**Understanding Hybrid Member-Investor and Multi-stakeholder Cooperatives**

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Most cooperatives are focused on a single group of user and distribute benefits to those users. Examples would include agricultural cooperative owned by farmers, retail cooperatives owned by consumers or taxi cab cooperatives owned by workers. In recent years, two new modified cooperative structures have emerged: the member-investor cooperative and the multi=stakeholder cooperative. The goal of these structures is to address limitations of traditional cooperative structures and/or extend the purpose of the cooperative.

Hybrid Member-Investor Cooperatives

The original Rochdale cooperative principles directed that returns on invested capital should be limited to no more than 8% and that the majority of profits should be distributed to users in proportion to use. Most U.S. cooperatives have focused entirely on patronage and not provided any return on invested capital. Under the traditional cooperative form the equity is not traded and cannot appreciate. That limits the incentive to invest in the cooperative since the return on investment must come through future patronage. Closed cooperatives link an appreciable usage right with equity which provides an indirect incentive for investment. Despite that incentive, many closed cooperatives have had difficulty raising capital since the pool of potential investors is limited to agricultural producers who are in a position to deliver to or use the cooperative.

The closed model has worked well for sugar beet and specialty crop cooperatives. In those situations, the cooperative’s processing and marketing activities were critical to the farm operation. As farm operations transitioned to the next generation, the younger producers were eager to purchase delivery rights. In other situations, such as ethanol cooperatives, the market for usage rights was more problematic. The original ethanol cooperative members were interesting in diversifying into value added activities. As they neared retirement age, many of the younger producer faced more attractive profits on the farm as well as escalating land and equipment costs. They were not as willing or able to invest in usage rights in ethanol cooperatives.

Cooperatives can issue preferred stock but the dividend rate is often limited by law to no more than 8%. Even if a cooperative is not subject to the 8% maximum, preferred stock generally pays a fixed dividend. The preferred stock dividend can be suspended if the cooperative does not have the capacity to pay it. Preferred stock is not closely linked to profitability because the dividend rate is fixed. CoBank and some of the large regional cooperatives have made use of preferred stock. Overall, preferred stock has not proved to be an effective method of raising outside capital.

The hybrid member-investor cooperative combines the investor owned firm model with the cooperative business model. As the name implies there are two classes of members, users and investors. The profits are split according to some established formula. The investor side distributes profits based on ownership while the cooperative side distributes profits based on ownership. Prior to the passage of statues enabling member-investor cooperatives, groups used to form three entities. A top level LLC to distribute profits to two other entities, an investor owned LLC and a cooperative. The member-investor statues simply facilitating that structure within a special cooperative entity.

There are inherent challenges with the member-investor model. The two membership groups have different incentives. Issues such as commodity prices become controversial. If a marketing cooperative were to offer favorable prices, the user members would benefit from the prices at the expense of the investor members who would receive less profit. Many new cooperative incorporate under the member-investor statutes just to maintain the flexibility. So far, there have not been many good examples of merging investors with user members.

The member-investor model also creates issues with compliance with cooperative principles. Cooperative principles suggest that members should vote on a one member-one vote basis or in proportion to business model. Investor members in a hybrid cooperative generally vote in proportion to investment, which is not in accordance with cooperative principles. The investor members also share in profits in proportion to ownership and that differs from the cooperative principle of benefit in proportion to use. Hybrid member-investor cooperatives would likely not be eligible for Capper Volstead protection and may face issues with CoBank eligibility, Sub-Chapter T taxation and SEC Security registration exemption.

Multi-Stake Holder Cooperatives

Many traditional cooperatives have members who use different aspects of the cooperative. For example, a grain and farm supply cooperative may have producers marketing grain and other producers who only purchase inputs. Credit unions have both depositors and borrowers. In both of those examples, the members are still in a similar group (producer or consumer). In a multiple stakeholder cooperative, there are more than one type of member. For example, a local food cooperative could have both consumer members and producer members. It could even also have worker members. Some stakeholders discuss multi-stakeholder cooperatives as part of a “solidarity model”. They want to expand the scope of the cooperative’s value package to a broader set of stakeholders.

The multi-stakeholder model requires defining multiple groups of membership and allocating governance and patronage across the groups. The multi-stakeholder model involves more individuals from the cooperative and provides incentives to additional groups. For examples, bringing the employee group in as members provides them “skin in the game” and additional incentives to remain as long term employees. The multi-stakeholder model can also increase the pool of equity capital since additional groups are investing or receiving profits in the form of equity.

The disadvantage of the mult-stakeholder model is that it is more complex and creates more potentials for conflicts. The various stakeholder groups obviously have different incentives. For example, worker members would lobby for increased wages while producer members would prefer reducing personnel costs. In designing their structure, the cooperative has to decide the investment of each group, how patronage is split across the groups and how the governance rights of each group. The various groups often have different time horizons and different economic situations. The structure may lead to dominance by one group or provide each group with equal power and benefits. Both alternatives can lead to difficulties. Even if the cooperative is able to navigate a fair structure, one group may evolve to dominate the cooperative over time. For example, there may be more members in one group or one group may have better information and be more active in govenance.

There are examples of successful multi-stakeholder cooperatives including Weaver Street Market in Carrbora North Carolina. Weaver Street Market is a worker and consumer owned cooperative selling natural, organic and locally based foods and operates at multiple locations in North Carolina. The worker members and consumer members have equal representation on the board of directors. In recent years, many groups have examined the success of Weaver Street Market and have investigated the multi-stakeholder model.

Given the challenges of navigating the multi-stakeholder model, many groups ask if there are alternatives. There are partial alternatives within the single stakeholder model. Consumer cooperatives often encourage their employees to become consumer members. That does not align the employee interest with the consumer members but does provide more employee engagement and understanding of the cooperative model. Multiple patronage pools facilitate different sub-classes but do not really address additional types of members. Some cooperatives appoint a non-voting employee delegate to report to the board of directors. That provides a partial alternative to create more employee engagement and loyalty.

Modeling Alternative Cooperative Forms in Your SYOC Project

The feasibility templates we use in class model traditional open membership or new generation, closed membership cooperatives. They do not explicitly model member-investor or multi-stakeholder cooperatives. Member-investors cooperative could be modeled by issuing preferred stock. In the real world, profits vary from year to year so a fixed return through preferred stock is very different from receiving a share of profits based on ownership. Because the returns we model through the template are stable a hybrid cooperative could be modeled by issuing the appropriate level of preferred stock and the dividend rate. As in any hybrid cooperative, the returns to investor members through the preferred stock reduces the investment of the user members but also reduces their patronage return.

The feasibility templates report the total cash and stock patronage as well as equity retirement payments. In your report you may want to convert those returns to a per-unit or per-member basis. If you are modeling a multi-stakeholder cooperative, you need to define how you will split the patronage and then describe the returns to each group. In other words, you would need to convert the total returns to the returns received by each group. You would also need to describe how your board is structured and the voting rights and board representation of each stakeholder group.