

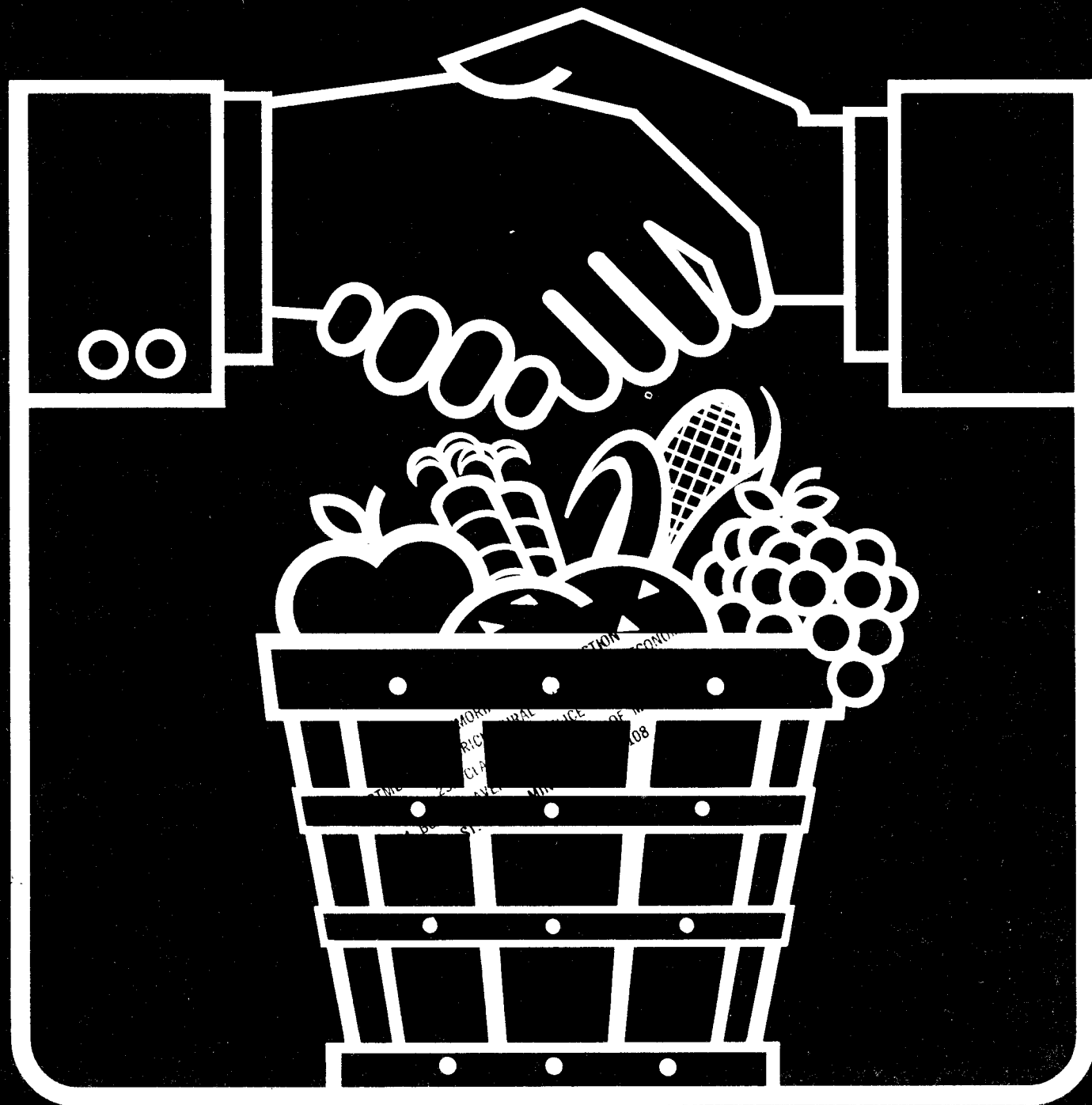
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United States
Department of
Agriculture

Agricultural
Cooperative
Service

ACS
Research
Report
Number 36

Working Arrangements of Fruit and Vegetable Processing Cooperatives



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Abstract

Organization and operations of nine working arrangements developed by fruit and vegetable processing cooperatives are described and evaluated. Three distinct approaches are identified — contractual agreement, affiliation through membership status, and formation of separate business entity. The specific structure and functions of joint undertakings reflect the needs and preferences of the participants. Benefits perceived in the cases cited included scale economies in processing and marketing, capital cost avoidance, product diversification, assured commodity supply, and enhanced market entry.

KEY WORDS: Fruit and vegetable cooperatives, joint ventures, contractual agreements, marketing services, processing services.

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Highlights

Working arrangements that extend or coordinate specific operations of individual firms are common in the business world. This study focuses on the application of that concept within the cooperative community. Nine recent agreements among cooperatives engaged in the processing and marketing of fruit and vegetable crops are examined.

Motivations for working arrangements are as diverse as are the participating organizations. In a sense, the strengths and weaknesses of the individual firms are mirrored by the joint activities they have developed.

Economic needs underlie the formation of all working arrangements. In the cases of the cooperatives included in this report, reasons for participation in joint undertakings centered on efforts to: (1) better utilize existing facilities and/or personnel, (2) avoid investments in additional plant and equipment, (3) assure reliable supplies of raw commodities for processing, (4) gain access to new markets, and (5) improve market position by broadening product lines. All arrangements were initiated with the expectation that they would ultimately impact favorably on net revenues.

Often several requirements or concerns of the participants were addressed in a given venture. In all cases, however, only after considerable study and negotiating to ensure the needs of each was a joint activity initiated. For example, the excess processing capacity of the Keystone organization could be drawn upon to supplement the facilities of Welch and Ocean Spray. The needs of Willamette Cherry Growers, Rogue River Packing, and Michigan Blueberry Growers' cooperatives to strengthen their sales programs led to affiliations with other associations. Plant and equipment owned by Carolina Apple Producers and Ag Mor formed the bases for the linkages with Red Cheek and Pacific Coast Producers — two cooperatives with management experienced in operating processing facilities and marketing finished products.

In most cases, working arrangements are conceived by the managements of the organizations involved. It is the responsibility of cooperative management to plan, conduct, and control operations so that returns to association owner-patrons will be maximized. In this context, it would be expected that identification and implementation of joint venture opportunities would rest with those intimately familiar with industry problems and developments. Management, through personal contacts made in the course of conducting day-to-day operations as well as at professional, trade, and cooperative meetings, is in a particularly advantageous position to exchange ideas and explore possibilities for developing mutually beneficial relationships with others of like mind. It is not surprising, therefore, that initiation of the working arrangements discussed in this report were largely managerial decisions. This is not to imply that the grower-members of the affected cooperatives weren't informed of the proposed ventures or given an opportunity to make their wishes known.

The legal, financial, and organizational frameworks for carrying out specific joint operations or functions may vary within broad limits. No hard rules govern the choice of structural form to accomplish venture goals. The Keystone - Welch copacking arrangement, for example, is subject to renegotiation each year. Because Welch Foods' need for supplemental packing services was anticipated to be temporary, a short-term agreement was deemed appropriate. On the other hand, performance of a similar service by Keystone for Ocean Spray was also arranged under an annually negotiable contract even though Ocean Spray intended to continue the relationship for the foreseeable future.

In cases where processing and sales services were provided by Red Cheek

and Pacific Coast Producers to Carolina Apple Producers and Ag Mor, respectively, closer and more enduring affiliations between the plant-owning-raw-product suppliers and the processor-marketers were thought necessary to attain mutually compatible goals. Large capital commitments of CAP and Ag Mor in plant and equipment, lack of managerial operating and selling expertise, and the need for assured market outlets provided strong incentives to integrate closely with the already well-established processing cooperatives. The membership bonds, in turn, provided the processing cooperatives stronger assurances that their raw product quantity and quality needs would be met over an extended period.

Each of the basic organizational approaches identified — contractual agreement, separate entity, and membership affiliation — seem adaptable to a wide range of joint undertakings. All three methods were used by the cooperatives when rendering of a sales service by one party for the other was a major function of the arrangement. While the relative importance of considerations such as services performed, products handled, motivations and personalities cannot be generalized, all can in varying degrees influence the form of the working arrangement. Because of the diversity of conditions and motives associated with different working relationships, the exact procedure for implementation of a particular arrangement must be tailored to fit each situation.

Results on the performance of the working arrangements cited here are limited because most arrangements are relatively new. However, all participants expressed general satisfaction with their involvement. Most would be receptive to additional joint ventures given the proper circumstances.

Size of operations of participating cooperatives does not appear to be a consideration in establishing sound working agreements. In the selected examples presented in this report, extremely wide variances in sales volumes among participants were noted. More important are the strengths each partner brings to the venture so compatible goals can be achieved more efficiently. But a mutuality of interest is not by itself sufficient to assure a successful joint operation. Respondents stressed personal integrity as an essential ingredient of any agreement.

