Cooperatives in Wisconsin
The Power of Cooperative Action
WHAT IS A COOPERATIVE?

A cooperative or co-op is a business that is owned and democratically controlled by the members who use its services. Cooperatives are found across the U.S. in nearly every sector of the economy.

Members who use the cooperative own their co-op because they finance it in a variety of ways. They share in both the business risks and the business profits. Each cooperative determines the level of financial participation that is required to establish membership status in the co-op.

Members democratically control their cooperative by exercising the voting rights that come with membership. In Wisconsin, each member is typically entitled to one vote.

Members benefit from the cooperative based on their use of the co-op. All or part of a cooperative’s profits may be distributed proportionately, based on each member’s use, or patronage, of the co-op.
WHY PEOPLE START COOPERATIVES

The cooperative model can be an effective way for people to meet a common set of economic or social needs. Often a cooperative is organized in response to some adversity - individual farmers face falling dairy prices, for example, or a community loses its grocery store. Instead of operating to maximize investment returns, a cooperative operates to maximize member benefit by meeting member needs in a financially sustainable way.

Cooperatives can diversify and strengthen their local economic communities because of their local ownership, control, and operations. Profits tend to remain in the local economy because they are returned to members, or reinvested in the locally based cooperative business. When members patronize their local cooperative, they are supporting employment and business activity in their communities.

Members’ active participation in a cooperative can also benefit a community’s civic life. The empowering experience of self-determination through cooperation provides a perspective and set of skills that can be applied to other community activities.

COOPERATIVES IN WISCONSIN

Cooperatives have long played an important role in the economy of rural Wisconsin. By the late 19th century, farmer-based organizations were advocating for cooperative enterprises to meet rural economic hardships. They familiarized many Wisconsin communities with cooperative stores, grain elevators, and mills. By the early 20th century, 46% of the state’s creameries and 37% of all cheese factories were farmer-owned. In the 1930s and 1940s, telephone and electric cooperatives brought those critical services to rural Wisconsin. Today, cooperatives can be found in all sectors of Wisconsin’s economy. As changes in the marketplace present competitive and economic challenges, the cooperative model continues to be an effective way for groups to respond to change and meet their shared needs.

Photo: Barron Co-op Creamery, ca. 1900 Wisconsin Historical Society

COOPERATIVE PRINCIPLES

One of the ways cooperatives differ from other business structures is their adherence to cooperative principles and values that reflect social, political, and business concerns. Cooperatives trace the roots of the cooperative principles to the Rochdale pioneers, who established the first modern cooperative in Rochdale, England in 1844. These principles have been refined, adapted, and reinterpreted over time. The seven principles used by the International Cooperative Alliance today are generally accepted by cooperatives worldwide.

Cooperatives are also based on the values of self-help, self-responsibility, democracy, equality, equity, and solidarity. Cooperative members believe in the ethical values of honesty, openness, social responsibility, and caring for others.
TYPES OF COOPERATIVES

Cooperatives operate in many sectors and can be broadly categorized by the type of members that own them.

**Producer cooperatives** are owned by members who produce similar types of goods or services. The members use the cooperative to more effectively negotiate prices and to access larger markets. The cooperative can further process member products to add value and increase producer returns. Some producer cooperatives also pool member demand for production inputs to provide better pricing on those inputs. Many agricultural cooperatives provide both types of services to their members.

**Wisconsin Cranberry Cooperative** markets the cranberries that its members grow on individual family farms.

**CROPP Cooperative** markets its organically produced milk, eggs, cheese, juice, and produce under the Organic Valley brand and its meat products under the Organic Prairie brand.

**Landmark Services Cooperative** provides its members with fuel, fertilizer, feed, grains, marketing, and agronomy services and operates retail automotive and convenience stores. *(pictured below)*

**Kickapoo Woods Cooperative** provides sustainable forestry education and management services to its landowner members.

**Q Artists Cooperative** owns and operates a gallery to exhibit and sell juried regional fine art by its members and to support the fine arts community.
Worker cooperatives are businesses that are owned by the workers. This allows the worker-members to control the operations and strategic direction of the business and to directly benefit from the business’s success. Profit distribution to worker owners is based on some combination of job position, hours worked, seniority, and salary. Worker cooperatives are found in a wide variety of industries.

