Member Relations. — Observed by many of us who are concerned with cooperative mergers are such membership problems as pride of identity; giving newly acquired members proper and proportionate representation in the new organization; expecting too much of the new organization; overcoming long-standing rivalries between groups being merged, and encouraging member participation in the new organization.

Solutions to membership problems lie in: (1) Careful advance planning; (2) foreknowledge or anticipation of what problems may arise; and (3) building and maintaining good communications.

These solutions must be tailored to fit the particular situation. The ideal would be to anticipate problems before they arise and take steps to avoid them. But such actions need to be based on experience. Following are some examples of actual experiences of cooperative leaders who have been involved in merger actions:

Pride of Identity.—"In certain parts of our area," writes one man, "there is an acute need to consolidate the operations of small dairy plants which appear to face future difficulties. These difficulties stem from the current trend in the dairy industry toward large volume manufacturing units.

"Despite this pressing need, very little progress has been made in the consolidation due primarily to: (1) Resistance to loss of identity; (2) reluctance to close down plants; and (3) competitive history among the plants.

"We have noted that consolidations are worked out with greater success between a centralized drying plant and one of its member associations. Usually there has been a working relationship between the two and the transaction to merge operations is a gradual one.

"Sometimes the problem of loss of identity has been overcome by having the operations merged but the member creamery continue as a member cooperative for the sole purpose of paying the local employees and keeping the books and records. After a period of time it is likely that this function will also be taken over by the central plant."

Giving Proper Representation. — Virtually all cooperative leaders agree on the necessity for careful advance planning so that all of the members of the firms being merged are properly represented in the new organization. From the standpoint of human relations, proper representation means a plan that the members believe is fair and reasonable to them.

Expecting Too Much of a New Organization.—This has been a perennial problem with cooperatives. The answer to this problem is obvious—not to overpromise during the discussions of the proposed merger.

Overcoming Long-Standing Rivalries. —This situation is apt to confront many cooperatives seeking to join forces for more effective action. When cooperatives are small and situated relatively close together, it is not uncommon for two or three cooperatives to solicit the patronage of the same farmer. Faced with the need to merge, managers and boards of directors of cooperatives which have long been rivals suddenly find they must sit down at the same table with their former rivals.

These comments by the manager of a local farmer cooperative emphasize the problem: "There are three small cooperatives in this immediate vicinity. Our cooperative is the largest, the two others are somewhat smaller. A 12-mile circle would encompass the three of us.

"As manager of our cooperative, I believe that a merger of all three would be for the common good. Due to personality conflicts, however, I feel that it would be better for the suggestion to come from outside. Would it be possible for your agency to survey the situation and determine whether or not this suggestion has merit?"

An FCS representative visited the three cooperatives in question and, at a joint meeting of the three boards of directors, discussed some of the factors involved in a merging operation.

Sometime later we received the following letter: "From all indications, it appears that our efforts have been in vain. One of the three associations has decided to close down and release its members. The other two associations seem intent upon going their separate ways. The conflict of personalities which you noticed and talked about is too great a hurdle for us to jump."

Encouraging Member Participation.— One of the best devices for cementing loyalty between a member and his cooperative is to put the member to work. Businessmen's service clubs recognize this fact and use it to advantage by putitng new members immediately to work on some club activity. In the same way cooperatives need to encourage member participation, particularly cooperatives which have just gone through a merger.

One writer in commenting about the necessity for strengthening membership participation has this to say: "We have long recognized that when total membership of a given organization has expanded through a merger process, there has been encountered an increased demand for membership relations education work. It is imperative that members of the new organization be kept fully informed regarding the operations."

Employee Relations. — A second merger problem encountered by those who have actually assisted cooperatives in joining involves personnel. Among personnel problems arising most frequently in merger actions are the following: (1) What to do with excess personnel; (2) what to do when employees face loss of status; (3) how to secure employees' loyalty to the new firm; (4) what to do about community status.

What To Do with Excess Personnel. —Some of those who have guided a cooperative merger feel there is no completely satisfactory solution to the problem of displaced personnel. However, others are not so pessimistic and indicate a number of things which can be done. Among devices for solving the problem of excess personnel, the most important is to plan a long way ahead of the actual merger. In this way uses can be found for many employees.

A second device is to make use of normal attrition. As employees leave the organization for one reason or another, jobs can be closed out or consolidated with other jobs. Another device to take care of employees no longer needed is to give them plenty of advance notice. If possible, it is well to try to find them other positions in the community.

In commenting upon this particular aspect of mergers, one cooperative leader feels that there is no problem. According to him, "In the mergers which have successfully been accomplished and in which we have played some part, personnel problems have seemed to solve themselves. This may be explained by the fact that in those instances where mergers have been accomplished it has been a case of a stronger cooperative taking over the assets and liabilities of a weaker cooperative.

"The managers of these weaker cooperatives have realized that their alternatives were either acceptance of a minor position with a stronger and continuing operation or sooner or later being without employment because the weaker cooperative had ceased to operate. Since the weaker cooperatives involved in each instance have been ones in which personnel had already been reduced to the minimum, there has been no concern other than with the manager. Managers in each instance have been retained as managers of the existing stations. Other employees have likewise been retained in most instances. Personnel problems have then been solved by applying the same personnel policies which have been the policies of the stronger organization."

