Management

Management is the most critical aspect of the plan. The reader must have confidence in your management team and its ability to implement this plan. Do not be modest, but, at the same time, do not be boastful.

Points to cover are:

1. Key Personnel
   Key management personnel and their duties and responsibilities. Resumes should be included in the supporting documents to show management has experience and skills needed to manage the company. Emphasize past successes and current role in the business.

2. Management Team
   Discuss how the management team's education, training and/or experience will help the company succeed.

3. Reporting Relationships
   Organization chart, salary structure and ownership share.

4. Directors and Advisors
   Board of Directors and outside advisory services.

5. Staffing Plan
   Discuss management needed in the organization, how you will fill key slots, hiring plans and the date positions will be filled.

6. Business Organization
   Form of business organization.

7. Ownership
   Names of stockholders and shares owned.

8. Management Duties
   Discuss the managers or private firms who will handle the management duties. Include internal control systems for accounting, inventory and management information reporting systems.

9. Other Investment
   Amount of money invested by owners.

10. Management's Competitive Advantage
    Unique competitive advantage from management experience or skills.

Sample Management

Management

1 Key Personnel and Management Team

2 The general manager of Family Farmers Choice will be Bailey B. Line. It is felt
that with his experience in processing and distributing pork products derived
8 from specialty grown, identity preserved hogs, that he would have the required
knowledge and perspective required for success. Also, because of his key role
as the organizer of the enterprise, he would be highly motivated to assure its
success.

A plant manager will oversee day-to-day operations. Larry Line, former owner of Larry and Linda's Locker Plant, has been employed to fill this role. His overall responsibility begins with acquiring the hogs to be processed, processing the hogs into products and then delivering products to customers. The concept of total material management will be used in order to assure a smooth product flow from start to finish. Accordingly, purchasing and scheduling will also be the plant manager's responsibility. Supervisors over production workers will report to the plant manager as well as the maintenance supervisor.

10 The quality control manager will report directly to the general manager. Ted Tobias, a former federal meat inspector, has been appointed to this position. His task will be to assure that pork products are processed in a safe and sanitary manner, so much so that Family Farmers Choice exceeds USDA standards. The reason for reporting directly to the general manager is that producing safe products will be one of the key marketing strategies. To assure positive inspection decisions, the quality control manager must be free of processing and delivery pressures.

The marketing manager will also report to the general manager. Linda Cook has been employed to fill this position. She has extensive experience both as a chef and manager of several upscale restaurants. She has a degree in institutional management from Iowa State University and is presently working towards her MBA with an emphasis in marketing. Her task, in addition to being responsible for sales and advertising, will be to identify new markets, be alert to new product trends and to maintain excellent customer relationships. She will also be responsible for keeping the independent hog producers involved in the marketing process as well as keeping them informed with respect to sales and product trends.

An accounting manager will carry out accounting and financial functions. Tina Total has been employed for this position. The emphasis for this position will be on day-to-day cost and financial management tasks – with auditing and tax reporting being carried out by a CPA firm. This person will also be responsible for the management information system. As part of the MIS responsibility, the accounting manager is responsible, in cooperation with other managers and supervisors, for developing and implementing appropriate performance standards. At least in the early stages, this person will serve as the office manager. Total has a degree in accounting and a minor in management information systems, and has experience as a cost accountant in a job shop.

Since each manager will be responsible for his or her own hiring, Family Farmers Choice will not employ a human resources specialist. It will rely on the state Workforce Development offices to do the initial screening. The accounting manager will maintain employee records and files as part of her office management responsibilities.

As outlined in the description of duties for the accounting manager, a computer-based management information system will be installed. It is anticipated that the system will provide current operating data on a real-time basis for each person needing that data. In addition, it will provide highly detailed cost/volume/profit data by batch, product, distributor type and distributor name.

An Intranet Web site will be installed for order processing purposes for the convenience of customers.

Another Intranet Web site will be designed for producer members. This will provide them instant access to sales statistics and operating statistics, customer feedback and pertinent general information. Also it will serve as a means of communication with other members and managers. They will be able to use this Web site to raise concerns, ask for advice and share information.

