

# Member Control of Cooperatives: What It Means and How It Is Exercised

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One of the fundamental principles of cooperatives is that they are controlled democratically by the members who use them. "Democratic" is most often defined as one vote per member<sup>1</sup>, regardless of investment in or volume of business conducted with the cooperative. This publication was designed to help members and managers understand what control means and how it is exercised.

## Member rights and responsibilities

Members are the foundation of the cooperative business. Member needs are the reason for the existence of the cooperative. Member support through patronage and capital investment is essential for the cooperative's economic health.

Cooperative membership carries rights and responsibilities. Rights of cooperative membership may include:

- Adopt and amend the articles of incorporation and bylaws.
- Elect and, if necessary, remove directors of the business.
- Dissolve, merge, or consolidate the cooperative or form a joint venture with others.
- Require officers, directors, and other agents to comply with the law under which the business was set up, and with its articles of incorporation, bylaws, and membership contracts.
- Hold directors and officers liable for damage injurious to members.
- Examine the annual reports.

Responsibilities of cooperative membership includes:

- Patronize the cooperative.
- Be informed about the cooperative.
- Be engaged in selection and evaluation of directors.
- Provide necessary capital.
- Evaluate the performance of the cooperative.<sup>2</sup>

## How members exercise control

A cooperative is a user/owner (democratically) controlled form of business; however, in most cooperatives, members cannot make all the decisions directly. Members exercise control over a cooperative directly by voting at membership meetings and indirectly through election of a board of directors. State Incorporation Statutes require the board to manage the cooperative and give it wide latitude in doing so. The board also may be restricted by provisions in state statutes, articles of incorporation, and bylaws that specifically reserve control of certain matters to the membership. In most cooperatives, few issues are reserved for the membership to decide. Therefore, the way members usually exercise control is through election of a board of directors.

All types of corporations have boards of directors. All boards are responsible for representing the interests of owners, protecting the public interest, and assuring proper management for the corporation. The board of directors' highest obligation is the fiduciary responsibility to preserve the financial integrity of the cooperative. Also the board has a responsibility to keep the members informed about the cooperative.



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## Contents

Member rights and responsibilities

How members exercise control

Actions members should take

Control versus management

Limitations and a major problem of member control

Conclusion

Notes

## Related programs

- [Agricultural Business and Policy Extension](#)

## Related publications

- [Basics of Missouri Agricultural Cooperatives](#)
- [Basics of Agricultural Cooperative Taxation](#)

Responsibility for management is far different from managing. The board's responsibility for management is exercised by employing professional management personnel and monitoring their performance.

The amount of authority and responsibility delegated to management is largely left to the board. Each board must decide what "control" means. Maintaining control does not require numerous actions at every board meeting. If no major policy decisions need to be addressed, an appropriate course of action is to monitor activities and performance.

While all boards have the same general responsibilities, the board of a cooperative differs greatly from the board of an investor-owned firm (IOF) and the differences are consistent with the principle of member control. People who serve on the board of a cooperative are members of the co-op, selected by other members. Board members of IOFs are selected by the board (although approved by owners) and might have no business relationship with the corporation.

### **Actions members should take**

Since much of the control authority is delegated to the board of directors, the most important single action a member can take is to actively participate in the director selection/election process. The procedures followed by cooperatives for securing directors vary widely. Some co-ops use nominating committees. Others nominate two people for each open board slot. Others allow people to "run" for the positions. The procedure a particular co-op follows should be specified in the bylaws.

More important than the election procedures is selecting the "right" people as directors. Essential requirements include actively patronizing the co-op, having no conflict of interest with the co-op, and making a commitment of time to the job. This means the person must also make a commitment to learn the business and learn how to become an effective director. General leadership characteristics are highly desirable.

Incorporation statutes outline methods that show members how to take direct action. Almost all co-ops in Missouri are incorporated under Chapter 274 or Chapter 357 of the Missouri Statutes. Chapter 274 specifies there must be at least one membership meeting a year, with members notified at least 10 days in advance. Further, 10 percent of the members may petition for a special meeting to accomplish specific business. If they petition, the directors must call a meeting. The chapter also outlines procedures for initiating the removal of a director.