The possibility of conflicts between participants in any joint activity is always present. However, if the basic agreement incorporates provisions equitable to all parties any differences should be relatively minor and easily resolved. Indeed, none of the participants in this study indicated any serious problems. Mutual trust and understanding contributed to the satisfactory relationships. These attributes, coupled with policies of open and close communication between the parties, made it possible to settle differences long before they could reach disruptive proportions.

In conclusion, the examples given in this report demonstrate the viability of the working arrangement concept as a strategy cooperatives might consider. Management, operations, and financial strengths of potential partners may be combined by other means such as mergers, consolidations, or acquisitions. But these alternatives are usually more costly and considerably more difficult to accomplish. The assimilation of people of different organizations often represents a major impediment to a successful consolidation. Because separate organizational identities are maintained under the working arrangement approach, this potential problem is largely avoided. Experience gained under a working arrangement, if favorable, may in time point to a desirability for more complete combination of operations.

Working Arrangements of Fruit and Vegetable Processing Cooperatives

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Cooperative managers are well aware of the movement toward increased concentration of manufacturing and marketing in the food industry. Most cooperatives lack the size, financial resources, and line of products necessary to compete with the large national and multinational food companies. Many co-ops seek ways to more fully exploit the capital, technological, and managerial resources at their disposal to better satisfy the income expectations of their farmer-owners.

This report highlights organizational and operational features of a selected number of joint undertakings involving fruit and vegetable processing cooperatives. However, other types of cooperatives interested in exploring joint ventures may find the information useful for identifying and appraising opportunities relevant to their particular circumstances.

The term "working arrangement" as used in this report applies to any type of organizational joint activity undertaken by cooperatives. Such relationships may be of either short or long duration but, in any event, the corporate identities of the participants are preserved.

Although cooperatives may enter into similar types of business arrangements with noncooperative firms, this study focuses only on arrangements involving cooperatives. Contractual arrangements between cooperatives and noncooperatives are commonplace and many undoubtedly have proved to be mutually advantageous. But the feasibility of developing closer working ties within the community of cooperatives merits special scrutiny by management. In addition to avoiding possible conflicts arising from differences in philosophy among corporate forms, ventures involving only firms organized under cooperative statutes largely eliminate the possibility of violating antitrust laws.

Information for this study was obtained through personal interviews with management of 16 cooperatives that have organized partnerships to process or market fruits and vegetables. The 16 associations were aligned into nine distinct working configurations. These arrangements were examined with emphasis on the circumstances that led to each venture, the objectives sought, the organizational framework for their accomplishment, and the division of responsibilities.

*Robert A. Skinner, Agricultural Cooperative Service, U.S. Department of Agriculture, participated in the interviewing and report preparation processes of the study.

All working arrangements in this report are meant to extend or supplement the operations of their originators. As independent business identities apart from the joint undertaking, the participants determine how the venture operates. The degree of involvement in managerial decisions varies between ventures, often according to participants' inputs of product, capital, expertise, or some other predetermined basis. Procedures for sharing expenses, income, and risks are similarly established.

In this study, joint undertakings are classified according to the type of approach used to accomplish specified objectives—contractual, separate entity, or membership affiliation (table 1). The difference among the three arrangement categories is primarily one of organizational structure.

CONTRACTUAL RELATIONSHIPS

Straight contractual agreements represent the most direct and simplest approach for documenting the intentions of the participating parties and their rights, duties, and obligations. Whether in written or oral form, contracts are legally binding and enforceable.

The contractual arrangements examined in this section typically have limited and relatively straightforward purposes. They are associated with activities that require little or no additional expenditures and may be terminated with minimal disruption. Any questions regarding decisionmaking authority and performance are usually settled at the time of contract negotiations.

Table 1 — Cooperatives in study classified according to basis of working arrangement and major purpose

Type of relationship	Functions performed
● Contractual	
Keystone-Welch	Processing
Keystone-Ocean Spray	Processing
Albion-Knouse	Processing, sales
Agripac-Rogue River	Sales
● Separate entity	
Lindsay Olive-Willamette Cherry	Sales
● Membership	
MBG-Pro Fac	Processing, sales
MBG-Cherry Central	Sales
Carolina Apple-Red Cheek	Processing, sales
PCP-Ag Mor	Processing, sales

Processing and Storage Lease Arrangements

Participants

Keystone Foods, Inc., North East, Pa., is a 226-member farmer cooperative in Pennsylvania's Concord grape belt. It began operations in 1910 as a fresh grape marketing association. The declining importance of Concord grapes for fresh use and the increasing importance of California grapes in the East prompted a reorganization in 1938 that put the association into the grape processing business. This entailed large investments in plant and equipment.

Keystone processes members' grapes, tomatoes, and apples into juices for consumer and industrial markets. About 70 percent of its consumer product sales are made to private label buyers such as major supermarket and voluntary grocery chain store buying groups. The remainder of its consumer-sized packs are marketed under its own "Keystone" brand. Buyers of bulk single strength and concentrate juice products include other processors and Government agencies. Total 1982 sales were more than \$12 million.

Keystone has aggressively sought to increase the use of its extensive facilities by processing and/or packaging liquid items for other concerns. Through these copacking arrangements, the staff has gained expertise in preparation of a wide variety of high-quality noncitrus juice products. Its processing, packing, and packaging capabilities are supported by a full range of machinery for pressing fruit and pasteurizing, concentrating, freezing, canning, bottling, and cartoning finished products. Storage capacities include tanks for holding up to 3.5 million gallons under refrigeration, dry warehousing capable of storing 550,000 cases, and frozen storage space of about 2,500 square feet. Close proximity to public cold storage warehouses, transportation, and major markets make Keystone an ideal contract packer.

Welch Foods, Inc., Concord, Mass., is the leading producer of Concord grape products, including juices, jellies, jams, frozen concentrates, and fruit drinks. A variety of grape and nongrape products are marketed under its internationally recognized "Welch's" brand. Total 1982 sales were \$229 million.

Welch Foods is a subsidiary of National Grape Co-operative, Inc., headquartered in Westfield, N.Y. National Grape was organized in 1945 by growers who had previously delivered grapes to the Welch company. Over the years, a proceeds-sharing plan was developed for the benefit of both organizations and eventually led to the 1956 acquisition of Welch by its grower-suppliers.

National Grape's membership embraces growers servicing Welch Foods plants in Westfield, N.Y.; North East, Pa.;

Lawton, Mich.; Springdale, Ark.; and Grandview and Kennewick, Wash. It has about 1,700 Concord and Niagara variety grower-members representing more than 36,000 acres of vineyards. Additional acreage is contracted from nonmember patrons when needed.

Ocean Spray Cranberries, Inc., Plymouth, Mass., is a grower cooperative formed in 1930 by a merger of six cranberry handlers. It has grown into a vertically integrated marketing association that now produces about 85 percent of U.S. cranberries. Products include fresh cranberries and a wide array of processed items. Ocean Spray has taken advantage of increased consumer demand for fruit drinks by combining juice of apples, grapes, apricots, and raspberry with cranberry.

The cooperative purchased a processing plant at Vero Beach, Fla., in 1977 to produce grapefruit juice and concentrate, adding a juice product compatible to its family of cranberry based drinks. Under the Ocean Spray label, the cooperative's grapefruit drinks rapidly took the lead in sales of branded, bottled grapefruit juices. More recently, tomato juice cocktail, the cooperative's first nonfruit drink offering, was added and merchandised under a new label called "Firehouse Jubilee." Ocean Spray juices and drinks are prepared in both single strength and concentrate forms and packaged in bottles or cans. In 1981, the cooperative introduced aseptic packaging, a new concept, to the market. Here, products are sealed in sterilized paper-laminate containers which are much cheaper than glass and can packages. Also, substantial reduction in storage and transportation costs are realized.

Sales reached more than \$360 million in 1982, a new high. Juice drinks accounted for over 70 percent of the total. This growth was accomplished through a strong commitment to research, new product development, modernization of processing facilities, and a successful advertising and promotion campaign.

Ocean Spray's membership is made up of more than 800 cranberry growers and about 100 citrus producers. The proceeds to grapefruit members are pooled separately from that of cranberry producers. In addition to its Florida grapefruit facility, Ocean Spray owns and operates manufacturing plants in Massachusetts, New Jersey, Wisconsin, Washington, and Texas. To supplement its processing capacity, the cooperative combines with other firms to develop a network of satellite facilities.

Agreement Features

"Processor for hire" arrangements are common in the food processing industry. Working agreements involving organizations such as Keystone, Welch Foods, and Ocean Spray involve services processors frequently provide for a fee. In the examples cited here, Keystone renders processing and

storage services that supplement Welch grape juice and Ocean Spray cranberry juice operations.

Keystone-Welch Foods — In 1979 and 1980 Welch Foods arranged with Keystone Foods to have a portion of its grapes processed in Keystone's plant. The agreements included the maximum and minimum quantities of Concord grapes Keystone would be required to process and store each year. A schedule for receiving and processing grapes was established, along with procedures and standards for inspecting, weighing, and processing. Grapes pressed by Keystone under seasonal contract totaled 4,600 tons in 1979 and 2,600 tons in 1980. The terms of the arrangement in 1979 were formalized by contractual agreement. In 1980, Keystone services were procured on the basis of a purchase order executed by Welch.