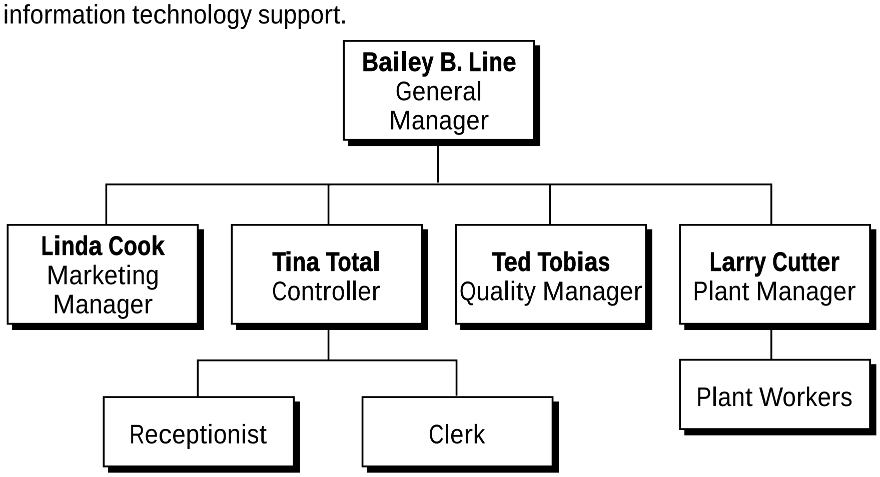
3 Reporting Relationships

The company will be managed with a traditional organization structure. Salaries will be as follows:

- Bailey B. Line — $55,000 (Salary is low, but he shares in profits.)
- Larry Cutter — $45,000 (Shares in profits.)
- Ted Tobias — $ 35,000
- Linda Cook — $30,000
- Tina Total — $35,000

7 Bailey Line is an equal owner in the venture along with other coop members. Larry Cutter will get a share of the profits. The distribution formula is not yet set, based on attainment of performance goals.

8 Global Accounting, Big City, IA, will be employed as the corporate accountant. Computer Specialists, also of Big City, will be retained to provide computer and information technology support.



4 Board of Directors and Advisors

The general manager will report to the board of directors elected by the coop members. Members will serve on the board on a rotating basis to assure turnover and full member participation. The board will select a chairperson. The length of each term will be designated in the coop by-laws.

The current Board of Directors is composed of Bailey B. Line and several advisors from public business assistance agencies, such as the Center for Industrial Research and Service (CIRAS), USDA Rural Development, SCORE and local and state economic development interests.

Persons on the Board of Directors are: Albert Banks, Carl Demarco, Ernie Fillman, Gina Hilton, Irene Jones, Kevin Leonard and Marvin Nelson. All of the board members live in the surrounding greater Midlands area and are largely, but not exclusively, representative of the pork business.

In addition to the board of directors, three standing committees, also composed of the members, will be formed to oversee areas of quality assurance, marketing and processing.

Quality Assurance: The purpose of the quality assurance committee is to assure that hogs are raised according to the standards established by the cooperative. Members will make site visits to conduct compliance audits, provide advice to hog raisers when asked and stay apprised of current research and methods in open range practices. In addition, they will work with the marketing manager to immediately address quality concerns. They also will contract with a veterinarian to provide health care and advice to the committee and hog raisers, and to assure that hogs are receiving treatment in accordance with cooperative standards.

Marketing: This committee will work proactively with the marketing manager to provide promotional assistance. In addition, it will help organize marketing and promotional assistance and assure that all members participate.

Processing: This committee will focus on the processing plant to assure that inspection standards are maintained and that employees are working in a safe environment. Members will stay apprised of the latest processing technology and will make recommendations about investments for processing and related equipment.

5 Staffing Plan

At the present time, with the management team listed above and with the purchase of Larry and Linda's operation, no additional hiring is anticipated.

6 Business Organization

While organized as a cooperative, in terms of operations, Family Farmers Choice will function similar to a conventional corporation. The coop members are the stockholders who employ salaried managers. Profits in excess of agreed upon reinvestment requirements will be distributed to members based upon their ownership share. (In addition, the members will receive a premium price for each hog delivered at the time of delivery.)

7 9

Ownership

Coop members and their ownership share will be supplied as needed by lenders. The document is considered confidential and is, therefore, not included here.

There are no other investors in this business.

Establishing Management for Your Business

In a small business, like the business of owning and operating a farm operation, there often are few staff people with many duties. Husband and wife teams are frequently a key factor to success of a business. One person operates the production and marketing aspect of the business, the other handles the office, finances and sometimes the marketing.