In one instance, top employees of several cooperatives being merged into a large, strong cooperative were guaranteed employment for at least 1 year following the merger. The agreement was that at the end of the year those who fitted into the new program would be retained. Those employees who, for one reason or another, did not find a place for themselves in the new organization would be released.

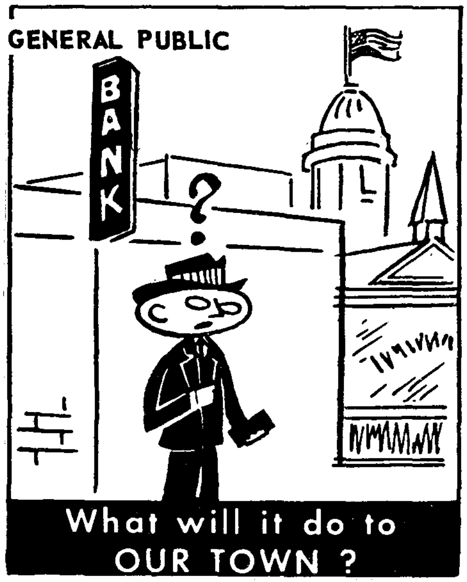
Another writer commenting on the same subject observes: "In most instances I believe that the employees of the smaller cooperatives have benefited both as a result of assured continued employment as well as increased compensation and other employee benefits usually extended by stronger cooperative organizations."

Loss of Job Status.—In some cases of mergers where declining or smaller organizations join with stronger organizations, employees of the smaller association may lose job status in the merger. In these cases the best solution is a good strong personnel program with all that that implies. This would include such activities as inservice programs to teach employees about the firm which employs them, sundry fringe benefits which large organizations usually provide, and a good membership publication through which the employee has an opportunity to learn about his organization.

Developing Employee Loyalty. — A problem often met following a merger is that top personnel of smaller associations fail to develop strong loyalty to the new firm. Here again a good personnel program has been found to be useful.

Loss of Community Status.—Community status, particularly in small towns, can be extremely important to an employee. It is one thing for a man to be the manager of a local association; it is quite another thing for the same man to become the manager of the local unit of a large organization whose head office may be several hundred miles away. This very fact in some cases may influence the attitudes of key employees toward a proposed merger.

One writer discussing this point has this to say: "Some observations have been made recently of the fact that personal opinions of managers of existing cooperatives may have an undue influence upon the decision of directors and cooperative members to act favorably upon merger proposals. We believe that this situation is one of major importance where producers in a given county, for example, may be considering the desir-



ability of merging two or more cooperative associations which may be operating quite satisfactorily under present management."

Public Relations.—The third major problem area involving cooperative mergers concerns community or public relations. It is imperative that the newly merged firm earn community acceptance by the manner in which it conducts its affairs, the services it performs, the degree to which it accepts community responsibility. A new firm, even in an old location, is a new face in town. Public acceptance of the new firm does not come automatically, but must be earned.

As an example of what may happen if public relations have not been considered, note the following comment from a man who participated in many successful mergers: "In general, the mergers that were consummated were worked out very satisfactorily. However, in one case involving a large diversified cooperative which absorbed five smaller cooperatives through individual acquisitions, the lack of planning resulted in a weakened organization and an unsatisfactory operation. This situation was due in part to the fact that the new organization did not plan its post-merger operations to gain operating efficiency from the merger. In addition, there was no attempt at educating members during the crucial integration period. Most of the activities were made with the understanding that the local plant would continue operating.

"Subsequently, when the new organization attempted to close plants and operations, it met considerable resistance from town people in that locality. Community factionalism soon became apparent on the new board of directors, with the result that board members were more interested in promoting the improvement of their own local plants than strengthening the overall organization. Accordingly, although these six cooperatives are now legally one, the job of integrating overall operations and attempting membership unity remains to be done."

Throughout current thinking about cooperative mergers there runs a single thread—that one key to successful merging is careful attention to human relations and to good communication with directors and members.

Perhaps this is best explained by the following comment: "In connection with our work with cooperatives involved in merger negotiations, we have noticed the difficulty boards of directors frequently have in understanding the overall factors involved. Frequently the goals of maximum returns to the farmer and the need for a stronger organization are lost sight of and attention is focused on items of little economic importance to the farmers. Since the membership of a cooperative usually follows recommendations of its board of directors, the board members are frequently one key to successful mergers and should be well informed on the overall and long-range benefits that can be achieved."

A fitting close to this article is the following comment on the value of an effective educational program: "It has been our observation that in those instances in which mergers have been completed, there has been conducted as a part of the merger procedure the necessary educational work among members which led them to accept the merger as being a desirable action. *In most cases membership relations among those members who were original members of the smaller cooperative have been improved.*"

Financial Problems and Procedures in Merger

by David Volkin
Farmer Cooperative Service.

THE end product of a cooperative merger, consolidation, or acquisition is an expanded set of assets, a realignment of liabilities, and an enlarged group of owners of the business.

A lot of time, money, and effort is saved if balance sheet values of a certain date are acceptable as a basis for merger. If all parties concerned *want* to merge, all that then is necessary is to proceed through the various steps required by the statutory provisions of the State or States in which these organizations are located.

But in actual practice there may be understandable reluctance to accepting balance sheet values as the basis for combining. The reasons for this reluctance are primarily these: Transactions may not be accounted for on the same basis; the *nature* of the assets being acquired must be determined accurately; and future operations may be affected by information obtained by accountants and appraisers.