*Union Cab* is a worker-owned cooperative providing taxi services in Dane County, Wisconsin. *(pictured right)*

*Isthmus Engineering & Manufacturing* is a worker-owned, engineering cooperative that specializes in automated equipment manufacturing.

*Equal Exchange* is worker-owned cooperative that distributes organic coffee, tea, chocolate bars, and other goods produced by farmer cooperatives in Latin America, Africa, and Asia. *(pictured above)*

*Cooperative Care* is a worker-owned cooperative that provides homecare services to the disabled and elderly in their homes.

*North Wind Renewable Energy* is a worker-owned cooperative specializing in solar electric systems for residential, commercial, agricultural, and governmental customers.

Housing cooperatives are collectively owned by member residents who control the housing in which they live. Residents buy membership stock in the cooperative cooperation, which usually owns the land, building, and any common areas. Residents obtain the exclusive right to occupy a specific unit.

*Homestead Cooperative of Mt. Horeb* provides 25 homes to active senior citizens who are interested in maintenance free living with all the benefits of home ownership.

*Prairie Lake Estates* in Kenosha is a 70-site resident-owned manufactured home community. The cooperative owns the land on which the member-owned manufactured homes are located.

*Madison Community Cooperative* is a non-profit housing cooperative with approximately 200 members living in 11 houses in downtown Madison.
**Consumer cooperatives** are owned by members who use the co-op to purchase the goods or services that they need. By combining member demand, the co-op can provide better availability, selection, pricing, or delivery of products or services to individual consumers.

**Group Health Cooperative of South Central Wisconsin** is a member-owned health plan providing health care services to members in Dane County, Wisconsin.

**Adams-Columbia Electric Cooperative** is a rural electric distribution cooperative that provides utility services to over 30,000 members in parts of 12 Central Wisconsin counties.

**Vernon Communications Cooperative** provides its member customers with internet, telephone, television, and security and automation.

**Outpost Natural Foods** is a consumer-owned natural food and organic grocery store, featuring quality organics and vegetarian, vegan, gluten-free, and other specialty foods. *(pictured right)*

**Heartland Credit Union** provides customized financial products and services to meet the money management goals of its members.

**REI Co-op** is a national consumer owned retail co-op dedicated to inspiring, educating, and outfitting its members and the community for outdoor adventures and stewardship.
Multi-stakeholder Cooperatives, also referred to as hybrid or solidarity cooperatives, are owned by two or more types of members who have different roles and interests in the same enterprise that more broadly benefits them all. Member classes may include consumers (either individuals or businesses), producers, workers, or investors.

**Fifth Season Cooperative** supports the marketing and distribution of regional food products through the activities of member producers, processors, distributors, purchasers, and workers.

**Weaver Street Market** is a consumer and worker owned retail grocery cooperative located in North Carolina that sells natural and organic products.

**Wisconsin Food Hub Cooperative** is owned by farmers and the Wisconsin Farmers Union. It aggregates and markets member products to wholesale markets that farmers could not easily access alone.
### COMPARING BUSINESS STRUCTURES

The legal structure of a business defines ownership, liability, earnings distribution, and control. The following table compares cooperatives to other types of business structures.