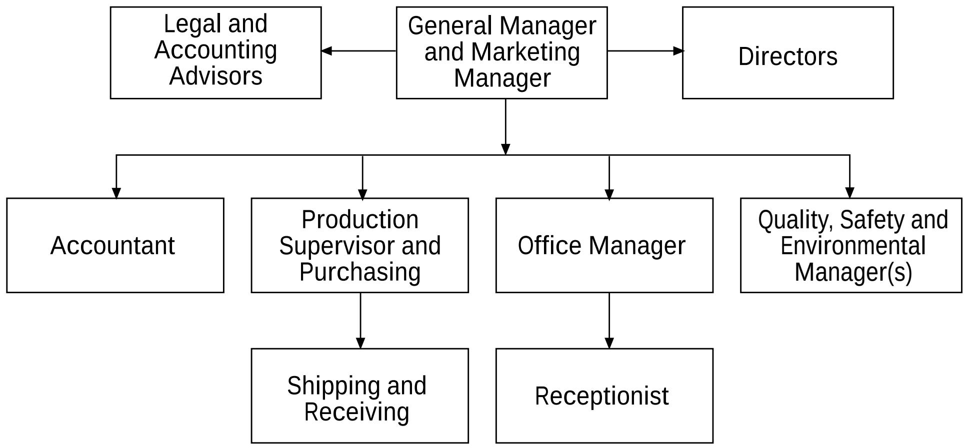
Key Personnel

Key personnel in a small business and their duties include:

- **President, owner or general manager.** This individual is the leader for the operation and has overall responsibility for the financial success of the business. He or she handles external relations with lenders, community leaders and vendors. Frequently, this individual also is in charge of either production or marketing for the business. This person will set in motion the vision, strategic plan and goals for the business.
- **Quality control, safety, environmental manager.** This is a key function in any industry and, in particular, one that deals in food products. In a small business, one person generally will be responsible for handling OSHA compliance, EPA compliance, monitoring air and water quality, product quality, training of employees in each of these areas and filing all necessary monthly, quarterly and yearly reports.
- **Accountant, bookkeeper, controller.** This is another key function. The individual filling this role has the responsibility for monthly income statements and balance sheets, collection of receivables, payroll and managing the cash. The key aspect here is managing the cash.
- **Office manager.** The person in this slot also may serve as human resource director, purchasing agent and “traffic cop” with salespeople and vendors. This employee, in general, will oversee everything not involved in production and may also handle some marketing duties.
- **Receptionist.** Sometimes called the “front-line” person, he or she handles phone calls, greets visitors, handles the mail, does the billing and performs many other tasks as required by the office manager.
- **Foreperson, supervisor, lead person.** This individual is the second-in-command in the shop and will oversee production in the absence of the owner, general manager or president. He or she usually will have an overall understanding of all aspects of the business and also will handle working with new employees, including setting up training and schedules.
- **Marketing manager.** If finances permit, a marketing manager may be on staff to handle all aspects related to promoting and selling the product. The top management person often handles this duty in a small business.
- **Purchasing manager.** Duties of this position may be filled by either or both the general manager/top management person and the office manager. The supervisor or lead person often also is involved.
- **Shipping and receiving person or manager.** This may not be a full-time position in a start-up business. Someone, however, needs to be assigned the task of packaging, ordering transportation for delivery, receiving incoming material and warehousing of finished goods and stock. Several people may be involved in this, including the office manager, foreperson or accounting clerk.
- **Professional staff.** Instrumental in each company, new or existing, are the firm’s professional staff resources. These include an accountant (CPA), a lawyer, a computer consultant and, possibly, a local doctor or access to a medical facility. Although perhaps not outlined as full-time staff positions in your organization, these

roles should be considered a part of the management team and discussed in the development of the business plan.

Organization Chart

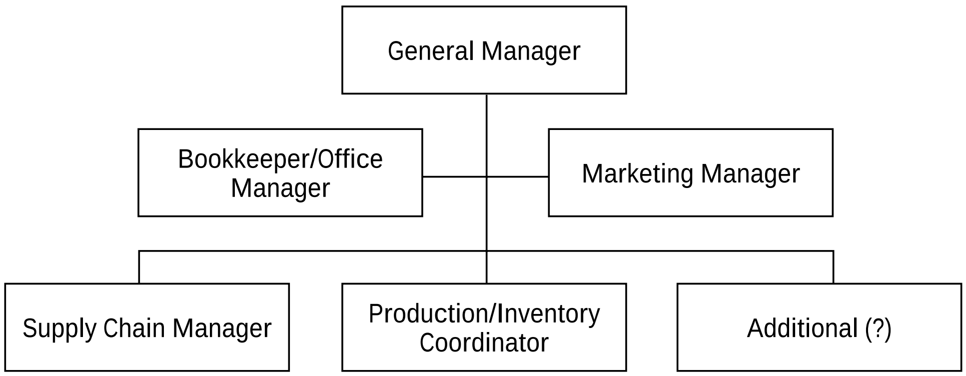


Management

Organization Characteristics

A look at the scenarios and general characteristics of wholesale and retail marketing organizations may further assist you in bringing your management needs into focus.