Specific situations give rise to a wide gamut of financial problems of three general types. These are:

a. Valuation of assets.

b. Payment for these assets.

c. Financial strength of the new organization.

Valuation of Assets.—Under the first category—valuation of assets—there are these questions or problem areas.

1. Have accounting systems of the cooperatives adequately reflected operating results?

2. Have accounting systems adequately reflected financial conditions?

3. What adjustments are needed to attain the greatest degree of comparability between financial statements of the respective associations?

4. Who will appraise the value of the assets?

5. If negotiating associations hold to the belief that "good will" is transferable and should be paid for, how should the value of this asset be determined? On the earning power of the tangible assets? On the physical volume produced? On efficient use of resources of production? On some combination of these bases? Or on bases totally unrelated to book value, earning power, physical volume, or efficiency criteria?

6. Will the merger involve acquisition of all assets, or will those of little or no utility be excluded?

7. Will all liabilities be assumed, or will some be excluded because of especially unfavorable terms and conditions?

The usual picture in mind when the subject of merger comes up is that of a financially weaker association merging with a financially stronger one. The stronger association then acquires all the assets of the weaker association and assumes all its liabilities. The equities of the weaker association which, by simple arithmetic, are equivalent to the excess

of the total assets over the total liabilities, are "traded in" for cash, or for equities of the stronger association—or a combination of both. Under such circumstances, the weaker association, by agreement, ceases to exist and the stronger association is the surviving association.

A rather curious but nevertheless practical situation arises where there is a weaker-stronger co-op merger situation. Non-financial trumps somehow seem to be held by the weaker association in many cases. There is an understandable tendency to overlook poor performance, operational or financial wise—to go easy on exacting the last pound of flesh.

But ordinarily it seems only sound business to make the financial settlement on the basis of a sound appraisal. It is at this point that what originally are academic figures on a balance sheet now come alive with real meaning. How good is each and every receivable? Is the inventory properly classified, enumerated, and priced, taking into account its future saleability? Is there any merchandise on a consignment basis? Are notes current?

Should negotiators accept the depreciated value of fixed assets as the fair value? What methods were used to depreciate the fixed assets? Straight-line? Physical output? Reducing fraction? In this inflationary period, professional appraisers generally come up with fixed asset values somewhat higher than net book value. The reason for this is that they generally appraise on the basis of replacement cost less straight-line depreciation back to the date of acquisition or installation. In addition they may make an adjustment based on their own experience to take physical condition into account.

Now turn to investments. Generally they arise as a result of patronage with other cooperatives. Somehow there seems to be a disinclination to accept these at their face or par value. Some cooperatives want to have these accounts turned into cash. Except for those cases where there is a clear-cut and documented impairment, these should be valued at par and endorsed or assigned over to the surviving organization without adjustment. It should also be clearly ascertained that there is no prior lien or attachment on these investments that may be unrecorded.

For that matter, are there any other unrecorded assets? Are there any contingent liabilities, pending litigations, or contractual arrangements that are unrecorded in the balance sheet except perhaps as footnote comments?

Payment for Assets.—Going on to problems associated with payment for the assets, cooperatives become involved in these areas:

1. In what form shall payment be made—cash, stock, notes, debentures, book credits, certificates of interest?

2. If part or all of the payment is cash, should it be a lump sum payment or spread over a period of years?

3. On what basis is financial settlement made to stockholders or other holders of net worth who object to merger?

4. How are settlement values to holders of certificates of indebtedness of differing maturities determined; to holders of stock of different par values; of different preferences; and of reserves allocated to individuals over such a long period of time that there is a real problem of locating them?

5. How are financial settlements between associations having different equity redemption policies decided? Will patrons of an association redeeming patronage certificates on a 5-year program, for example, be willing to exchange their capital holding for equities of another association having no serial redemption program—or no policy for redemption of equities held by estates or those who have terminated their memberships?

6. Is there anything in the organization papers of the association to be dissolved concerning the distribution of capital gains or losses which may create serious obstacles to merger?

Assuming negotiators have arrived at what appears an acceptable figure on which to make financial settlement, let's look into the manner in which distribu tion to the dissolving association's patrons will be made. Do the organization papers provide for pro rata distribution based on patronage, on book value of outstanding capital stock, or on membership?

Imagine the obstacles to merger created if a relative handful of members —most of whom have possibly not patronized the association in recent years —fall heir to a capital gains windfall if settlement is related to membership only.

The important point to be remembered is this: That although a satisfactory financial settlement for the assets may be agreed upon, if the manner of distributing them creates legal and membership problems — the nature of these problems should be ascertained early in the negotiations.

Perhaps changes in bylaws can be effected. Perhaps partial liquidation of certain of the association's assets may be necessary in order to settle capital equities held by certain patrons. Or perhaps the best features of revolving plans in effect should be retained and incorporated into the financial structure of the merged organization.

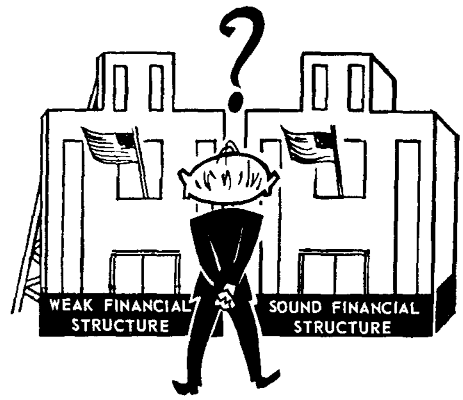
But in any event those individuals closely concerned with the merger should anticipate the internal financial problems of the individual association in the matter of distributing cash or equities incident to the financial settlement resulting from merger.