Under the arrangement, Keystone was reimbursed at fixed dollar rates for each hour of actual operation. These charges were to be paid within 10 days after completion of processing. Keystone provided 100,000-gallon storage tanks to Welch Foods at a minimum rental for a 5-month period ending March 31, regardless of use. At the conclusion of the rental period, Welch retained the right to continued access to as many of the leased tanks it needed until June 30 on either a month-to-month or day-to-day basis. If only a portion of the leased tanks would be needed, Welch Foods had the option to utilize the set-aside tankage for storage of other juices or concentrates as long as Keystone incurred no additional expenses. Storage payment was required at the end of each month beginning with the month of harvest.

Storage specifications were in the contracts. Welch was to inspect the tanks for suitability and sanitary conditions prior to use and for quality control checks during storage. Keystone monitored the tanks' temperatures twice daily and submitted weekly records to Welch.

If Welch found it necessary to further process the stored juice it could do so itself or have Keystone do it. The fees for pasteurizing cooling and/or filtering the juice were also spelled out. Any such services would be performed during regular hours and would not conflict with Keystone's own work.

The contracts also covered allowable line loss, shrinkage, and scheduling of juice removal by Welch. Removals were expected to be made during regular hours and shipped at proper temperature. Once a tank had been opened and withdrawal started, its entire contents were to be drained within a week.

The 1979 agreement included some provisions not present in 1980. The 1979 contract specifically held Keystone responsible for safekeeping the grapes. Any loss or damage from processing and storage, unless directly attributable to Welch Foods' negligence, would acquire indemnification by Keystone. To cover its liability, Keystone was required to

carry insurance covering that part of its operation subject to the agreement and designate Welch Foods as the named insured.

To ensure sufficient storage and processing time to fulfill the terms of the 1979 contract, Keystone closed its Concord grape membership until after the harvesting season. Keystone, however, was given an option to purchase up to 300,000 gallons of Welch grape juice at a predetermined price per gallon. This option could be exercised at any time or number of times up to the maximum quantity prior to April 1 of the following year.

Most of the other terms, except for changes in volume requirements and fee schedules, were essentially similar during the 2-year period.

Keystone-Ocean Spray — The Keystone-Ocean Spray working agreement is somewhat similar to that of Keystone-Welch. Again, Keystone is "processor for hire," pressing juice from Ocean Spray cranberries, preparing concentrate, storing, and shipping. All work is supervised by Ocean Spray and is performed according to specifications.

The arrangement under which Ocean Spray cranberries from Massachusetts and Wisconsin are blended at Keystone's Pennsylvania facility has been in effect since 1974. To assist the operation, Ocean Spray installed some of its own specialized equipment in the Keystone plant. Earlier, Keystone also packed Ocean Spray products in consumer-sized glass containers but now stores only in bulk lots.

The quantity of cranberries to be processed by Keystone, the amount of storage space to be made available, technical requirements of the operation, and the schedule of charges and payments for services rendered are all subject to negotiation and change each season. Once agreement is reached, details are summarized in a purchase order to Keystone. About 5,000 tons of cranberries are processed for Ocean Spray each year.

Observations

Keystone-Welch Foods — Although the Keystone-Welch processing relationship was short, it illustrates how processors may benefit from such affiliations. Welch Foods' participation was motivated by higher than anticipated grape production in 1979 and 1980. During this period, it decided to supplement members' production with a limited number of grape contracts from nonmember patrons to ensure future Welch finished product needs. The large 1979-80 crops, however, strained Welch Foods' processing facilities. Management, believing that its first obligation was to handle the production of its members, was faced with a dilemma. If nonmember grape supplies were to interfere with plant delivery schedules

of its own growers, a membership relations problem could develop. At the same time, the obligation to take care of nonmember production remained. The solution came from Keystone, which provided the additional processing and storage capability.

Prior to the contractual arrangements of 1979-80, the two cooperatives had occasionally worked informally together on short-term operating matters involving exchanges of production materials, supplies, and the like. The spirit of cooperation that developed in the course of these arrangements, along with a desire of Keystone to increase use of its existing plant and equipment, led to the contractual agreements.

The volume of grapes handled by Keystone for Welch under the 1979-80 agreements is only a fraction of Welch Foods' total production. Nevertheless, it was sufficient to ease the pressure on Welch Foods' overburdened processing facilities.

No new contractual undertakings have been established by the two since 1980. However, both informally cooperate solving day-to-day operating contingencies when possible. The decision to discontinue the 1979-80 operations was dictated by the success of Welch Foods' ongoing program for expanding and upgrading its own facilities.

Keystone-Ocean Spray — Ocean Spray's agreement with Keystone is part of its strategy initiated several years ago to develop a nationwide network of facilities for packing and distributing its products. Copacking agreements were developed with a number of noncooperative and cooperative firms, including Sun-Diamond in California and Citrus World cooperative in Florida. The Ocean Spray-Sun-Diamond joint venture, under which products of both are prepared and shipped on a cost-sharing basis, far transcends the Keystone arrangement in terms of complexity, size, and commitment. Although smaller, the economies derived from the Keystone-Ocean Spray arrangement were deemed sufficient to justify continuance.

To keep pace with a rapidly expanding demand for its products, Ocean Spray policy is first to obtain maximum utilization of its existing manufacturing facilities, then fulfill additional production through contracts with other companies. Management believes this approach provides its growers with substantially higher returns than if they invested in new plants, equipment, and personnel. As a result, about 30 percent of the cooperative's processing is performed by others on a fee basis.

Keystone's involvement with Ocean Spray reflects a tendency toward contract packing. Being a seasonal packer, the addition of cranberries enables it to extend the use of its facilities and disperse overhead costs.

Informal Processing and Marketing Arrangement

Participants

Albion Cooperative, Inc. (ACI), Albion, N.Y., was organized in 1946 to freeze and market cherries. At that time, the management function was performed by Agway under contract and the cooperative was known as "Agway." In 1975, cherry grower members who also produced apples expressed a desire to get into the apple juice business. Because of Agway's financial relationship with Curtice-Burns — a large multiproduct food processor — and the possibility of a conflict of interest, the Albion growers decided to assume complete management control.

The cooperative is basically a "first processor" of cherries and apples. Cherries are prepared in frozen form and apples are converted to juice and concentrate. In addition, 300,000 cubic feet of cold storage capacity is owned. Most products are sold to other processors and industrial users. Total annual revenues, including cold storage rental fees, are about \$5 million.

Knouse Foods Cooperative, Inc., Peach Glen, Pa., was formed in 1949 to process fruit crops. It has 170 producers. Major crops are apples, peaches, cherries, and blueberries. Fruit is prepared for market in canned and frozen forms in plants at Peach Glen, Chambersburg, and Orrtanna, Pa. A fourth processing facility in Paw Paw, Mich., was acquired in 1982. In addition, Knouse Foods maintains a fruit-receiving station near Newfane, in northwestern New York, an important fruit producing area also served by Albion.

Knouse products are packed for both retail and institutional outlets. A high proportion of consumer-sized container sales is made under its own "Lucky Leaf" label. Gross sales in 1982 were about \$90 million.

Agreement Features

ACI and Knouse Foods have collaborated on a "handshake" basis since 1980 in the processing and marketing of red tart cherries. Under the agreement, production of a set group of Albion member growers situated closest to Knouse's receiving facilities in the Newfane, N.Y., area is directed there. Knouse is completely responsible for all handling, grading, product preparation, selling, and accounting functions.

The price ACI growers get for raw fruit depends on Knouse's income from the sale of the processed products. Payment for fruit deliveries is on an installment basis. ACI receives an initial payment at harvesttime to cover picking costs. It receives periodic supplements thereafter. Final payment is made in June of the following year when Knouse can assess its

cherry operation results. All monies received from Knouse are credited to ACP's red tart cherry pool so net returns of all Albion cherry producing members are impacted similarly.

The processing and marketing of Albion cherries is conducted under the same terms as are applied to Knouse Food Cooperative members.

Observations

Prior to the present arrangement, Knouse Foods had purchased red tart cherries from Albion to supplement its raw product requirements. In recent years, cherry production declined in the area served by the Pennsylvania cooperative. At the same time, Knouse's cherry pie filling market was growing. Knouse arranged to procure cherries from New York, which worked well because the New York crop came on stream about the time Pennsylvania production ended.

To assure a more dependable supply of high quality raw product, a closer linkage with New York growers was deemed desirable. This goal led to the Albion-Knouse arrangement. Albion's management and members were receptive to tying in with Knouse because of favorable past business dealings. But more important, the arrangement enabled them to handle more fruit without further capital investment. ACI committed to take all of its members' cherry crop. This would not be possible in years of heavy production unless processing capability were expanded or other alternatives developed. The arrangement worked out with Knouse proved to be a practical alternative. ACI benefited by holding down capital expenditures, while Knouse benefited from an extended cherry processing season. In addition, a portion of ACI's fruit was channeled to the retail market served by Knouse Foods, which gave ACI the potential for higher returns.