<table>
<thead>
<tr>
<th>Cooperative Corporation (WI Chapter 185)</th>
<th>Unincorporated Cooperative Association (UCA) (WI Chapter 193)</th>
<th>Corporation (C Corporation or S Corporation)</th>
<th>Limited Liability Company (LLC)</th>
<th>Partnership</th>
<th>Proprietorship</th>
<th>Non-Profit</th>
</tr>
</thead>
<tbody>
<tr>
<td>Who are the owners?</td>
<td>Members (individuals or entities)*</td>
<td>One or more shareholders (individuals or entities); An S corporation is limited to 100 shareholders.</td>
<td>One or more individuals who are members</td>
<td>At least two individuals or entities</td>
<td>Individual proprietor</td>
<td>No ownership</td>
</tr>
<tr>
<td>What are the ownership requirements?</td>
<td>Determined by bylaws, usually one share/fee per member. Bylaws may include other requirements with other rights attached.</td>
<td>One share of stock, with rights and privileges attached to it determined by the articles of incorporation, bylaws, shareholder agreement, and applicable law.</td>
<td>At discretion of LLC members</td>
<td>At discretion of partners</td>
<td>At discretion of owner</td>
<td>Membership fee may be required</td>
</tr>
<tr>
<td>Who controls?</td>
<td>Board of Directors</td>
<td>Board of Directors elected by shareholders</td>
<td>LLC members</td>
<td>Partners</td>
<td>Proprietor</td>
<td>Board of Directors</td>
</tr>
<tr>
<td>What is the primary purpose of the business?</td>
<td>Meet member needs for goods or services</td>
<td>Earn a return on owner investment</td>
<td>Provide employment for members and a return on members’ investments</td>
<td>Provide employment for partners and a return on partners’ investment</td>
<td>Provide employment for owner and a return on owner’s investment</td>
<td>Provide services or information</td>
</tr>
<tr>
<td>How is the business financed?</td>
<td>Sale of stock/shares to members and outside investors; retained profits</td>
<td>Sale of shares to patron and investor members; retained profits</td>
<td>LLC members' investments; retained profits</td>
<td>Partners’ investments; retained profits</td>
<td>Proprietor’s investment; retained profits</td>
<td>Grants, individual contributions, fees for services</td>
</tr>
<tr>
<td>Who receives the profits?</td>
<td>Members in proportion to their use; preferred shareholders in proportion to investment</td>
<td>Shareholders in proportion to investment</td>
<td>LLC members in proportion to investment or by agreement</td>
<td>Partners in proportion to investment or by agreement</td>
<td>Proprietor</td>
<td>Retained within the organization</td>
</tr>
<tr>
<td>Who pays income taxes on the profit?</td>
<td>Members on qualified profit allocations profit and cash distributions**; co-op pays on nonqualified and unallocated profits</td>
<td>C corp. pays on profits, shareholders pay individual capital gains rate on dividends; S corp. shareholders pay individual rate on profit share and capital gains</td>
<td>LLC members pay individual rate, or can elect to be taxed as a corporation</td>
<td>Partners pay individual rate</td>
<td>Proprietor pays individual rate</td>
<td>Not applicable; tax exempt</td>
</tr>
<tr>
<td>What is the owner’s legal liability?</td>
<td>Limited to members’ investment in the cooperative</td>
<td>Limited to members’ investment in the UCA</td>
<td>Limited to shareholder’s investment in the corporation</td>
<td>Limited to LLC member’s investment in the LLC</td>
<td>Unlimited for general partners, limited to limited partner’s investment in the partnership</td>
<td>Unlimited for owner</td>
</tr>
</tbody>
</table>

*Preferred stock shareholders may include nonmembers, and may only vote on limited issues such as dissolution. As a group, preferred stock shareholders do not set policy. Only members have full voting rights and can vote for the board of directors.

**Members of personal consumer co-ops do not pay taxes on patronage allocations that follow certain IRS guidelines.

There may be exceptions to what is summarized here. See statutes for further information.

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Effective cooperative operations depend on four groups: members, the board of directors, management, and employees.

**Members** own the cooperative, which is organized and operated for their benefit. Members are expected to financially support the cooperative business by investing in it and by using its services. Without these activities, cooperative operations may not be sustainable.

Members usually exercise control of the cooperative by voting to elect a board of directors to act on their behalf. Members also directly vote on changes to articles of incorporation and bylaws, and on cooperative mergers or dissolution. In Wisconsin, each cooperative member typically receives one vote. Members must understand the issues facing their cooperative so they can make informed voting decisions. Member communication and education programs are essential for informed decision-making and are a sound investment in the cooperative’s future.

The **board of directors** establishes long-term business strategies that balance the needs of the membership with the cooperative’s financial sustainability. They review and evaluate all financial reports, assess the capital needs of the cooperative, and determine patronage refund allocations. They establish operating policies and are responsible for hiring and evaluating the general manager. Directors must avoid conflicts of interest so that their decisions serve the needs of the entire cooperative, rather than specific member interests within the business.

