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Cooperative Enterprise and Organization Theory: An Appraisal

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What is a university? The literal minded person may think in concrete terms: ivy-clad buildings, impressive laboratories, and a huge library. The journalistic and legal types may think of the governing board and top administration. Faculty members may stoutly insist that they are the university. A management theorist may argue that it is a special type of organization, invisible and abstract but embodying a nexus of contracts among thousands of stakeholders. A conciliator may suggest all of the above.

In last year's classic reprint, Phillips treated the cooperative as an association of farmers jointly controlling a plant. He pictured an agricultural cooperative as an organization of firms rather than itself being a firm.

This year's classic by Helmberger and Hoos asserts that the cooperative should be viewed as a firm. Is this a disagreement comparable to ancient disputes about whether the earth is flat or round? Why is not the "correct" paper alone considered to be the classic? Or is this disagreement a difference in viewpoints similar to the divergent concepts of a university?

There were also disagreements among the first two classics published in this *Journal of Agricultural Cooperation* (now *Journal of Cooperatives*) series. Nourse, a leading agricultural economist of his day, wanted agricultural cooperatives to stimulate competition to the point that they would no longer be needed. Sapiro, a leading California attorney for cooperatives, campaigned for use of a type of commodity-wide cooperative that had worked well for some specialty crops grown mainly in limited areas of California. As Nourse perceived Sapiro endorsing a permanent cartel-like organization, he wanted nothing to do with such an anti-competitive approach. Sapiro saw Nourse as building organizations on sand that would accomplish far less than commodity-wide cooperatives. These clearly divergent concepts of cooperatives for market competition or for market power still arise from time to time.

We can understand that these two pioneers were addressing general audiences and arguing for what should happen. We can see the crucial differences in their education and experiences. Thus, we can understand their differing conclusions. But what shall we say about the differences

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between Phillips (P) and Helmberger and Hoos (HH)? Presumably, both papers were objective analyses written for professional peers.

The Cooperative's Economic Structure

Both P and HH appear to be addressing the same issue of whether to consider the cooperative to be a separate identity called a firm. Both would have agreed that, in a literal sense, a cooperative is considered a firm. For example, most cooperatives were incorporated and "a corporation is an artificial being separate and distinct from its agents, officers and stockholders" (Hulbert 1958, 22). But the question was whether, in economic terms, a cooperative should be considered as a firm. HH say yes and P seems to say no. Six years earlier, Robotka at Iowa State had written: " 'The cooperative organization is a business enterprise firm' is almost universally accepted without question or verification. . ." (1947, 103). What were P's reasons for disregarding such precedent? His reasoning is quite explicit. "Although it is descriptively correct to say that a cooperative is a business organization owned and controlled by its patrons and operated for their benefit as patrons, such a statement contributes nothing to the understanding of the *economic structure* of the cooperative" (Phillips 1994, 68; emphasis added). HH were later to use the theory of the firm to explore the *economic conduct* of cooperatives. But P addressed issues about the economic structure of the cooperative. In order to explore systematically the relationships among members as they formed and operated jointly a set of marketing activities, P resorted to a vertical integration model that necessarily pretended that the cooperative was the association of farmers rather than a discretely separate firm. The test is whether the fiction is useful or not.

In contrast, HH ignored the conditions of how and why cooperation can make sense to farmers and focused on how the cooperative would set price in terms of its costs, demand for the finished products, the supply curve of the available commodity, and the cooperative maximand. They argued convincingly that any difference in the maximands of a cooperative and an investor-owned firm did not affect the treating of a cooperative as a firm in economic analysis. At the time, neoclassical theory was content with a black box about the structure of the firm. Nor were economists appreciative of the idea that different approaches might reflect different insights rather than error. Even today, many agricultural economists may question Randall's argument that "The (false) premise of much scientific pedagogy—that disagreement about the nature of material reality means at least one party is wrong—serves us poorly" (1985). Perhaps, if P had said that a cooperative is a firm, but that we can learn something about cooperating (the very core of a cooperative) by pretending it is not a firm, then HH would have seen their model as new and different but not as a correction of P.