Some additional costs have been incurred in connection with the joint endeavor, however. Knouse must staff and maintain a receiving facility in New York. Transportation and handling services were required and a procedure developed for bulk containerization to ensure that cherries arrived in good condition after an 11- to 12-hour trip to Knouse Food Cooperative processing plants.

Under the arrangement, Albion's growers are bound to Knouse's pooling and pricing system. Knouse pool participants receive one-third of the earnings realized above the commercial market value of the crop in cash while the remainder is credited to a 15-year revolving fund.

The raw product returns ultimately realized by Knouse growers depend on the efficiency of its processing and marketing operation and the prices at which the finished products are sold. Both cooperatives are convinced that grower returns under the arrangement are higher than would

be obtainable on a cash sale basis at harvesttime.

Some 15 to 25 percent of ACI's cherry volume — depending on the size of crop each year — is assigned to the Knouse pool. This volume is significant to Knouse in that it represents 7 to 10 percent of the cooperative's red tart cherry pack.

Because the ACI-Knouse relationship is based on a verbal agreement, high integrity of the participants is essential. The arrangement has demonstrated that a formal, detailed, written plan is not mandatory for a successful joint operation.

Joint Sales Agreement

Participants

Agripac, Inc., Salem, Oreg., is a cooperative canner, freezer, and marketer of 20 different types of vegetables, fruits, berries, and nuts produced by about 240 growers. Major vegetable commodities are green beans, beets, sweet corn, and carrots. In the fruit category, purple plums, cherries, and blackberries are the leading items. Hazelnuts and walnuts complete the product line.

Agripac was formed in 1971 by the consolidation of two long-established Oregon fruit and vegetable processing cooperatives. In 1980, processing capabilities were substantially expanded through purchase of a freezing plant in Salem. Additional canning capability was recently acquired in Salem under a lease/purchase arrangement with a noncooperative processor. The organization now has several canning and freezing facilities in Salem and Eugene, Oreg., and a canning plant in Junction City, Oreg. The Eugene plant also can brine cherries and dry nuts. Distribution warehouses are at Eugene and Salem.

The cooperative's finished product volume exceeds \$80 million. The Agripac sales department deals through brokers or directly with buyers. Products are packed under its "Jack and the Bean Stalk" and "Diamond A" brands or the private labels of chain and wholesaler customers. Sales under buyer labels are, by far, the most important. Agripac products are distributed nationwide, and in some foreign markets.

Rogue River Packing Corp. (RRPC), Medford, Oreg., is a cooperative canner of Bartlett pears organized in 1970 by four fresh pear marketing firms, one a grower cooperative. A nearby canning company was acquired to process members' production not readily absorbed by fresh markets. The cooperative's sales in recent years has ranged from \$5 to \$6 million.

Agreement Features

Agripac and Rogue River Packing formed a joint sales

arrangement in 1981. The contract was written to cover a 1-year period with an automatic renewal provision. Either participant can terminate the agreement upon written notice 3 months prior to its renewal date.

Agripac markets and sells all Rogue River Packing's canned pear output. For this service, RRPC pays Agripac a fixed percentage of gross sales plus reimbursement for certain other direct distribution costs. The sales commission is subject to annual renegotiation.

Agripac is expected to maintain a trained sales staff and use its best efforts to sell RRPC's canned pears. Agripac must maintain close communication with RRPC regarding market developments and future supply requirements.

Prices at which RRPC products are moved may vary within a predetermined range prevailing at the time of sale. Sales proposals at prices lower than standard and customary within the industry are cleared first with Rogue River.

RRPC pear sales are handled on an individual account basis. Orders and invoices for RRPC products are not consolidated with Agripac's. Customer payments are received by Agripac and are deposited directly to RRPC's account on a weekly basis.

To facilitate sales, Agripac may offer RRPC pears under any of its house brands except its "Jack and the Bean Stalk" and "Diamond A" labels. Pears sold under these two leading labels are purchased outright from RRPC at prevailing prices. Agripac receives no commission on these sales.

In addition to selling and labeling, Agripac provides casing, storage, transportation, and forward warehousing. Assistance in procuring canning supplies on favorable terms is also rendered.

For sales arranged through Agripac's independent brokerage network, 1 1/2 to 2 1/2 percent is charged. Any commission above 2 1/2 percent must first be approved by RRPC.

When Agripac facilities are used for labeling, casing, and storing RRPC products, the actual costs are billed monthly. Any freight charges for shipping RRPC products when combined with Agripac products are also included. Straight shipments of pear products are billed directly by the carrier.

Agripac maintains warehouse facilities in a number of distant markets for better service to buyers. RRPC is directly charged for shipment and storage of its products that are forward warehoused. Rogue River is not charged for holding processed pears at Agripac's Eugene warehouse location. Each party is responsible for maintaining its own product liability insurance.

Observations

As a new venture, the Agripac-RRPC agreement will be subject to further refinements as time passes. By assigning the marketing function to Agripac, RRPC not only ties into a well-established sales network, but reduces selling costs as well. At the same time, the additional sales volume helps meet Agripac's overhead expenses.

Both cooperatives benefit by being able to offer customers a wider variety of food products. The arrangement expands RRPC's marketing opportunities while Agripac is further strengthened by the addition of a commodity not available from its members. Although the arrangement centralizes sales functions, it still is flexible enough to enable RRPC to have some control over marketing of its products. In practice, the exercise of such discretionary authority has in no way limited Agripac's ability to satisfy the product-mix requirements of large buyers. Rather, market accessibility has been enhanced at little or no additional costs or risks.

Both parties are committed to the program. Agripac is interested in developing similar arrangements with other cooperatives.

SEPARATE ENTITY

Establishing a new business enterprise apart from the ongoing operations of its organizers is common practice in the corporate world. The separate entity approach offers the participants considerable flexibility to adjust operations quickly as business conditions change. Capitalization of separate entity ventures can vary from very small to extremely large, depending on services performed. In the example cited here, only operating funds for a marketing program are required.

Joint Sales Agency

Participants

Lindsay Olive Growers, a 425-member cooperative headquartered in Lindsay, Calif., processes and markets olives. It started in 1916 as Lindsay Ripe Olives. Over the years, the cooperative consolidated several canning companies with its operations and is now considered the volume leader in the California industry. While canned ripe olives constitute the major portion of its pack, green and stuffed olives have gained importance in recent years. The cooperative's "Lindsay" label is widely recognized. Its 1982 sales of olives and olive products were \$52 million.

Willamette Cherry Growers, Inc., of Salem, Oreg., was organized in 1932 and is a processor and marketer of cherries grown by 353 producer members. The cooperative was

primarily a cherry briner but in recent years has expanded to include maraschino processing and bottling for retail. In 1975, the "Royal Willamette" label was developed as a focal point for building a consumer franchise for the cooperative's bottled products. Sales have since passed \$11 million.

Lindsay International, Inc., was established by Lindsay Olive Growers of Lindsay, Calif., in the early 1970's as a vehicle for strengthening its sales operation. It is a separate nonprofit agricultural cooperative designed to attract and facilitate entry of other noncompeting cooperatives into a coordinated marketing effort. Until the affiliation of Willamette Cherry Growers in 1976, Lindsay Olive was the sole member of the new organization and in effect, Lindsay International was Lindsay Olive's sales and marketing department.

Lindsay International has established itself as a prime marketer of specialty food products. It has a staff of marketing professionals, four regional sales managers, and a network of 90 brokers. The cooperative has the capability of servicing its customers through 19 distribution centers in key areas throughout the county. Both the retail and food service segments of its market are covered.

Lindsay International has a policy of enlisting additional cooperatives in its joint sales program. In 1982, a new participant, Kona Farmers Cooperative of Kona, Hawaii, joined to market macadamia nuts. Lindsay continues to seek other cooperatives with compatible product lines.

Agreement Features

Affiliation with Lindsay International in a joint sales effort entitles the participant to membership in the cooperative and a voice in setting its policies. Each member is given the right to nominate one director to the Lindsay board. Composition of the remainder of the board is based on member volume marketed through Lindsay International. The board presently consists of seven directors, four from Lindsay Olive Growers, two from Willamette, and one from Kona.

Capital contribution is not a requirement for membership. However, provision is made for future fundings upon mutual agreement by members. Membership may be terminated on 6 months' advance written notice.

The rights and responsibilities of the participating parties are spelled out in a marketing agency contract.

Lindsay International is designated as the exclusive sales agent for its members. The agent is responsible for selling, promoting, and distributing all products handled or processed by its membership except those specifically excluded. In the

case of Lindsay Olive Growers, the marketing agreement does not apply to sales of its bulk processed or bulk unprocessed olives. Sales of Willamette's bulk brine or bulk finished cherries are likewise excluded. Thus, Lindsay International's major responsibility rests in the area of marketing member products that are prepared in canned or bottled form for retail and institutional outlets. Sales under member-controlled brands are stressed although buyer label purchases are also accommodated.

Lindsay International's functions, in addition to selling the products of its members, include market analysis, advertising, promotion, order processing, invoicing, collection, arrangement of transportation and warehousing at locations other than at processing points and preparation of reports on inventory and sales. It has full authority to enter into binding contracts with buyers for the sale of each member's covered products, to transfer title in fulfillment of such contracts, and to collect sales proceeds. However, Lindsay International may not pledge, or otherwise use the products of its members as collateral. The members, in turn, are to deliver good quality, properly packaged products.