Let us next discuss the *form* of financial settlement.

Shall equities distributed by the surviving association be in the form of common stock, preferred stock, certificates of interest, reserve book credits? Should there be any difference in treatment between those equities for which members and patrons paid cash and those distributed as proportionate shares of net margins?

Perhaps the easiest solution would be to make settlement in cash equivalent to the par value of the outstanding equities for which members originally paid cash.

But before reaching this decision, certainly these factors should be considered: Can the newly formed (or surviving) association afford a reduction in its working capital by a cash settlement? Are most of these particular equities held by still current members? And will a more adverse membership relationship problem be created by such a selective cash settlement?



The *form* of equities can assume an exaggerated importance when rate of dividends or other special benefits of an immediate monetary effect are their prime characteristics. If dividends or other benefits *are* the most important characteristics of equities, then they really become more of the nature of investment for profit rather than evidence of capital furnished by members as producers.

Returns to members as *producers*—not as investors—are the basic reason a farmer makes an initial capital outlay. This is furthermore demonstrated by his willingness to enter into a contractual arrangement for reinvestment of capital from his proportionate share of the overages resulting from operations.

When equities are exchanged in a merger procedure, the capital structure can be simplified. One suggested method is to distribute one share of common voting stock to each eligible member and the remaining equities in some form of allocated reserve that retains its original order of redemption.

Consider now the financial structure of the newly formed organization. Cooperative members as owners and users must realize that long-term capital supplied by creditors to finance continuously increasing levels of operations or to finance the purchase of fixed assets should eventually be replaced by member capital. Conventional sources are retains, reinvestment of net savings, and outright purchase of equities.

If cooperative financing becomes investor-oriented or creditor-oriented, some measure of control will be sacrificed. And the extent of that loss of control could be in direct proportion to the amount of non-member non-patron capital introduced into the financial structure, especially if it reached a substantial proportion of the total.

Most cooperatives never reach a 100 percent equity goal nor, in fact, do most of them intend to. It would certainly seem impractical in a highly seasonal business for an association to have sufficient working capital of its own to finance large short-term needs.

But the point is that those involved should not sell the idea of merger with promises of great financial gain or accelerated redemption of equities. Rather, they should stress the importance of attaining a sound financial postion so the new association can perform the kind and type of services its members and patrons deserve and demand.

Projecting Financial Position.—The third category of financial problems—financial strength of the new association—deals with financial projections. These problems may be summarized as follows:

1. Will the newly formed organization provide for adequate financing to meet the demands of normal business and normal expansion?

2. If not, to what sources shall the new organization turn for additional financing?

3. When merger is consummated will the ratio of debt to equity capital be more—or less—favorable from a credit standpoint?

4. Will preferences or special terms and provisions that may be required as a prerequisite of additional financing needed by the new organization create any problems with holders of equities of component organizations before merger?

5. Will the newly formed organization be in a better position to obtain funds for working capital or expansion purposes than the *component* organizations individually seeking funds from the same sources?

6. Will the organization structure of the newly formed cooperative permit the preparation of separate financial statements on a parent-subsidiary basis, or on a division basis?

7. What projected operating results will be anticipated.

8. Who will be responsible for the assumptions to be made in projecting operations?

Negotiators of mergers have found it useful to project operations in statement form to show what management hopes to accomplish with the expanded resources. Such a projection helps them understand how anticipated changes in physical and dollar volume, cost reduction, shifts in or disposition of fixed assets, and other proposed operating efficiencies can result in increased returns to them.

Ideally, preparation of projected financial statements depends on collaboration and advice of economists, bankers, attorneys, marketing analysts, management, and operating personnel.

Those immediately involved with financial problems in merger negotiations are justifiably concerned that the ultimate effect of a financial settlement should not adversely affect the value of equities held by patron-owners in the capital structure of their respective organizations. Actually, there should be no real objection by the individual members and patrons of the association involved to the agreed upon financial settlements, if—

1. The form of equities distributed by the surviving or newly formed organization is simple and closely approximates the value of equities presently held by or allocated to them, and;

2. Patrons are convinced that the new organization will operate so as to assure them of top quality products and service at least equal to or better than those from their present organizations.

In Conclusion.—One thought should

be stressed: Each specific combination of cooperatives is surrounded by its own peculiar circumstances. If those involved in the negotiations do not stray too far from the basic concept that the new organization should be organized and financed to operate for the mutual benefit of its members as producers, then there will be a sound underlying basis for all the detailed financial analyses and projections which must be made in working out a *successful* merger.

Steps In Merging Cooperatives

by J. WARREN MATHER
and STANLEY F. KRAUSE

Farmer Cooperative Service.

PREVIOUS articles have indicated numerous areas to explore in bringing about consolidation or merger of two or more cooperatives.

These may have raised such questions as: How do you go about studying the various points? What steps or procedures do you take? Is timing of certain actions important? How do you best organize to bring about a merger—to avoid stumbling blocks?

Probably no two mergers have been achieved in exactly the same manner. There is certainly no one best way to fit all conditions. However, based upon our experiences, this article lists some of the more important steps many associations are following. For convenience, they are grouped into four stages.