A Correction of P's Error?

Agricultural economists generally concluded that the HH model was a correction of P's error. See Royer (1994) for his argument that the HH model was much the better. In summary, he argued that the HH model was more realistic, more workable, and more complete than P's model. The HH model is still in use. The 1989 text on cooperatives by Cobia and a committee of leading cooperative economists contains three citations of HH and only one of P. More telling, the two chapters in the Cobia text on the economic theory of cooperatives are based mainly on HH. How cooperatives would price—both up front and including patronage refunds—and whether they would close membership are issues on which the HH model throws light.

Cotterill (1987) has built more elaborate models on the HH base. He credits Royer and Enke for their contributions. Cotterill develops market equilibrium positions for a cooperative within various market structures—particularly oligopoly and oligopsony—as it is guided by alternative maximands, patronage refund policies, open or closed membership, and U- or L-shaped economies of scale. He then explores the inclusion of certain investment and finance considerations within the model. Clearly the HH formulation has been helpful.

Recent Theoretical Developments Closer to P

We have discussed the earlier classics, and especially P, in order to put the publication of HH in its historical and intellectual context. It turns out that recent theoretical developments extending the theory are more closely related to P than to HH.

Alfred Marshall (1890), the great synthesizer who invigorated neoclassical economics, treated a firm interchangeably with a single proprietor in his *Principles*. An early exception to this orthodoxy, J.R. Commons (1924), treated the firm as a going concern, an organization of people. Williamson resumed that idea more recently. "The firm as production function needs to make way for the view of the firm as governance structure if the ramifications of internal organization are to be accurately assessed" (Williamson 1981, 1539). Williamson has enriched firm theory with his emphasis on transaction costs as they affect both the horizontal and vertical dimensions of the organization of firms. His focus on the firm as a governance structure has encouraged other economists to look at the firm in organizational terms. Fama (1980) has explored the concept of a firm as a set of contracts among all its stakeholders. The usage is partially similar to that of P when he says "The cooperative association consists of the sum of the multilateral agreements among the firms participating in the joint activity. . ." (Phillips 1994, 68). The difference is that P did not conceive of calling this set of agreements a firm. Nor would his reviewers have done so in 1947. Galbraith (1967) argued that the supreme importance of information required effective control of the large firm to be in the hands of a small managerial technostructure. His firm became a set of committees—a concept that has never appealed to those academics sick of committee service.

HH chose to assume that their cooperative was managed by a person or group of persons that they dubbed a peak coordinator. While such centralized decision-making is convenient for their concept of firm as production function, it is not helpful to those interested in exploring management and control issues in large investor firms or cooperatives. Sexton

(1986) and Staatz (1987 and 1994) have used game theory in exploring some of the economics of the coalition of the stakeholders within a cooperative. They have helped us to understand how much differences in the economic interests of members can threaten a cooperative's progress and even its existence. Staatz (1994) credits P as a forerunner. Cook (1994) explored some of those issues in a context that derives more from the management than the economics literature. Sociological studies of membership structure and control of the cooperative organization are summarized in a recent *Journal of Agricultural Cooperation* paper by Gray and Butler (1994). While Cook's paper was favorably received by discussants Anderson and Lang, many economists are uncomfortable with the imprecision of management theory. That is even more true for sociological theory. But as our profession squirms from criticisms of too much attention to theory for theory's sake and an alleged lack of usefulness in attacking real world problems, it may be that considerable discomfort is a price worth paying.

In summary, the HH model is an essential tool of agricultural economists today. I have tried to show that HH 's contribution should no longer be considered a refutation of P. Their contributions are separate and complementary. Both models are more restricted than they once appeared. But we surely should not look down on those on whose professional shoulders we stand.

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