Lindsay International operates on a nonprofit basis and returns to its members on a weekly basis all sales proceeds after expenses. Deductible expenses include all necessary operating and marketing costs. Costs directly attributable to selling a member's product such as advertising, brokerage, freight and similar expenses are charged to each member's account.

General administration and sales expenses are allocated on a patronage basis in proportion to the dollar sales volume of each participant. Lindsay International is authorized to retail from sales the cost of each member's share of indirect expenses as determined by the board of directors. The amount initially authorized was set at 4 percent of net sales (gross sales less customer allowances).

Credit losses on any sale, physical loss, or product liability is borne directly by the affected member.

Each member organization shares in decisions affecting their participation. Each cooperative retains control over the price of its products, the quantities of different product categories prepared, and packaging. Decisions regarding advertising, promotion, product development, and capital expenditures require the prior approval of the participant before expenses or obligations are incurred. Marketing commitments in excess of 6 months also require the specific approval of the participant affected. Member cooperatives retain full ownership and control over their respective brands and use by Lindsay International is permitted only with the express approval of each.

Observations

Willamette's decision in the mid-1970's to emphasize retail and food service market sales rather than bulk sales to further processors called for a drastically different marketing approach. Realization that its cherry volume alone would be insufficient to support an adequate sales network led to Willamette's decision to link with Lindsay Olive Growers. The pairing of the two processing cooperatives for marketing purposes seems natural when the characteristics of the commodities they represent are considered. Both canned olives and cherries are amenable to similar end uses but are not direct substitutes. Neither product can be categorized as essential to human nutrition. Being high impulse specialty items, their purchase is subject to consumer discretion and sales respond to similar merchandising approaches.

That olives and maraschino cherries could represent a desirable product mix was recognized by the Lindsay organization in the early 1970's. At that time, an attempt was made on a limited scale to convert purchased brined cherries into maraschinos. The experiment proved unsuccessful because of insufficient cherry volume. Because of the large capital expenditure required for additional equipment to operate economically, Lindsay decided not to pursue the concept further. Thus, the recognition of limitations regarding selling capability by Willamette and production capability by Lindsay made both organizations receptive to the idea of a marketing alliance for maraschino cherries.

The arrangement appears to have met the expectations of both organizations. Both agree that by joining their respective sales and distribution costs are lower.

The program's effectiveness is evidenced by Lindsay's growth. Total sales of Lindsay International increased from about \$32 million in 1977, the first full year of joint operation to about \$62 million in 1982. Willamette's contribution to sales increased during this period from about \$3 million to more than \$11 million. This volume represents about 90 percent of Willamette's total cherry marketings. The Willamette brand has grown from a zero base in the mid-1970's to a dominant position in the national market. Lindsay Olive Growers volume also increased at an accelerated pace during the period.

Neither party has experienced serious problems with the arrangement. Terms of the agreement assure retention of individual member control over key production and pricing decisions. And frequent contacts between managements assure early resolution of any problems that might arise.

MEMBERSHIP AFFILIATION

Membership affiliation is a technique by which cooperatives can integrate operations. Membership status entails financial

and patronage obligations on the part of the joiner. The member participates in the decisionmaking process and shares the returns in proportion to the volume of business done through the association. Control over association affairs exercisable by any one member is affected by the voting power of other members of the organization.

Because substantial investments are often required, a membership status usually implies a long-term commitment.

In the cases summarized, membership is required in the organization providing the processing or marketing service.

Processed Product Marketing Arrangements

Participants

Michigan Blueberry Growers Association (MBGA), Grand Junction, organized in 1936, provides marketing services to 540 growers of cultivated blueberries on more than 10,000 acres in Michigan and northern Indiana. The cooperative maintains receiving stations and warehouses at seven locations to assemble, inspect, and grade fruit and distribute production supplies.

All members' blueberries, excepting direct farm sales, are marketed through MBGA. MBGA owns the berries once they are delivered.

The cooperative handles about 60 percent of the Michigan crop. Its 1982 gross sales were more than \$16 million.

The most important end-use of MBGA blueberries is for bakery products and pie filling, which account for almost 60 percent of production. Fresh use accounts for about 20 percent and sales in frozen form direct to retailers and frozen food distributors amount to about 10 percent. The remainder goes for preserves, syrup, puree, concentrate, and whole berries in can or glass.

MBGA growers may select the markets they wish to service. Members having the capacity to supply berries in a "prepared to freeze" form may do so. Others, preferring to deliver their fruit in the fresh state, may designate the portions to be sold for fresh-market and processing uses. Marketing decisions are made in consultation with management so products are in line with the needs of buyers.

The association operates a multiple pool system to accommodate the various marketing alternatives open to members. Fresh blueberries are pooled weekly. Blueberries for processing are included in an annual pool. Grower fruit for processing is classified according to quality grades and product form. Payment between grades and forms is a management decision. Selling expenses, handling charges, and retains for

operating and capital purposes are deducted from pool proceeds.

Although MBGA does not own or operate processing facilities, it has substantial investments in property. An estimated \$175 million would be required to replace its existing warehouses and delivery equipment.

Pro-Fac Cooperative, Inc., Rochester, N.Y., was founded in 1961 to market fruit and vegetable processing crops. Pro-Fac's membership consists of about 800 individual growers or associations of growers located principally in New York, Pennsylvania, Indiana, Michigan, Nebraska, Washington, Oregon, Iowa, and Georgia. The cooperative procures about 25 different commodities, including apples, cherries, snap beans, potatoes, cucumbers, sweet corn, peas, asparagus, beets, tomatoes, cabbage, popcorn, and southern vegetables. The farm value of these and other crops represented by the cooperative totaled more than \$36 million in 1982.

Pro-Fac has close ties with Curtice-Burns, Inc., a publicly held corporation also headquartered in Rochester. Curtice-Burns started as an amalgamation of two upstate New York canners under the general guidance of Agway, Inc., of Syracuse.

Agway, a large farm supply cooperative, purchased controlling interest in Curtice-Burns as a way for its members to maintain access to shrinking agricultural markets. Agway was also instrumental in organizing Pro-Fac to fill the raw commodity needs of Curtice-Burns. About 62 percent of Curtice-Burns' raw product requirements are supplied by Pro-Fac.

Since its formation, Curtice-Burns has extended its operations to 12 States, largely through acquisitions of existing food processors. In addition to canned and frozen fruits and vegetables, such diverse items as condiments, potato chips, other snack foods, fruit fillings and toppings, salad dressings, canned meat products, soft drinks, and cereal products are prepared.

The bulk of finished products are sold directly to supermarket chains or through food distributors. In recent years, the company has developed strong regional brand names. Between 1966 and 1982, products sold under buyer-controlled labels have declined from about 85 percent to 23 percent of total marketings. Combined branded, private label, and food service sales in 1982 netted more than \$484 million.

Pro-Fac's relationship with Curtice-Burns extends far beyond selling produce to it. The cooperative owns 28 food processing plants and other distribution facilities, and leases them to Curtice-Burns. In addition, the two are tightly linked through other financing arrangements. Pro-Fac is committed to provide substantial long- and short-term capital for Curtice-Burns both directly from its members and indirectly through borrowings. In return, the cooperative receives a 50-percent

share of Curtice-Burns' pretax earnings. Details are spelled out in long-term contractual agreements.

Neither Curtice-Burns nor Agway own stock in Pro-Fac but each is entitled to one "public" director on Pro-Fac's 15-member board. The remaining 13 Pro-Fac directors are elected from 8 geographical regions. Each Pro-Fac member has but one vote regardless of the number of shares owned. The number of directors from each region is generally determined by the value of raw product from that region. One Pro-Fac director also serves on the Curtice-Burns board.

Operational functions are performed by Curtice-Burns employees under direction of the Pro-Fac board. Curtice-Burns is reimbursed for that expense.

Cherry Central Cooperative, Inc., Traverse City, Mich., markets fruit items produced in Michigan, Wisconsin, Indiana, and Utah. Started in 1973 by 5 cherry processing cooperatives, it now counts 20 cooperatives and producer-packers.

Cherry Central markets the canned or frozen fruit products of its members. Through its divisions, it furnishes production supplies such as cans, sprays, and fertilizers and provides transportation services. In 1979, the cooperative acquired Wilderness Foods, Inc., a Midwest-based food manufacturer especially well known for its retail line of fruit fillings. In 1981, Cherry Central purchased Naturally Good Products, which offers a retail line of individually quick-frozen fruits and vegetables.

Cherry Central's list of products include red tart and sweet cherries, sliced apples, purple plums, strawberries, and blueberries. Most fruit items are prepared in frozen solid pack and individually quick frozen forms. Cherries and plums are canned as well as frozen. Purees and concentrated juices in bulk are also available. Cherry Central's biggest customers are food manufacturers. About 10 percent of its cherry and blueberry volume is exported. Total 1982 sales were more than \$70 million.