A cooperative’s **management** is hired by the board to carry out its strategies and objectives. The general manager or CEO oversees the day-to-day operations of the cooperative and reports on the co-op’s financial and operational performance to the board. The general manager makes recommendations for long-range planning and develops the budget for board approval.

A co-op’s **employees** carry out cooperative operations that provide the goods and services needed by the members. Employee understanding of cooperative principles and objectives can be an important part of positive member relations. In the case of worker-owned cooperatives, the management and employees may also be members.
COOPERATIVE FINANCE

A cooperative, like any business, requires money, or capital, for start-up, stability, and growth. Cooperatives can use both debt and equity to meet their capital needs.

**Debt** is money that is borrowed and must be paid back to the lender with additional interest payments. Banks or other financial institutions are the usual sources for loans to businesses, including cooperatives. While lenders may be financing a significant portion of a cooperative’s capital needs, lenders do not have ownership rights.

**Equity** is money that is invested in a business without a guarantee of payback or financial return. The “at risk” capital entitles the investor to share in ownership, control, and any business profits or losses. Equity provides businesses with capital without interest expense or fixed payback obligations.

Cooperative members make equity contributions that give them ownership and control rights in their cooperative. These rights enable them to prioritize cooperative operations that meet their needs instead of increasing investment returns.

**Sources of Cooperative Equity**

**Membership equity requirements**
Membership in a cooperative requires an equity payment, usually through purchasing common stock or a membership certificate. The stock cannot be traded and does not appreciate. Each co-op determines the cost of becoming a member and must balance its need for capital with the members’ ability to pay.

**Retained earnings**
When a business is profitable, the owners may decide to retain all or a portion of the earnings and reinvest them in the business. In a cooperative, profits may be allocated to members based on their use, or patronage, of the cooperative. These patronage allocations may be distributed to the member as a refund, retained as **allocated** equity in the member’s name, or a combination of both. A portion of net profits may be retained and collectively held as **unallocated** equity in the cooperative. Typically, unallocated equity is the profit from business conducted with non-members.

The board of directors makes decisions annually about profit allocations and redemption of past retained patronage allocations. The board considers the co-op’s capital needs, its members’ needs, and its tax position.

**Per unit retains**
Per unit retains are often used by producer co-ops. The co-op retains a percentage of each financial transaction with a member for products that it receives or purchases. The retained payments are credited to member equity accounts.

**Preferred stock**
Wisconsin co-ops may raise equity capital by selling preferred stock to members and non-members. Preferred stock offers a dividend but does not grant member voting rights. Dividends are paid out of the cooperative’s net profits, but are not guaranteed and are made at the discretion of the board.

**Other Approaches to Cooperative Financing**
Cooperative start-ups that are capital intensive may require more equity than members can provide. Accumulating the retained earnings needed for new capital-intensive investments may be difficult for cooperatives, which operate to benefit members rather than to maximize profits. Some states, including Wisconsin, have adopted hybrid cooperative laws that allow both investor and patron members. Patron members determine whether non-patron members may vote and receive a portion of net profits based on investment. In Wisconsin, these hybrid cooperatives are called Unincorporated Cooperative Associations. See page 8 for more information on this model.
Cooperative Profit Distribution and Taxation

Cooperatives are taxed differently than other types of business. A cooperative pays taxes at the corporate rate on the net profit that is retained as **unallocated** equity. Members pay taxes on the net profit that is **allocated** to them on the basis of patronage. Allocated patronage can be designated qualified or nonqualified.

Members pay taxes on patronage allocations that are retained and designated as **qualified**. At least 20% of the qualified allocation must be distributed to members in cash to help pay the taxes they owe on the entire patronage allocation. This method provides a way for members to make ongoing equity investments in the co-op in proportion to their patronage. There is an expectation that the retained allocations will be redeemed over time, since the member has paid taxes on them.

If patronage allocations are retained and designated as **nonqualified**, the co-op initially pays the taxes at the corporate rate. When nonqualified retained allocations are distributed to members at some point in the future, the member pays the required tax and the cooperative receives a tax credit. Since the member has not paid taxes on nonqualified retained allocations, there is less pressure to redeem this type of retained equity.