Wholesale Management



Generally speaking, sales of products to wholesalers will tend to require fewer people to run the business. Following is a description of the management positions that will need to be filled.

Wholesale General Manager

Manages the entire operation in a style that keeps business running smoothly.

- Possesses excellent leadership skills and sense of fairness.
- Places concerns about costs and production ahead of popularity.
- Directs others in order to accomplish the mission of the business.
- Fills in as required in order to get the work done.
- Has firm grasp of the vision for the business.
- Maintains the driving force of the business.
- Always protects the interests of the owners.

Wholesale Bookkeeper/Office Manager

Handles all day-to-day duties involved with front office business operations.

- Possesses excellent bookkeeping/accounting skills.
- Supervises all bank issues.
- Does all billing.
- Handles receivables.
- Manages payroll.
- Pays all bills in a way that takes advantage of all discounts.
- Manages cash flow.
- Composes all correspondence.
- Sends and receives e-mails and faxes.
- Answers the phone on the second ring.

Wholesale Marketing Manager

Conducts and oversees all activities that foster and promote sales. The Marketing Manager creates opportunities for success.

- Designs and executes an effective marketing program.

- Maintains accurate files on activities and efforts.
- Builds database on industry trends.
- Identifies potential customers.
- Oversees advertising.
- Makes sales calls.
- May recruit other members to assist in calls on potential customers.
- Works with General Manager and Bookkeeper to set both purchase and sales prices.
- Responds to customer complaints in a way that is satisfactory to the customer.
- Coordinates with the Production Coordinator to ensure the correct product is processed and delivered to the customers.
- Handles all sales orders promptly.

Marketing activities often require more than one person. Frequently, the General Manager and Marketing Manager will coordinate to pick up all marketing needs.

Wholesale Supply Chain Manager

Works with all producers to ensure quality and availability of quantity.

- Oversees quality during growing process.
- Sorts hogs for purchase.
- Works with production coordinator on delivery of hogs.
- Handles all issues related to producers including drug and feed protocols.
- Arranges for inbound transportation.

Wholesale Production/Inventory Coordinator

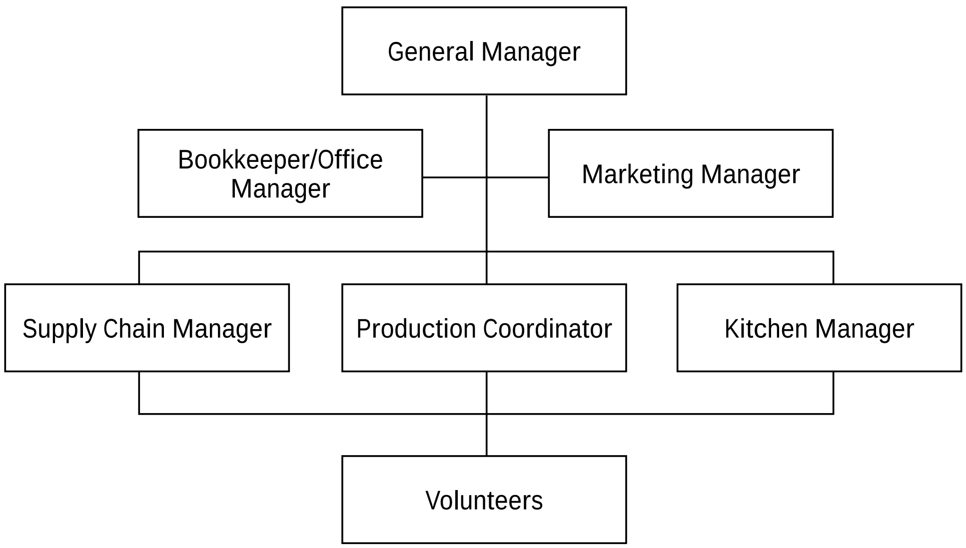
Works with the slaughter plant and the processing plant to ensure quantity and quality.

- Works closely with supply chain manager.
- Coordinates delivery of hogs to slaughter plant.
- Coordinates delivery of product to processing plant.
- Handles any issues involving either plant.
- Coordinates with marketing person(s) to ensure product processed per needs of customers.
- Manages inventory of finished product to ensure freshness.
- Coordinates delivery of product to wholesaler in quantity and sizes needed.
- Arranges for outbound transportation per delivery needs.