Chapter 357 specifies the board of directors manages the general affairs of the co-op but says business policies are controlled by the shareholders (members). Policies specifically mentioned are: declaring dividends; setting aside reserve funds; establishing the method of distributing profits; amending the articles of incorporation, increasing and diminishing capital stock; and other general policies. The chapter also provides for removal of a director for cause at any annual or special meeting.

### **Control versus management**

Member control is quite different from management. It is the task of management to faithfully pursue the goals and policies of the membership and to periodically report on performance. Management should have the right to make a wide range of decisions on a day-to-day basis. Examples include establishing prices, hiring and firing employees, selecting vendors, preparing work and delivery schedules, and establishing daily priorities. Members cannot maintain control, however, unless their elected representatives (the board of directors) retain and exercise the right of employing and evaluating management and making necessary managerial changes.

The membership can and should delegate actual management to a professional manager. Professional managers have many skills the typical member does not have. Further, management of an enterprise of any significant size is a full-time job. Perhaps of even greater importance is the timeliness of decisions. If members become involved in day-to-day operations, it will almost certainly lead to poor performance of the

cooperative. Management must have the flexibility to fail as well as to succeed and be rewarded accordingly.

## **Limitations and a major problem of member control**

Members often face external restraints when policy decisions are made. Laws must be obeyed. Cooperative lenders, suppliers and customers may also place restrictions on policies. Such restrictions do not violate the principle of member control. In fact, a precise wording of the principle would be, "members control the cooperative subject to legal and institutional constraints and the realities of the economic situation faced by the cooperative."

A cooperative faces a dilemma in representing the views of its membership. If operating properly, the cooperative reflects the views of a majority of members. A member who is in the minority has three options: bow to majority rule, solicit support for the minority view, or leave the co-op.

Another constraint is the number of members who vote on issues relating to control. In many cooperatives, voting occurs at a membership meeting called for that purpose. Others permit proxy voting, voting by mail, or a combination of meeting, proxy, and voting by mail. Regardless of the method, the percent of members voting is usually low. Those who do vote set policy and those voters may or may not be representative of the membership.

## **Conclusion**

Members can control their cooperative by many means. An essential ingredient is being actively interested in and participating in co-op activities. Without member interest and participation, there is no guarantee members will control the cooperative or that the cooperative will serve the interests of the members.

## **Notes**

1. The Missouri Cooperative Associations Act, part of Chapter 351 of the Revised Statutes of the State of Missouri, grants flexibility to the principle of one member one vote. Under Chapter 351 the cooperative may choose to vote on the basis of patronage rather than one member one vote. However, electing to vote based on patronage may adversely impact whether the cooperative meets the requirements of Subchapter T of the Internal Revenue Code. The Missouri Act also gives the cooperative the option to choose to be taxed as a partnership, providing tax treatment similar to Subchapter T, without some of the restrictions. However, forgoing Subchapter T requirements involves additional considerations including Capper Volstead protections and whether or not cooperative debt/equity may be considered "securities". For more information regarding a comparison of the benefits of alternative incorporation structures for cooperatives in Missouri, seek the advice of qualified legal counsel and refer to the Revised Statutes of the State of Missouri.
2. For more information on members rights and responsibilities see U.S. Department of Agriculture (USDA) Cooperative Information Report 11 and Cooperative Information Report 45 listed below.

## **References**

Ginder, Roger G. and Ron E. Dieter, "Managerial Skills, Functions, and Participants" in David Cobia (ed.) *Cooperatives in Agriculture*, Prentice-Hall, 1989, p. 322.

U.S. Department of Agriculture, [Cooperative Information Report 45, Section 4. Understanding Cooperatives: Who Runs the Cooperative Business? Members](#) (PDF).

U.S. Department of Agriculture, [Cooperative Information Report 11, "Co-op Essentials: What They Are and the Role of Members, Directors, Managers, and Employees"](#) (PDF).

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