In consumer cooperatives, where members conduct business for personal use, patronage allocations are treated like refunds and are not subject to income tax.
HOW TO START A COOPERATIVE

Starting a cooperative presents a unique opportunity for a group of people to meet a shared economic or social need. As democratically governed businesses, cooperatives can be a great way to structure businesses that are guided by member values.

Starting a cooperative can present challenges. Cooperatives are subject to the same market forces and economic conditions that other businesses face. The demand for the co-op’s goods and services must generate enough revenue to offset both the risk of investing and the costs of operating the business. People will bring many different perspectives to the development process, and the common interest that runs through these differences must be identified.

As with any new venture, starting a cooperative requires good ideas, expertise, time, energy, and money. It can take six months to two years, sometimes longer, for a co-op to go from an initial concept to launch.

The following are basic guidelines for starting a new cooperative, but each new cooperative is unique. The manner in which the momentum, people, and money come together will vary. Often the circumstances of a particular start-up venture require that some steps occur simultaneously or in a different sequence. However, each of the steps described below is a logical point at which organizers can evaluate a cooperative’s progress and decide whether or not the effort should move forward.

Stage 1: Explore

Identify the opportunity and gauge interest

A core group of individuals explores an opportunity or common need for a particular product or service. They identify the benefits that a cooperative approach might offer and reach out to a broader group or community to gauge interest in the idea. This group organizes informational meetings for potential members to further define a common need. It also recruits others who have the skills and expertise required to lead the cooperative development process.

Form a steering committee

If there is enough initial interest in the cooperative idea, it is time to establish a steering committee. The steering committee should be made up of trustworthy individuals who have good business sense, will champion the project, and are capable of putting the interests of the group before their own. Many potential cooperative members will base their support of the cooperative on the credibility of the steering committee members. The steering committee:

- Gathers more information on the cooperative option and potential member support;
- Refines the business idea and its initial mission, purpose, and goals;
- Manages financial matters in a responsible and trustworthy manner;
- Leads decision-making during the cooperative development process.
Stage 2: Assess

**Conduct a feasibility study**
The steering committee coordinates a feasibility study to assess the viability of the proposed cooperative venture. This study examines whether there is a market for the new cooperative’s products or services, and whether the co-op can generate enough revenue to cover the risks and costs of operating the business. It should be completed by someone who is knowledgeable about the particular business sector and does not have a vested interest in the study’s outcome. This study is a key step in the development of the cooperative. The group may need to pay for the study by conducting the first phase of a membership drive, or by applying for funding from federal, state, or non-profit agencies.

A feasibility study includes:
- Market analysis;
- Management, equipment, and facility needs;
- Revenue projections;
- Sources of financing;
- Potential membership base.

**Evaluate feasibility study results**
The results of the feasibility study help the steering committee decide whether to continue the cooperative development process. This is a critical decision point during the development process.

Stage 3: Incorporate

**File articles and adopt bylaws**
If the feasibility study indicates the concept is viable and the steering committee decides to move forward, the group may decide to legally incorporate as a cooperative. In Wisconsin, the group can choose to incorporate under Chapter 185 or Chapter 193 of the state statutes by filing Articles of Incorporation with the Wisconsin Department of Financial Institutions. The Articles provide the basic organizational information required by state statutes.

The steering committee often acts as the interim board of directors. It may draft the Articles and the initial set of bylaws, which describe how the cooperative is governed. Articles and bylaws should be reviewed by a lawyer familiar with cooperatives. Bylaws must be adopted or amended by the cooperative’s members at the first membership meeting.

**Open a bank account**
Once the cooperative is established, the interim board of directors should open a bank account for cooperative financial transactions. In many cases, a group will incorporate earlier in the process so that the cooperative can receive funds and pay initial expenses.