The Idea Stage. — This is the seed planting and germinating stage. Some of the initial steps may be these:

1. *Directors and the manager of the initiating association informally discuss merger possibilities at board meetings.* This idea may grow out of the manager or directors hearing or reading about merger explorations or achievements by other cooperatives. They discuss in broad terms the need and possibilities for combining with one or more other cooperatives.

2. *Directors or the manager "feel out" the idea with the other cooperative or cooperatives.* If the board exhibits real interest, it may suggest and arrange for an exploratory meeting with directors and manager of the other association. More than one meeting may be necessary.

3. *Directors appoint a consolidation or merger committee.* If each cooperative reacts favorably, then each should appoint representatives to a joint study committee to examine all aspects of merger. Such a committee frequently consists of two or three directors from each association, with the managers or assistant managers as ex officio members. In actual practice, the manager can be very important in compiling information, exploring alternatives, and encouraging the directors.

The Study Stage. — The committee, working on its own and contacting other merged associations, may develop a satisfactory basis for merger action. A thorough study will examine all the various aspects involved—economic, financial, human, and legal phases of merger.

Frequently, however, merger committees and boards of directors desire help in studying various problems. For this reason, the boards of directors should specifically outline the authority of the merger committee to obtain outside assistance at the time the committee is appointed. Some assistance will require expenditures by the cooperatives, and some public agencies provide such assistance only at the specific request of boards of directors.

1. *Merger committee initiates study of merger proposal.* The first step is to outline the information required and areas

where recommendations must be made. Individual members or subcommittees may collect information on various phases, such as facilities, operations, or member equities, with the assistance of general managers and staffs of their cooperatives. Conclusions and recommendations are formulated where possible.

The committee should set up a timetable with target dates for various steps or reports to help assure action without undue delay.

2. *Merger committee requests needed assistance from public and private agencies.* Local cooperatives often can obtain assistance from agricultural economics staffs and extension marketing specialists of State universities. Other sources of help are State Departments of Agriculture, State cooperative councils, district banks for cooperatives, and regional cooperatives.

Regional cooperatives and a limited number of local cooperatives usually can obtain assistance in studies of merger possibilities from Farmer Cooperative Service, U.S. Department of Agriculture. Also, regional cooperatives can employ management consulting firms to assist in portions of the overall study.

3. *Merger committee reviews findings with agency making the study.* A report made by any of the agencies mentioned may be sent to the committee a week or two ahead of the meeting called for discussion of it. A suggested procedure for presenting and discussing the report, or reports, may be as follows:

First, the person making the study should present his findings orally to the merger committee;

Second, the representatives from each cooperative will then meet alone to determine points of agreement or disagreement with the findings;

Third, the committee will meet together again to share views and ask questions. Members may suggest alternatives to be examined.

The full boards of directors of the cooperatives may wish to sit in on the meeting when the outside agency reports to the merger committee. In this case it should be understood that the merger committee still has the responsibility of completing its study and making recommendations. This may vary from complete acceptance and endorsement of the agency report to modification or even rejection of it.

The merger committee may require several hours or more to hear and discuss the report of an outside agency. In most cases, however, all three steps proposed above may be completed in one day and evening.

4. *Merger committee completes its study and prepares recommendations.* Two or more rounds of study requiring outside assistance may be needed, and there may be many meetings of the merger committee.

The completed study should include a detailed examination of possible benefits in terms of savings, efficiency, and service; a basis for merger that is equitable; and also consider problems, possible points of conflict, and limitations of various kinds.

The Proposal and Compromise Stage. — This is the stage where open minds, sincerity, and statesmanship must prevail if the interests of members are to be served. Willingness to compromise may mean the difference between a merger and no merger. Neither cooperative involved, especially the largest and strongest, should insist on the "last pound of flesh"—for example, the exact appraised value of the assets or the book value of the capital stock. The largest cooperative, however, can afford to be generous to bring about unification.

1. *Merger committee reports to boards of directors.* This report should be at a joint meeting of the boards of directors. This will provide an opportunity for the leader in each area of study to present his report, and for oral reporting by outside agencies that helped the merger committee. The same steps may be followed as in the merger committee hearing reports of outside agencies: First, a joint meeting; then, separate executive sessions; and third, a reconvened joint meeting.

Agreement on basis of merger may then be reached by boards of directors. It is desirable that all the directors of each cooperative support the proposals; but if this is not possible, at least two-thirds should approve.

2. *Merger committee prepares a written proposal for merger.* The merger committee should outline the basis for merger accepted by boards of directors of the cooperatives.

3. *Attorneys prepare agreed-upon merger proposals in legal form to submit to the members.* Also, explanatory notes may be desirable. Laws of some States require signature of a merger agreement by boards of directors.

The Member Approval Stage.—This might be called the membership information and voting stage. Steps include the following:

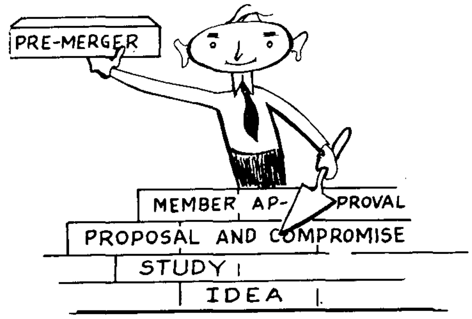
1. *Directors of each association call a special meeting of members to vote on the merger.* Mail ballots usually are necessary to obtain the required proportion of votes under State cooperative laws. A full and clear explanation of the proposals should be sent to each member.