At a minimum, the wholesale business would require at least five or six people who are able to commit a minimum of 20 hours per week to the business. At 20 hours, the business is then only a part-time business. One of the issues when running a business is to be available whenever the customer calls. So all staff will need to be available during all work hours by phone, fax, e-mail or pager. This type of business requires conformity to the hours of operations maintained by the customer, usually 8 a.m. to 5 p.m., five to six days per week. More producers will be required to participate in the wholesale markets to meet higher demand for products.

At a minimum, the wholesale business would require at least five or six people who are able to commit a minimum of 20 hours per week to the business. At 20 hours, the business is then only a part-time business.

Retail Management



This analysis is based on the concept of running a food booth or catering trucks.

It is easy to understand that going from raw product to finished retail involves several more steps than selling primal cuts on a wholesale basis. The retail process adds more value; value is earned by finishing the product to meet the exact tastes of the individual consumer. The trick is to earn value in a profitable way. Value added attempts could result in more work and less profit if not managed very carefully.

For the most part, the organizational charts look much like the earlier scenario. The major difference when going retail is the need for greater refinement of the product and greater coordination between the various components of the organization. For those reasons, you will notice a few more lines running between a few more boxes on the organizational charts. Wholesale trade provides the luxury of slightly wider product tolerances regarding quality, appearance and maybe even freshness. When you put your product directly in the consumer's hands, everything must be exactly right. Retail presents more opportunities for greater profits and greater losses.

Retail General Manager

Manages the entire operation in a style that keeps business running smoothly.

- Possesses excellent leadership skills and sense of fairness.
- Places concerns about costs and production ahead of popularity.
- Directs others in order to accomplish the mission of the business.
- Fills in as required in order to get the work done.
- Has firm grasp of the vision for the business.
- Maintains the driving force of the business.
- Always protects the interests of the owners.

Retail Bookkeeper/Office Manager

Handles all day-to-day duties involved with front office business operations.

- Possesses excellent bookkeeping/accounting skills.
- Supervises all bank issues.
- Does all billing.

- Handles receivables.
- Manages payroll.
- Pays all bills in a way that takes advantage of all discounts.
- Manages cash flow.
- Composes all correspondence.
- Sends and receives e-mails and faxes.
- Answers the phone on the second ring.

Retail Production Coordinator

Handles livestock and volunteer related activities.

- Works closely with supply chain manager.
- Arranges for delivery, slaughter and processing of hogs.
- Handles any issues involving either plant.
- Manages inventory of finished product to ensure freshness.
- Arranges for volunteer staffing at events or fairs.
- Arranges for either volunteer or hired drivers for factory catering program.

Retail Kitchen Manager

Oversees all food preparation duties.

- Coordinates with Retail Production Coordinator to arrange for volunteer help to prepare all food.
- Monitors all food preparation to ensure quality and food safety.
- Orders all supplies needed for preparation and serving of food.

Retail Volunteers

Food servers, kitchen helpers, cooks, clean-up staff, delivery and truck drivers, booth set-up staff, sales staff at the booth or in the catering truck.

- Be available when needed to do whatever is needed to ensure a quality product is sold and customers are satisfied.

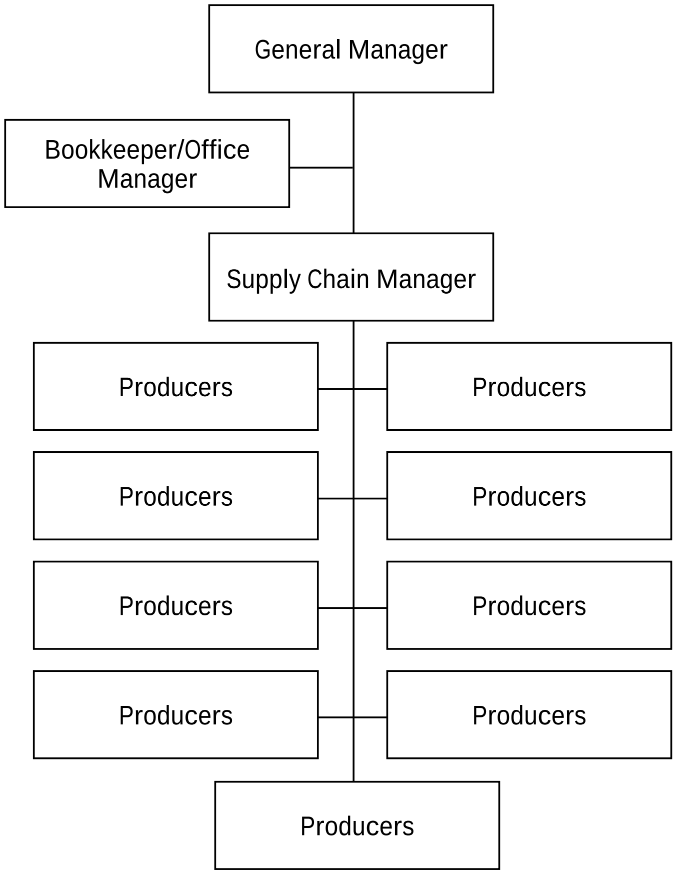
The retail business where prepared product is sold directly to customers will demand the involvement of many people. If large groups of people are not willing to help, the few who do will quickly burn out. It requires a willingness to work at nights and on weekends.