Stage 4: Plan

**Prepare a business plan**
A business plan is an in-depth analysis of and plan for the cooperative business. It is also an important communication tool for answering questions that potential members will have about the proposed cooperative. Banks and other funding sources will want to assess the business plan as part of their financing decisions. The business plan includes:
- Description of the goods or services offered;
- Market analysis;
- Marketing plan;
- Operational plan;
- Description of the management and ownership structures;
- Sources and uses of start-up funds;
- Projected financial data for the first five years of operations.

**Elect a board of directors**
A membership meeting is held within six months of incorporation to elect the first board of directors and to present and approve the bylaws. The board of directors begins coordinating the business plan implementation and works to secure start-up capital.
Stage 5: Capitalize

Begin membership drive
The membership drive will indicate whether there is sufficient member support for the new cooperative. Materials for prospective members should clearly explain the cooperative’s mission, the financial requirements for membership, and the risks and benefits of membership. Some groups launch the membership drive earlier in the development process.

Secure start-up capital
A cooperative may use both debt and equity to meet its initial capital needs. Cooperatives may also use member loans or preferred stock to raise start-up capital. Lending institutions will evaluate the risks associated with making a loan to the start-up cooperative business by analyzing the financial projections in the business plan and ensuring the co-op has capable staff lined up. Lenders will also look at the amount of member equity invested in the cooperative, since this indicates the level of risk and commitment that members are willing to assume. Members will typically be expected to supply 30-50% of the start-up equity capital. The cooperative will need to borrow the balance from a financial institution. Banks, credit unions, and loan funds that are specifically oriented to cooperatives and understand their unique structure can be important resources.

Stage 6: Launch

Hire staff
The board hires a general manager, who plays a key role in securing the operations site, developing vendor networks, and hiring additional staff. Some groups hire staff earlier to assist with the development process.

Address licensing, regulatory, and insurance requirements
There are often specific licensing or regulatory requirements that must be met before the business can begin operations. Legal, insurance, and risk management issues must also be addressed before launching.

Commit to ongoing training and education
Ongoing member education and board training are vital to establishing a sustainable foundation for successful cooperative operations. Education topics might include the cooperative model, cooperative finance and governance, industry trends, and working together effectively.
COOPERATIVE CONVERSIONS

Another way to start a new cooperative is to convert an established business to the cooperative structure. This most commonly occurs through the sale of the business to its employees, but transitions to consumer ownership are also possible. Factors that influence the process and successful outcome of the transition include:

• Management style, culture, and financial stability of the established business;
• Transition timeline and process;
• Development of management and governance systems;
• Availability of financing, technical assistance, and professional advisors.

FACTORS THAT CONTRIBUTE TO SUCCESS

Certain common characteristics are often cited as influencing the successful development of a new cooperative. Successful new co-ops:

• Maintain alignment around a clearly defined mission, purpose, and focus;
• Use committees, advisers, and outside expertise effectively;
• Keep members informed so that they stay involved and supportive;
• Complete a thorough and accurate feasibility study and/or business plan;
• Secure adequate financing and financial commitment from members;
• Conduct business-like meetings by using agendas, parliamentary procedures, and democratic decision-making;
• Hire competent management to run the cooperative’s operations;
• Maintain good board-management relations by clearly defining roles and responsibilities;
• Follow sound accounting practices and present financial reports regularly;
• Identify and minimize business risks;
• Develop clear policies on confidentiality and conflict of interest;
• Develop alliances with other cooperatives.

RESOURCES FOR STARTING A COOPERATIVE

Reading about cooperatives and talking to knowledgeable people is a great way to learn more about starting a cooperative business. The website of the University of Wisconsin Center for Cooperatives is another resource for learning about cooperatives. The website offers an array of information, contacts, publications, and articles related to cooperatives. [www.uwcc.wisc.edu](http://www.uwcc.wisc.edu)

Knowledgeable staff at UWCC can provide a wide range of resources and assistance to individuals, groups, and cooperatives. Contact us at:

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The University of Wisconsin Center for Cooperatives fosters critical thinking and understanding about cooperatives through research, education, and outreach programs. It also provides technical assistance to groups interested in starting new cooperatives. The University of Wisconsin Center for Cooperatives is an interdisciplinary center that leverages the resources of University of Wisconsin-Madison and the University of Wisconsin-Madison Division of Extension.

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