2. *Directors of each association strongly urge approval of the merger proposal.* After directors have voted to recommend a consolidation or merger, they should actively support the idea. While a merger proposal should be presented objectively and not oversold, some forceful action by directors usually is necessary to get it approved by members. Local informational meetings ahead of the meeting calling for voting on the merger may be desirable. Articles for member publications and special letters may be used.

Ample time for discussion should be provided at the special meeting. Both the pros and cons should be presented, but it should be clearly evident that probable advantages will outweigh disadvantages.

3. *Notification of the completed merger is sent to the proper State officials.* Changes in charters or articles of incorporation are handled by the Secretary of State in most States.

Pre-Merger Coordination. — Frequently a satisfactory agreement for merger is not reached in the first attempt by directors or members of the



cooperatives. When progress is slow and the study or member approval steps as outlined are interrupted before completion, one of the following plans may be considered:

1. *The two cooperatives may develop contractual arrangements for coordinating or unifying operations.* This might include all operations or just one phase such as joint use of one plant or of certain personnel. This arrangement will give the cooperatives a chance to try out coordinated operations. If it works, plans can go ahead for merger and farmer members will have gained benefits from one or more years of unified operations.

Coordinated business arrangements can be established by the directors through contractual agreement without time-consuming efforts to gain approval of members.

2. *The two cooperatives may set up a third cooperative to perform some of their services.* This procedure is more likely among regional cooperatives. They may, for example, decide to use it to bring about unified operations of one fertilizer plant or of one milk manufacturing plant. This method could also be used to unify all operations of the two associations. If this proved satisfactory the two associations could dissolve; such procedure technically would be known as a consolidation rather than a merger.

However, if unification was not satisfactory, the associations could resume individual operations with their same corporate structures.

3. *The larger association may offer to buy either the assets or capital stock of the smaller association.* This technically

is known as an acquisition rather than a merger. It frequently occurs among local cooperatives. Under some State laws it may be accomplished easier and faster than a merger.

Hazardous Hurdles.—It seems important to emphasize that leadership must avoid dissipating detours and be prepared to overcome obstinate obstacles. Some of the things which can cause negotiations to falter or break down at an early stage are:

1. *Premature release of information.* It is desirable that the committee and directors work with discretion and release publicity jointly and only with consent of the entire committee. Also, such releases should cover only the facts that studies are underway and any plans that have been definitely formulated. We suggest informing members of the studies underway, because many of the members are likely to learn of this through word of mouth anyway. A little information provided early may avoid the spread of damaging controversy and inaccurate rumors.

2. *Too early discussions on the role or assignment of employees—especially the managers.* Tentative selection of the manager and other employees for the proposed merged association can easily upset personnel in each organization, divide directors, and break down objective discussions. Only the new board of directors of the merged cooperatives can appoint the manager.

3. *Too early discussions of a new name for the unified association.* This can detour directors off the main track and use considerable time at meetings.

4. *Untimely discussions on closing plants and stations or altering services in the area served by the smaller cooperative.* Directors and employees must use judgment and timeliness in discusssing possible effects of a merger on the services and operations of the two associations. Rumors among members soon become greatly exaggerated.

5. *Over-emphasis on immediate savings to the cooperatives rather than probable long-term benefits to farmer-members.* Committeemen and directors should strive to keep discussions on the basic question: How will a merger strengthen and improve services to farmer-members?

* * *

So we can see many stages or steps in completing merger plans. Some of these are overlapping. The timing and sequence may vary, but at some time during negotiations the boards and managerial employees will be involved in the stages just discussed—idea, study, proposal and compromise, and member approval.

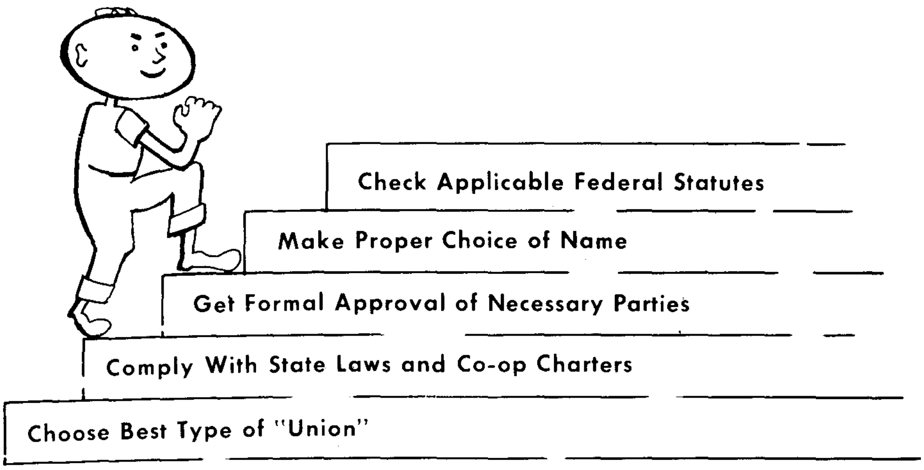
Legal Problems Involved in Mergers

by Elmer Mostow
John F. Donoghue
Raymond J. Mischler

Office of the General Counsel.

A cooperative planning the acquisition of, or a merger or consolidation with, either another cooperative or another type of organization confronts legal problems. These involve both State and Federal laws. Many of the problems are peculiar to the particular action. These problems require particularized consideration by management and its attorney. Following are some of the basic legal considerations.