The food event business tends to be largely seasonal between May and September each year, with most weekends committed to some event. For a factory catering business, the truck will need to be staffed for three-shift factory operations.

Positive Side of Retailing	Negative Side of Retailing
greater chance for immediate returns	fewer hogs needed to meet demand
capture value of free labor	possible higher initial investment costs
get full benefit of sweat equity	more time required for management

Commodity Marketing

This business is the one where the group will seek better market access and prices due to marketing a larger number of quality hogs on a steady basis.



Commodity General Manager/Marketing Coordinator

This person needs to be a leader with the aptitude to gainfully direct others in their accomplishment of the mission of the business. It is a key position.

- Establishes marketing relationships with major packers and buyers.
- Handles overall management of the business.
- Fills in any position as required to get the work done.
- Has the vision for the business and is the driving force in the business.
- Maintains the best interests of the owners at all times.

Commodity Supply Chain Manager

This person works with all producers to coordinate their efforts. It is a key position.

- Works to ensure quality in all hogs sent to slaughter.
- Is responsible for identity preservation from pen to plant.
- Chooses hogs for purchase and coordinates delivery of hogs.
- Arranges for transportation.
- Deals with all issues related to producers including drug and feed protocols.
- Serves as inspector, enforcer and trainer.

  As inspector - makes periodic visits to all producers to ensure quality practices and procedures are followed.

As enforcer - requires producers to make necessary changes in practices to ensure available supply of quality hogs.

As trainer - teaches producers any new requirements of the market or producer group.

Commodity Bookkeeper/Office Manager

Handles all day-to-day duties involved with front office business operations.

- Possesses excellent bookkeeping/accounting skills.
- Disperses payments to producers in a timely manner.
- Supervises all bank issues.
- Does all billing.
- Handles receivables.
- Manages payroll.
- Pays bills in a way that takes advantage of all discounts.
- Manages cash flow.
- Composes all correspondence.
- Takes care of any necessary permits.
- Sends and receives e-mails and faxes.
- Answers the phone on the second ring.

The commodity business has the most potential to serve a large group of producers for a number of reasons. It is easier to set up and get started, and more members can participate with no requirement for extra outside work. Less financing will be required for marketing materials or fixed assets. Everyone involved is already familiar with this type of business; and business could result in a faster payback to participating producers.

Key Decisions

The pork team will find a common thread running through each of these scenarios:

One common question is the definition of quality.

- What does quality mean to this group?
- How will you define it so other producers understand it?
- How will you measure quality?
- How will explain quality to your customers? Your definition of quality will need to include aspects of how the hogs are raised, traits of the hogs in terms of fat content, etc.

Another key factor is the amount of investment you are willing to make. Initial investment will absolutely affect:

- the size of the business
- the near-term market potential
- the amount of sweat equity required from each producer
- the potential return on investments

The last factor is: Who will step up to be leaders in this project and fill the key roles as outlined?

Notes

Management

Who Needs to be at the Table?

As you establish management for your business, one or more involved in creating the business should have a working knowledge of the business planning process. This knowledge and understanding can be obtained through a business plan training course. A number of training courses are available across the state. One such course is FastTrac for Manufacturing, which is taught through The Center for Industrial Research and Service (CIRAS) and the Small Business Development Center (SBDC), both of Iowa State University.

By the time you have reached this phase, you will have some parts of the Business Plan completed, with others to follow soon.

A "management team" needs to be pulled together, with serious thought given to the key positions that need to be filled and who should fill them.

The path of least resistance should be avoided – that is, placing close friends and relatives in key positions simply because of who they are. There are two criteria to justify placing someone in a position on your management team. One, the person has the training and skills to do the job; and two, the person has the track record to prove his/her talents.