Agreement Features

MBGA has integrated its products beyond the raw fruit stage by joining Pro-Fac and Cherry Central. Through membership in Pro-Fac, MBGA is entitled to be sole supplier of blueberries to Michigan Fruit Canners, Inc., Benton Harbor, a subsidiary of Curtice-Burns. By joining Cherry Central, it has acquired an exclusive sales agent for its frozen blueberry output.

Both Pro-Fac and Cherry Central assume title to the blueberries committed to them by MBGA. But MBGA retains full control over all raw product sales made to fresh market and other types of end use buyers.

MBGA - Pro-Fac — MBGA became a member of Pro-Fac in 1980. The capital contribution requirement for membership is determined by Pro-Fac according to the kinds and quantities of crops committed. For blueberries, the Pro-Fac board established that the amount of common stock purchased be at the rate of \$180 per delivered ton, one-fourth to be paid upon joining and the balance payable in three equal installments. Payment can be made in cash or from proceeds of crop sales or other sources as preferred by the member. At the time of this report, the par value of Pro-Fac common stock has \$5 per share carrying a dividend rate up to 12 percent. MBGA's stock purchase requirement totaled \$198,000, which allows it to deliver 1,100 tons of blueberries to Curtice-Burns for processing.

In addition to the common stock investment, a portion of the patronage earnings of Curtice-Burns payable to Pro-Fac members is withheld for a 5-year period. During this time, no interest or dividends are paid on the amounts retained. However, upon completion of the waiting period, the retains are converted into noncumulative, freely transferable preferred stock with a par value of \$25 per share. In recent years, annual cash dividends of up to 12 percent have been paid on this stock.

The concept of commercial market value (CMV) and how it is established is a critical element in the agreements governing relationships between Pro-Fac and its members and Pro-Fac and Curtice-Burns. CMV is defined as a "weighted average of prices paid by commercial processors for similar crops sold for similar or related uses in the same or competing marketing areas." Curtice-Burns agrees to pay Pro-Fac at least the CMV of Pro-Fac crops and the cooperative, in turn, strives to pass the full amount of the CMV to its members as cash payment for raw commodities delivered.

The CMV is determined by a five-member committee, consisting of two directors of Pro-Fac, two from Curtice-Burns, and one appointed by the committee. Provision is also made for the formation of commodity committees composed of member-growers of each of the major crops produced for Pro-Fac. These committees advise on CMV and matters concerning specific commodities. In the case of MBGA, CMV is based on the weighted average of the prices it receives from other processors who purchase blueberries for pie filling and hot pack on prearranged terms during the Pro-Fac delivery season. Pie filling and hot pack are the major end product uses of blueberries marketed through Pro-Fac. Prices received by independent growers in the area are not considered in the CMV calculation because most do not meet the quality and grade standards of MBGA and sell to buyers who utilize blueberries over a longer time period than does Pro-Fac.

Pro-Fac uses the single pool concept to determine the crop payments it receives from Curtice-Burns. Thus, the proceeds paid MBGA for its blueberries are related not only to the

CMV but also to the total profitability of all Pro-Fac crops in the pool.

It is Pro-Fac policy to pay cash advances to cover harvesting and delivery costs. Additional payments are made to members as money from the sale of processed products is remitted by Curtice-Burns. Pro-Fac pays half of the estimated CMV within 30 days of delivery of a particular crop, another 25 percent within 120 days after delivery, and the balance before July 15 of the following year.

As a member of Pro-Fac, MBGA agrees to honor Pro-Fac's bylaws, general marketing agreement, and the annual crop agreement applicable to blueberries.

The Pro-Fac bylaws state the objectives and operating framework of the association and define membership responsibilities and rights.

The marketing agreement appoints Pro-Fac as MBGA's exclusive agent for processing and selling the quantity of blueberries covered by Pro-Fac common stock over a 3-year period. At the end of this period, either party may terminate the agreement by giving a 1-year notice.

The crop agreement specifies the terms under which MBGA's blueberries are to be sold. It is renegotiated each year and any changes relating to quantity and quality specifications or other conditions pertinent to the crop are incorporated.

MBGA - Cherry Central — MBGA began its affiliation with Cherry Central in 1980, the same year it joined Pro-Fac. This step represented another facet of MBGA's strategy to place its product closer to the consumer. As with Pro-Fac, membership in Cherry Central committed MBGA to be bound by the rules of another cooperative.

To become a member, MBGA was required to purchase Cherry Central capital stock at the rate of \$24,000 per million pounds of fruit marketed. A 3-year moving average is used to determine the number of pounds on which the investment is based. MBGA's frozen blueberry supply commitment to Cherry Central required an initial financial obligation of \$192,000, which MBGA paid in equal installments over a 3-year period. Should MBGA choose to withdraw for any reason, the stock would be redeemed at full face value. However, a year's written notice of intent by either party is required before the marketing contract may be canceled or terminated.

Voting in Cherry Central is based on one-member-one-vote. One seat on the Cherry Central 21-man board goes to an MBGA-named representative.

MBGA has developed a market intelligence network and statistical base to determine a fair market price for its

blueberries. Cherry Central sells blueberries only at prices suggested by MBGA.

Cherry Central maintains a separate pool for each of the commodities it represents. Annual proceeds from the sale of each commodity, less expenses, are distributed to members. Costs of marketing and other services are assessed to each member based on sales volume. Set annually, it has averaged about 3 percent in recent years. About 20 percent of the fee is usually returned each year as patronage refunds.

Cherry Central makes payments as sales revenues are received. Final allocations are made at the end of the marketing year when sales and operating figures are known.

Because MBGA is the only supplier of blueberries to Cherry Central, all net blueberry pool receipts from Cherry Central accrue to MBGA's process pool. Amounts sufficient to cover MBGA operating and capital costs associated with the sales are deducted. The proceeds are then remitted or allocated by the association according to the volume of process fruit each grower-member delivered to MBGA.

Observations

MBGA has gained additional market security and stability by affiliating with larger, broader based food manufacturing and marketing agencies.

MBGA - Pro-Fac — As a member of Pro-Fac, MBGA is assured an outlet for its processing blueberries at prices commensurate with what it could obtain from other processors. In addition, MBGA participates in Curtice-Burns' earnings in proportion to its patronage. The price paid by Curtice-Burns to Pro-Fac for crops has substantially exceeded the CMV of those crops in each of the past 5 years. Typically, members are paid about 30 percent of patronage earnings over the CMV in cash, the remainder being retained by Pro-Fac and allocated to member accounts. These funds are used by Pro-Fac to purchase processing facilities and equipment and provide operating capital for the Curtice-Burns operation. Earnings on Curtice-Burns products not based on Pro-Fac crops are considered nonpatronage income and are treated as earned surplus of Pro-Fac. Although these funds are not allocated directly to members, they add financial stability to the cooperative. The production of products unrelated to Pro-Fac crops permits fuller utilization of Pro-Fac facilities and thereby reduces the overhead burden on all products.

Pro-Fac has instituted a commercial market value stabilization program to cushion the impact of possible short-term adversities in earnings of Curtice-Burns. Should net proceeds received from Curtice-Burns in any year be less than needed to pay full CMV, the short fall would be covered to the extent it did not exceed 15 percent of the CMV of all Pro-Fac crops

delivered the previous year. Funds for this program, up to the maximum, would be drawn from Pro-Fac's equity and paid to members for their crops. However, once the 15 percent of CMV limitation was reached, further stabilization payments, if required, would be authorized only to the extent that amounts previously expended under the program had been restored from subsequent Pro-Fac earnings.

From MBGA's point of view, membership in Pro-Fac provides an assured market at competitive prices for a portion of its production and an opportunity to earn extra income from Pro-Fac's patronage earnings. Through its participation in Pro-Fac's single pool arrangement, MBGA participates in the potential benefits of crop and geographical diversity. Further price stability is added by Pro-Fac's CMV stabilization program.

Being the single most important supplier of raw blueberries for the Curtice-Burns operation gives MBGA a strong voice in recommending the CMV for this commodity. Moreover, should increased quantities of raw product be required by Curtice-Burns, the cooperative would be given the first opportunity to fulfill the additional requirements.

In addition to the required purchase of a substantial amount of Pro-Fac common stock over the years through patronage retains, a large sum will be invested by MBGA in the form of preferred stock. While both types of stocks pay dividends, the patronage retains are held by Pro-Fac interest-free for 5 years before being converted to the preferred category. As is true for any cooperative, risks of ownership and operation are ultimately borne by the membership.

Benefits accruing to Curtice-Burns through its arrangement with Pro-Fac include an assured supply of quality raw agricultural commodities and provision of capital on very favorable terms. Acceptance of delayed payments by Pro-Fac members for their crops reduces the seasonal borrowing requirements of Curtice-Burns and consequently further reduces capital acquisition costs.

MBGA - Cherry Central — Marketing, cost, and income considerations motivated MBGA to federate with Cherry Central.

Fresh blueberries not sold at harvest must be held in frozen storage. Prior to 1980, MBGA had experienced a sharp decrease in the number of customers purchasing blueberries for freezing as this function was increasingly assumed by farmer packers. The high cost of carrying frozen inventory exacerbated this development. As a result, the association was placed in the position of having to be a full-time, year-round marketer of frozen blueberries rather than a part-time seller only in big crop years. It was apparent that this growing segment of its business would require substantially more sales effort.