Technically, a consolidation is a



union of two or more organizations which results in the creation of a new association and the termination of the organizations involved in the consolidation. A merger, on the other hand, constitutes an absorption of one association by another which retains its corporate identity. A mere purchase or acquisition of an organization's assets by another association does not necessarily constitute a merger or a consolidation. However, in some instances such a purchase is, at least in effect, a consolidation.

A consolidation or merger must comply with State law and the charters of the organizations involved. When an association plans to sell its assets, its directors and those of the buyer must agree upon the terms and conditions of sale. Generally there must be statutory authority for such a sale and agreement of the members of the selling company. Also, the articles of incorporation and provisions in the bylaws must be considered in each case. Usually the purchasing company requires neither statutory authority nor member authorization to acquire the assets of another association.

Consolidation or merger action is valid only when authorized by State statute or by the charters of the organizations involved. In many States, mergers and consolidations of agricultural cooperatives are governed by general corporation statutes. In some States there may be special statutes dealing specifically with mergers and consolidations of agricultural cooperatives.

When contemplating a merger or consolidation, a farmer cooperative faces the same questions for consideration as other corporations. However, since cooperatives provide more democratic control by the patrons than other types of corporations, such control may pose additional problems . Nevertheless, the procedure is often the same. Scant written material is available regarding mergers by farmer cooperatives; but articles, textbooks, and other literature pertaining to corporate acquisitions, mergers, and consolidations are extremely helpful.[1]

Plans and agreements for a proposed merger are usually prepared and then resolutions approving the agreements affirmed by each board of directors involved. Members of each organization then vote on adoption of the agreement, which must be accepted by a proportion of the members ranging from a simple majority to a three-fourths majority. Statutory provisions covering rights of dissenting stockholders, if any, must also be studied carefully.

The agreement usually must be signed and acknowledged by appropriate offi-

[1] 15 Fletcher, Cyclopedia of the Law of Private Corporations, Sec. 7040-7199 (1938 replacement). See Packel, *The Law of the Organization and Operation of Cooperatives*, 120-121 (2d ed. 1947), and cases cited therein

cers of each of the organizations. Frequently, when the agreement is for a consolidation, it must contain those provisions required to be stated in the articles of incorporation.[1] Thus the agreement also serves as the basis for the articles of incorporation of the new corporation. When the agreement is for a merger, it is the usual custom to set forth therein the articles of incorporation of the surviving corporation amended as the result of the merger. Statutory provisions for the form and content of the agreement for merger must be complied with.

Where a consolidation is contemplated and a choice of effecting the consolidation in one of several States is available, laws of those States should be consulted. Consolidation under the laws of one State may be more advantageous than under the laws of other States, assuming that geographical and economic conditions do not outweigh these advantages.

When associations desiring a consolidation are organized under the laws of different States, it is necessary to determine whether the statute of the State where the consolidation takes places permits a consolidation with an association of another State and, if so, whether the consolidation statutes of the two States are sufficiently reconcilable with one another that there will be no hopeless conflict of procedure.

Selection of a name for the new organization should be carefully weighed. There are some States in which a cooperative organized in some other State and having the word "cooperative" in its name may not do business as a foreign corporation. The reason is that in some States the cooperative statute prohibits the use of the word "cooperative" by any corporation except one organized under that statute. Thus, when a cooperative has incorporated in a State which makes the use of the word mandatory it sometimes finds it cannot be admitted to do business in certain foreign States.

One apparent choice for a cooperative desiring to do business on a national basis is to incorporate in a State which does not require the use of the word as a part of the corporation name, and then adopt a name which does not include the word "cooperative."

Whether a marketing contract should be used and, if so, what sanctions should be put in it can involve legal as well as management decisions. Care must also be taken in selecting trademarks and trade names. State blue sky laws and antitrust laws should also be consulted and a study made of ways to minimize State taxes.

Although the authority to incorporate or effect a merger is provided by State laws and the procedure to be followed is governed by these laws, Federal laws also may apply. The most significant of these laws are the Federal antitrust laws and the tax laws.

Economic ramifications of the proposed action with respect to the antitrust laws should be explored. If the proposed action constitutes a violation of these laws, it must be abandoned or at least modified. Pertinent antitrust laws are Sections 1, 2, and 3 of the Sherman Act and Section 7 of the Clayton Act (15 U.S.C. 1–3, 18). Certain exemptions therefrom are provided by Section 6 of the Clayton Act, the Capper-Volstead Act, and Section 5 of the Cooperative Marketing Act of 1926.

The Sherman Act declares illegal every contract, combination, or conspiracy in restraint of trade and monopolies of, or attempts or conspiracies to monopolize, any part of the trade or commerce among the several States or with foreign nations. Section 7 of the Clayton Act prohibits a corporation from acquiring the stock or assets of another corporation where the effect of the acquisition may be to substantially lessen competition or tend to create a monopoly.

Despite the sweep of the language of these statutes, not all acquisitions, mergers, and consolidations are prohibited. Special statutory recognition of cooperatives is provided in Section 6 of the Clayton Act, the Capper-Volstead Act, and perhaps by Section 5 of the Cooperative Marketing Act. Section 6 of the Clayton Act declares that the antitrust laws shall not prohibit the existence and operation of nonstock agricultural and horticultural organizations. The Capper-Volstead Act, enacted in 1922, in effect, extended the scope of the Clayton Act to include stock corporations as well as nonstock corporations, but it requires a cooperative to meet certain requirements in order to obtain the benefits of the Act. That Act also provides that an association of agricultural producers may act together "in collectively processing, preparing for market, handling, and marketing in interstate and foreign commerce" products of its members, that "such associations may have marketing agencies in common," and that they "and their members may make the necessary contracts and agreements to effect such purposes. . . ."