Often, a management team evolves over time. Members of your team may wear several hats until the company grows and the company can afford the additional team members.

Team Members

Chief Executive Officer (CEO) or President

This person will be the driving force behind the company; he or she will make things happen, put together the resources to support the company and take the product to the market place.

Chief Operating Officer (COO), Vice President of Operations or General Manager

Whether called an organizer, an inside manager or an operations person, this person is the one who will make sure company operations flow smoothly and economically. He or she is responsible for making certain that necessary work is done properly and on time. An understanding of details of the business and an enjoyment of handling details are necessary.

Vice President of Marketing or Marketing Manager

Few businesses can be successful without marketing their products to the customer. The individual in this slot must have both marketing and industry experience.

Chief Financial Officer (CFO) or Controller

You may wish to establish two positions or combine both roles into one. The responsibility of one role is to seek money; that is, to look for investors and deal with banks, lenders, etc. (This function also could be assigned to another team member, such as the CEO or the General Manager.) The responsibility in the Controller role is to manage money and watch over the assets of the company. It is not uncommon to have the same individual seek money and manage money.

Vice President of Production or Production Manager

Good production managers with specific industry knowledge and experience are sometimes difficult to find. In the beginning, you may subcontract some production.

Management

Hiring Right and Retaining Good Employees

Hiring is something many people need to do and yet few seem to do effectively. A CEO of a Fortune 500 company confessed recently that his biggest downfall in the past couple of years had been "making some bad hiring decisions." Two executives he had selected had been extremely disruptive to the organization and had to be let go. He seemed to have little insight into why he had selected the wrong people. He feared repeating the mistake.

Many hiring supervisors share this fear. The process they follow for hiring gives them little confidence that the right person will be selected. Too often some comments and questions are exchanged, an application may be filled out but not checked out and the hiring supervisor relies on "gut" instinct.

The importance of hiring right is illustrated by your company's turnover. Average corporate turnover is more than 15 percent. According to a Harvard University study, 80 percent of turnover is due to hiring mistakes.

The importance of hiring right is illustrated by your company's turnover. Average corporate turnover is more than 15 percent.

Instead of rolling the dice, there are proven steps that will help you hire the right person, lower your turnover and improve your productivity. Sound like a dream? It can be a reality for you if you follow a rather simple process.

1. **Determine your needs.** As the old expression says, "If you don't know where you are going, any road will take you there." The first step in the hiring process is to determine your needs. Write out the qualifications (duties/responsibilities, skills/ expertise needed, experience and education/training required or desired) for the position you are trying to fill. Put the needs into priority so you will have a clear picture of the person you seek.
2. **Write a job description.** If you don't already have a job description for that position, develop one that is accurate. Good job descriptions can be completed in one page and serve as an important guide not only for hiring but also for performance appraisals.
3. **Advertise.** Using the qualifications from your updated job description for the position you wish to fill, consider various ways to advertise your open position. Besides the usual methods of placing ads in newspapers and magazines, talk to your good employees and tell them of your needs. Also consider "word of mouth" advertising with people with whom you come in contact professionally and socially. Think about posting the position on the Internet.
4. **Create an application form.** Have an application form ready to be filled out by interested applicants. This form should be sensitive to the questions to ask – and not to ask. If in doubt, have your attorney review it.
5. **Screen.** Screen applicants based on the specific qualifications you listed. This phase of the hiring process becomes easier if you have been honest and specific in listing your needs.
6. **Conduct an initial interview.** Have an initial interview with those applicants who appear to meet your needs. This does not need to be a face-to-face interview and can often be successfully accomplished over the phone, holding down your hiring expenses. The key here is good questions. Some are offered later in this article.
7. **Conduct a face-to-face interview.** A face-to-face interview with those candidates who looked good on paper and responded well to your questions over the phone is the next step. It is a good idea to have more than one person doing the interviewing so that what one person sees (good or bad) can be discussed if not confirmed by someone else on the hiring team. Again, good questions plus the ability to listen are

the keys. (See “Basic Interviewing Questions.”) Beware of the common mistake of doing too much of the talking during the interview. Studies have shown that expecting applicants to be able to discuss their previous experiences and accomplishments more than triples your chances of hiring the right person. Ask them to “tell me about a time when you . . . .” Don’t just talk in generalities during the interview; strive for open-ended questions. Be sure to avoid illegal questions about age, marital status, pregnancy, day care arrangements, disabilities, religion, race and national origin.

A sample candidate rating form is included here. You can prepare a similar form that lists your needs/qualifications. After you determine those key job qualifications, you might want to weight each in terms of its importance. Ask all who attend interviews to complete a form about each candidate.