In deciding how best to address its additional marketing responsibilities, MBGA management noted that the number of firms in the fruit and vegetable processing sector had diminished substantially over the years. Those remaining were bigger and more diversified. Specifically, the association's customers were often more important users of other fruits such as apples and cherries. Raw product procurement concerns of such firms, therefore, more often centered on locating sources capable of supplying a combination of commodities meeting desired volume and quality specifications. In this context, MBGA reasoned that being a single-commodity organization would make it increasingly difficult to compete with suppliers able to provide a variety of products. Thus, it was concluded that to strengthen competitive position and improve market outlook, it would be advantageous to become involved, if possible, with other broader based, large-volume organizations.

The Cherry Central organization appeared to be a logical vehicle for moving MBGA's frozen blueberry output. Being an aggressive marketer of industrial fruit products, the cooperative was receptive to adding new members with products compatible with its existing line. Likewise, the opportunity to draw on the sales expertise and servicing capabilities of the Cherry Central organization was viewed favorably by MBGA.

As a specialized marketer of frozen fruit products, Cherry Central had established trade relationships with a large number of different types of frozen commodity buyers — both domestic and foreign. MBGA blueberries could be merchandised to these customers along with Cherry Central's other product offerings. MBGA's sales opportunities would thereby be expanded. By joining, both Cherry Central and MBGA could more readily and effectively meet the product and service requirements of their buying clientele. At the same time, Cherry Central's per-unit operating costs would be reduced as a consequence of the added volume of MBGA.

Prior to joining Cherry Central, MBGA thoroughly analyzed the potentials of the venture. It concluded that longrun benefits far exceeded costs projections. In particular, substantial savings in inventory insurance costs and selling expenses were indicated. And in addition to being paid prevailing market prices for its blueberries, MBGA would also participate in the earnings of Cherry Central through patronage dividends. Included in such payments would be the profits of Cherry Central's Wilderness Foods and Naturally Good Food Products divisions.

Lease and Operating Arrangement — Apple Processing

Participants

Carolina Apple Processors (CAP), Hendersonville, N.C., was organized in the mid-1970's to improve the area's juice-

quality apple sales. Historically, the price for these apples had been lower than prices in the Northeast. Apple growers working with North Carolina State University and others, decided that the best means for growers to improve their market share would be to involve an established processor-marketer. They picked Red Cheek, Inc., a Pennsylvania apple-processing cooperative that customarily supplemented its raw fruit requirements through open-market purchases in North Carolina.

In 1975, a number of North Carolina apple producers were incorporated to build a processing facility. To finance the plant, 126 producers purchased stock in the new association at the rate of \$1,000 per share per 40 tons of apples delivered for processing. The committed tonnage translated into an initial \$416,000 capital contribution, sufficient to qualify for an \$800,000 loan from the Columbia South Carolina Bank for Cooperatives.

To ensure a sufficient supply of apples, CAP required its members to enter into a 5-year marketing agreement. At the end of the period, the agreement would automatically continue from year to year unless either announces intention to terminate. At the same time, CAP contracted with Red Cheek to have its supply of apples pressed into juice in Hendersonville on a fee basis. Red Cheek agreed to take and market the products so produced. This operation lasted through 1978.

Red Cheek, Inc., Fleetwood, Pa., began as the Berks-Lehigh Mountain Fruit Growers Association in 1936, a fresh fruit marketing cooperative formed by eastern Pennsylvania apple growers. In 1940, the association began producing and marketing apple juice under the Red Cheek label. The organization changed its corporate name to Red Cheek, Inc., in 1972 in recognition of the growing popularity of the juice.

In addition to its main plant in Fleetwood, the cooperative maintains satellite pressing operations in New York, North Carolina, Michigan and Ohio. Membership includes 5 grower cooperatives along with about 120 individual producers.

Finished product sales in 1982 were about \$26 million, with Red Cheek apple juice products about 95 percent of the total. Other items packed by the cooperative include frozen apple slices, and fresh apples. Red Cheek is the leading apple juice brand in metropolitan New York, Philadelphia, and Miami.

Agreement Features

The 1975 CAP - Red Cheek arrangement evolved into a more permanent relationship in 1979 with a restructure of the Red Cheek membership format. This development bonded the members of the two associations into a single decisionmaking unit with former CAP employees becoming Red Cheek

employees. The corporate identity of the North Carolina growers was preserved, however, because title to the land, buildings, and equipment at Hendersonville remained with the North Carolina group. Primary responsibility for debt servicing and major decisions relating to the use and maintenance of facilities stayed with the CAP board. Red Cheek is responsible for the normal maintenance to building and machinery.

Under the new arrangement, CAP facilities for juice processing are made available to Red Cheek on a lease basis. In addition to the land and buildings, CAP owns about 40 percent of the equipment. Red Cheek owns about 5 percent of the remaining equipment, the balance being rented from an equipment leasing company. Red Cheek may acquire CAP's land and buildings under a qualified purchase option.

Another major CAP function is to provide a reliable supply of juice grade apples for processing. Terms and conditions affecting quantities, quality, payments, and associated contingencies are covered in the Red Cheek membership agreement. The provisions of the marketing agreement between CAP and its members, in turn, are consistent with Red Cheek's membership requirements.

Capitalization of Red Cheek is achieved through issuance of stock and capital retains. Each member is entitled to only one vote regardless of the number of shares held.

Red Cheek management has total responsibility for the juice production process and sales of finished products. The North Carolina operation is now a division of Red Cheek, Inc. All management, technical expertise, labor, manufacturing materials, and operating capital are provided by Red Cheek.

All proceeds from the sale of juice products are pooled. Carolina Apple Processors shares in the pool in proportion to the amount it contributes. Red Cheek remits within a month of delivery about half of the projected season's field price for juice apples. Additional payments are made as the season progresses and final payment is made after the crop has been marketed. To determine the actual value of raw commodity inputs, Red Cheek sales proceeds are reduced by all costs associated with the preparation and marketing of the finished product. Remittances to members are in cash and capital allocations. Capital from patrons is placed in a revolving fund and returned at the discretion of the Red Cheek board on a first-in, first-out basis. The CAP board is responsible for distributing or allocating receipts from Red Cheek to its membership.

Observations

Both parties agree that the joint venture has met original expectations. North Carolina growers believe that returns

from their juice apples have increased to levels comparable to those of northeastern producers. The quantities of North Carolina apples processed and marketed by Red Cheek under the arrangement has increased from 460,000 bushels in 1976 to 760,000 bushels in 1981. About 20 percent of Red Cheek's total sales volume is now generated through the CAP operation. Short-term plans call for an expansion in warehousing facilities and processing capabilities through installation of juice concentrator equipment at the North Carolina site.

Initiation of the working relationship was contingent on the willingness of the North Carolina growers to commit sufficient volume of fruit and equity capital required for efficient operation. The ability to borrow needed funds was enhanced by the willingness of Red Cheek to undertake processing and marketing functions for the North Carolina group.

The CAP - Red Cheek plan offers a number of attractive incentives for each of the participants.

For North Carolina producers, it promises an assured outlet for their juice apples and higher returns at minimum cost and risk. The task of managing the processing function is assigned to the experienced Red Cheek staff. This circumvents the problem of acquiring the managerial and technical expertise necessary to establish an efficient physical operation. Further, affiliation with Red Cheek enables the CAP growers to participate in the sales program of a well-established marketer of apple products having a recognized consumer brand that commands a premium price at the retail level.

As a division of Red Cheek, the CAP operation can draw on the financial strength of the larger association, if needed, and share in its net margins. Because Red Cheek is obligated to use CAP's facilities to process a pre-set quantity of fruit, the ability of the North Carolina growers to service the debt covering their premises is made more certain.

From the standpoint of Red Cheek, the inclusion of CAP in its membership broadens the procurement base needed to supply the growing demand for apple juice products. By drawing on more distant production areas, the cooperative reduces the risks of short apple crops due to weather vagaries. The arrangement also alleviates problems associated with raw product procurement and pricing on the open market. Volume commitments are known in advance and grower payments are contingent on the returns eventually realized from the sales of finished products.

The CAP site provides a locational advantage to Red Cheek. As a distribution base it enables Red Cheek to more efficiently serve its important southeastern markets. By operating the CAP facility under a leasing arrangement, Red Cheek largely avoids incurring the financial responsibilities associated with

the installation. At the same time, CAP because of its membership status in Red Cheek is obliged to share in the capitalization of the Pennsylvania cooperative.

The North Carolina group entered the arrangement fully aware that certain of its managerial prerogatives would be diluted and additional responsibilities would be incurred as a member of Red Cheek. The CAP growers' control over processing, pricing, and marketing decisions regarding their production is diffused as a result of the Red Cheek affiliation and its one-member, one-vote rule. The importance of the North Carolina group to the overall operation is specifically recognized, however, through representation of CAP by one director on the Red Cheek 10-member board.