Holdings of the Supreme Court of the United States make it clear that a cooperative qualifying under Section 6 of the Clayton Act and the Capper-Volstead Act is not immune from prosecution under the antitrust laws. A cooperative which enters into a conspiracy or combination with a noncooperative party in restraint of trade is subject to prosecution. Care must be taken to avoid such a situation.

Of particular interest to this discussion are several recent statements of the Supreme Court. These statements furnish some guides in determining the permissible and prohibited areas in mergers and acquisitions:

"We believe it is reasonably clear from the very language of the Capper-Volstead Act, as it was in section 6 of the Clayton Act, that the general philosophy of both was simply that individual farmers should be given, through agricultural cooperatives acting as entities, the same unified competitive advantage—and responsibility—available to businessmen acting through corporations as entities." (362 U.S. 466)

"This indicates a purpose to make it possible for farmer-producers to organize together, set association policy, fix prices at which their cooperative will sell their produce, and otherwise carry on like a business corporation without thereby violating the antitrust laws. It does not suggest a congressional desire to vest cooperatives with unrestricted power to restrain trade or to achieve monopoly by preying on independent producers, processors, or dealers intent on carrying on their own businesses in their own legitimate way . . ." (362 U.S. 466, 467)

"But even lawful contracts and business activities may help to make up a pattern of conduct unlawful under the Sherman Act. The contract of purchase here, viewed in the context of all the evidence and findings, was not one made merely to advance the Association's own permissible processing and marketing business; it was entered into by both parties, according to the court's findings as we understand them, because of its usefulness as a weapon to restrain and suppress competitors and competition. . . . We hold that the privilege Capper-Volstead grants producers to conduct their affairs collectively does not include a privilege to combine with competitors so as to use a monopoly position as a lever further to suppress competition by and among independent producers and processors." (362 U.S. 471, 472)

It is clear, therefore, that the acquisition of a non-cooperative entity by a cooperative with the *intent* and *effect* of restraining trade is proscribed. In view of the language of Section 7 of the Clayton Act, it would appear to be necessary to point to some exemption from that section to immunize such an acquisition made with a legitimate intent but with the effect of restraining trade.

If the cooperative is in interstate commerce, this means that it will have to consider the effect that a proposed merger or asset acquisition will have on the competitive factors in the market or markets in which the cooperative and the to-be-acquired firm or firms make most of their sales.

The fundamental points to keep in mind are: (1) That mergers or acquisitions are precluded only where there is reasonable *probability* that a *substantial* lessening of competition or a monopoly might result within an area of effective competition, and (2) the market affected must be *substantial* and it must appear that competition may be foreclosed in a *substantial* share of that market.

Accordingly, if a cooperative acquires necessary facilities for business use through methods legally sanctioned and the acquisition does not have the prohibited effect on competition, it is believed that the provision in the Capper-Volstead Act would furnish support for the acquisition.

It has been suggested that in view of the language of Section 1 of the Capper-Volstead Act, a qualified cooperative "may have more freedom in the acquisition of assets than an ordinary business corporation."[2] This appears particularly true where the merger or acquisition involves only qualified cooperatives. Cooperatives may federate and have marketing agencies in common,[3] and, therefore, the extent to which consolidations among cooperatives would substantially lessen competition or tend to create a monopoly would in many instances be problematical.[4]

On the other hand, a word of caution. The Department of Justice has consistently emphasized the position that Capper-Volstead confers no blanket immunity upon cooperatives and that except for the collective action specifically sanctioned by Section 1 of the Act, they are accountable under the antitrust laws as other forms of business.

Therefore, counsel for a farmer cooperative planning an acquisition, merger, or consolidation should consider submitting the matter to the Antitrust Division of the United States Department of Justice in order to obtain a "merger clearance" which will provide the parties involved with some assurance from the Department of Justice that the proposed action does not appear to involve a violation of the antitrust laws.

In some instances, the agreement for the proposed acquisition or merger contains a condition that such clearance will be obtained. However, note that persons alleging injury could still file an action for damages in the courts.

When planning an acquisition, merger, or consolidation, consideration should also be given to the Federal income tax laws in order to obtain all possible tax benefits.

If the organizations involved have qualified as exempt cooperatives as defined in Section 521 of the Internal Revenue Code and have in fact been operating as exempt cooperatives, the effect of the proposed action on their tax status must be considered and a determination made as to whether it will be affected by acquisition or combination.

Also, if one or more of the organizations have not qualified as an exempt cooperative, Section 521 should be consulted in an effort to decide whether or not the new or resulting organization can qualify thereunder as an exempt cooperative.

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[2] Stark, *Capper-Volstead Revisited* in American Cooperation 1960, 464.

[3] Report of the Attorney General's National Committee to Study the Antitrust Laws, 1955, p. 308; 36 Op. Atty. Gen. 326, 339-340 (1930).

[4] Saunders *The Status of Agricultural Cooperatives Under the Antitrust* Laws, 20 Federal Bar Journal 54 (1960).