CAP participates in all the risks of Red Cheek — the same as any cooperative member. In addition to providing required financial support to the Red Cheek organization CAP is solely responsible for the debt outstanding on its North Carolina facility.

Member-management rapport is vital to the long-term effectiveness of all cooperative endeavors. The CAP-Red Cheek linkage may be characterized as one in which a sense of commitment and accommodation is well developed. It is a relationship grounded on mutually compatible economic goals coupled with sincere desire to work in harmony toward their attainment.

Lease and Operating Arrangement — Tomato Processing

Participants

Pacific Coast Producers (PCP), Santa Clara, California, is a fruit and vegetable canner serving 150 growers over a 300-mile area between Bakersfield and Oroville. PCP was organized in 1971 at which time it acquired three plants from Stokely-Van Camp. Can manufacturing and can preparation facilities were later added along with warehousing for can and pack storage. Items are prepared for both the retail and food service trade.

PCP packs apricots, cling peaches, pears, fruit cocktail, grapes, spinach, and tomatoes. Tomatoes are processed into a variety of products, including puree, paste, sauce, and catsup.

The cooperative is primarily a private label canner. Its annual sales volume in 1982 was about \$122 million. Proceeds of all PCP sales are combined in a single pool. Growers receive pro-rata shares based on the PCP Board's determination of the commercial market value of their raw product deliveries.

Growers' payments may be made partly in cash and partly in per-unit retain certificates. Cash advances prior to the closing of the pool are provided and final payment is made within 3 1/2 months after the close.

To capitalize the cooperative, growers initially deposited 10 percent of the market value of products intended to be handled by PCP. For the deposit, the member was issued a 10-year promissory note at 8 percent annual interest. Members were also obligated to contribute 15 percent of the established market value of their raw products as per-unit retains. Retain certificates are issued 8 1/2 months after the close of the pool.

To assist financing, several limited partnerships of PCP growers and employees were established. The funds are used to purchase facilities and equipment for lease to the cooperative. Use of limited partnership arrangements enable the cooperative to revolve capital retains faster than could be done otherwise.

PCP voting policy allows members to accumulate additional votes for every \$1,000 worth of products marketed up to a maximum of 3 percent of the total voting power of the association.

All PCP growers are required to enter into an agreement with the association. Kinds and quantities of specific crops to be delivered to the association are jointly determined each year. The agreement is 15 years, subject to change if conditions warrant. A member may terminate affiliation anytime after the third year, by giving a 1-year notice.

Ag Mor, Inc., is a cooperative organized in 1978 by 17 Sacramento area tomato producers, 8 of whom were also PCP members. At the time, the canning tomato market was good but existing processors were not in a position to take on additional tonnage. So when an opportunity came to purchase an existing canning plant, the farmers decided to organize and acquire it. The plant, located in San Jose, was purchased in early 1979 by Ag Mor for \$5 million. It was fully equipped, with a capacity of 100,000 tons of raw tomatoes over a canning season. To finance the purchase, the growers assessed themselves \$31 per ton. At 100,000 tons, this procedure yielded \$3.1 million. The balance was obtained through a bank.

A procedure was then developed to integrate the Ag Mor growers and their plant into the PCP operation.

Agreement Features

Two contracts govern the PCP-Ag Mor relationship.

A crop purchase and membership agreement makes Ag Mor a member, obligating it to deliver raw tomatoes to PCP for processing and marketing. A lease and operating agreement covers the Ag Mor canning facility.

The membership terms are essentially the same as for an individual grower except that the plant-leasing arrangement

imposes new conditions. The Ag Mor membership is contingent on PCP's continued access to the Ag Mor processing facility. In addition, the quantity of tomatoes that Ag Mor may provide is restricted by the capacity of its plant even though PCP management may at its discretion divert deliveries to any other processing facility in the PCP complex. Thus, without modifications to plant capacity Ag Mor growers are limited to supplying about 100,000 tons of tomatoes at a maximum rate of 2,000 tons per day each season. However, technical or other considerations may alter this figure.

As with other members, Ag Mor must deposit with PCP an amount equal to 10 percent of the value of the raw products it delivers. The PCP board established a rate of \$2.80 per ton of tomatoes so Ag Mor deposited \$280,000 ($\$2.80 \times 100,000$ tons) for membership under the terms of the agreement. The deposit is repayable within 10 years at 8 percent annual interest.

Ag Mor's membership in PCP is for 15 years, but may expire earlier if PCP opts to purchase the Ag Mor plant any time within 3 years of the end of the lease. Individual Ag Mor members would then be entitled to continue with PCP as direct members.

PCP is free to prepare and market the products any way it wishes. Payments received by Ag Mor for its deliveries are made on the same basis as for individual PCP grower-members. The Ag Mor board decide how to distribute the receipts.

Although most PCP bylaws and membership terms apply equally, any breach of contract by Ag Mor would be especially serious for its members because of their high financial commitments in plant and equipment.

Under the lease and operating agreement PCP leases and operates the Ag Mor cannery for 15 years at an annual cost of \$1,014,000, payable quarterly. Annual rentals are reduced if Ag Mor fails to supply a minimum tonnage of tomatoes during any given season or if Ag Mor's share of net margins exceeds specified amounts. However, there is no reduction if the inability to deliver is beyond the control of growers.

The rent is subject to reduction if the plant's processing capacity cannot be maintained because of insufficient capital, damage, destruction, or problems of compliance with State and Federal regulations. PCP is responsible for all operating costs, including maintenance and repair, utilities, taxes, and insurance.

Capital improvement costs are primarily the responsibility of Ag Mor. The lease requires Ag Mor to contribute a total of \$6.75 million at an average annual rate of \$450,000 for these costs. For any given year, the amount paid may vary from a minimum of \$315,000 to \$585,000. However, for the first 5

years, Ag Mor is obligated to commit a total of \$2.25 million. If the amount paid is insufficient to maintain the capability of the plant at 2,000 tons per day, PCP must pay the additional amount necessary to preserve that capacity.

If both parties agree to increase the plant's processing capacity, provision is made for also increasing the quantity of tomatoes Ag Mor may deliver. The additional tonnage Ag Mor would be entitled to deliver would be determined by the additional capital each contributed.

PCP has an exclusive option to purchase the plant any time during the first 12 years of the lease. Earlier termination of the lease may occur for any number of reasons. These include substantial reduction of plant processing capacity due to damage, destruction, default of quarterly rent payments; or failure to observe other terms of the lease or membership agreement. Disputes related to claims for damages arising from the lease are to be settled by binding arbitration.

Observations

The PCP - Ag Mor arrangement for processing and marketing tomato products stemmed from a mutual desire of the participants to enhance their production and sales capabilities.

Prior to the agreement, the processing capacity of existing PCP plants was inadequate to handle the tomato tonnage deemed necessary to meet product line and sales objectives. The lease-operating contract provided the means for obtaining additional processing capacity quickly with minimum capital expenditure on the part of PCP members.

At the same time, Ag Mor growers wanting to take advantage of the then relatively high per-acre returns associated with tomato production, determined that their best alternative for accomplishing this objective was the acquisition of a processing facility. Realizing that it would probably not be profitable to process and market alone, a decision was made to have these functions performed on a contractual basis. The interest of PCP in expanding its processed tomato line matched Ag Mor's desire to increase raw tomato production. Through the efforts of some Ag Mor growers who also held individual memberships in PCP, the two organizations were able to form a close-knit relationship.

To accomplish its purpose, Ag Mor has assumed a heavy financial burden associated with plant ownership. This has proved especially troublesome because of high prevailing interest rates. In addition, substantial financial commitment is required for membership in PCP and strict adherence to prescribed standards of performance specified in the association's membership agreement and bylaws. Ag Mor is open to all the problems and risks associated with the role of landlord. The fact that some growers hold dual memberships may give rise to member relations problems. Furthermore,

PCP's limitation of the number of votes that may be cast to not more than 3 percent of the total diminishes the influence and control of large volume members such as Ag Mor over the affairs of the association.

As a result of the arrangement, PCP's tomato volume has increased substantially. Sales of tomato products as a proportion of total fruit and vegetable marketings increased from about 30 percent in 1979 to 50 percent in 1982. Ag Mor's contribution represents about 40 percent of the total tomatoes handled. But net returns, especially during the first 2 years of operation have been disappointing. Higher than anticipated plant start-up costs, high interest rates, heavy supplies and weak markets for tomato products all contributed to the poor showing. However, substantial improvement in operating results occurred in 1982.

The arrangement survived the severe test of unfavorable economic conditions. The commonality of interest of both parties reinforced by strong legal sanctions provided the bases for a sound working relationship in a volatile industry.

As a result of the good working relationship developed during the course of the arrangement, the parties decided to merge operations. PCP exercised its option to purchase the Ag Mor processing plant as provided in the contractual agreement. PCP can negotiate more effective loan terms for the processing plant and equipment than available directly to Ag Mor members. Also, PCP eliminates the rental payment for facilities and will take advantage of cash flow benefits accruing from depreciation. Ag Mor's primary motives for merger were to eliminate the direct expense of the loan on their facilities and problems associated with administering the association's affairs.