8. **Consider innovative approaches.** Give candidates an assignment before the interview. For example, ask them to review your product or Web page and give you their comments. If the position for which you are hiring is especially key to your organization, make an effort to see the person in action. For example, ask a shop foreman candidate to walk through your plant and comment on things he/she sees. Always give a 5-minute warning before closing an interview. People often reveal something important about themselves at the last minute.
9. **Check references.** Thoroughly check references of final candidates before you make any job offers. Often this is done as a way to screen applicants, but this step is best utilized after the interview since it is a good way to verify information discussed in the interview. It is a good idea to talk to others who know the candidate – in addition to the references listed – before making any offers. If your reference checks are a dead end, that may be a negative red flag. Many companies have adopted a policy of refusing to confirm any information about a previous employee other than dates of employment. However, the burden of supplying reachable and responsive references belongs with the candidate! An interview may only test the candidate’s ability to interview well. A reference check may be the single most important step of the selection process.
10. **Make an offer.** If the reference checks confirm your interest to hire someone, make an offer to that candidate. Any offer should be subject to accurate and honest information filled out on the application form. If you are not sure, a follow-up interview may be needed.
11. **Inform other candidates.** Once the applicant has accepted the job offer and completed any written forms required, inform the other candidates (via letter or phone) that the position for which they applied at your company has been filled. Sincerely thank the other candidates for their interest in working for your company, and perhaps even consider a close runner-up for another position within your company.
12. **Review.** Review with your hiring team what went right and wrong so that you can continually improve the hiring process for the next time.

In summary, the more you do at the beginning of the hiring process, the fewer problems you will encounter during the process and after the person is hired. It is much easier and less expensive to hire right the first time than to have to keep doing it over and over for the same position or to have to deal with people who are not the right fit for the job. Nothing you do will be more important than getting the right people into the right jobs.

A Few Pointers

The following pointers may seem obvious. They are overall good business practices that can impact your ability to hire the right people. But, as we look at the poor hiring situations at plants and businesses around us, we realize that not everyone – even those with the best intentions – follows the sage advice perfectly. A quick review may help.

- **Consider new strategies.** As a hiring manager, you know that finding qualified candidates in today's environment is tougher than ever. You can't rely simply on historical practices, because candidates can afford to be choosier, and the best candidates almost always have options. Consider adopting some new strategies that will help you hire better over the long run.
- **Treat your employees well.** A good work environment will create positive messages about your company in the community. You will be a place where people want to work.
- **Promote your company name.** If no one has ever heard of your company, it will make it far more difficult for you to attract good candidates.
- **Focus on employee retention.** Lowering turnover will reduce your need to hire from outside and lower your costs considerably. In addition, give your own employees (internal candidates) the same courtesies and opportunities as you do external applicants! Consider promoting someone who already knows "the system" and has proven to be an excellent employee.
- **Be on constant look-out for good people.** Don't just rely on newspaper advertising when you have an opening. Encourage your employees to recommend people to you. Talk positively about your company wherever you go and ask your employees to do the same.
- **Move quickly.** Don't let another employer ace you out because you moved too slowly. The hiring timeline of the past no longer works.
- **Convey your enthusiasm!** Always speak positively about your company. Sell the candidate during the interview on yourself and your company.

Basic Interviewing Questions

1. We have read your resume and looked over your application. Please briefly summarize your background as it relates to this position. In other words, how has your training and experience prepared you for this job? What skills have you acquired in your past positions that will be an asset in this job? (Good "ice breaker" and good way to see if the candidate can focus on being brief with specific information. Look for the proven skills needed.)
2. What aspects of your last job did you like the best and the least? Why? (Look for positive and negative "red flags.")
3. Considering the various people you have worked for, please describe the management styles of your favorite and least favorite boss. (Again, look for "red flags" that could prove to be a good or bad fit in your organization.)
4. What if . . . scenarios/situations. Provide candidates with situations in which they have to resolve a "problem." (Look for specific traits, skills and abilities needed, e.g., integrity, the ability to work with other people, temperament and problem solving.)
5. What appeals to you the most and the least about this position? Why? (Any red flags?)
6. When we contact your references, what do you think they will they tell us are your greatest strengths and weaknesses? (How do the candidate's strengths and weaknesses fit with your needs as the employer?)

Notes

7. What are you specifically looking for in this position and organization? (Again, how do the answers fit with the needs of your company?)
8. What questions do you have for us? (Make sure you allow enough time for this even if other questions have to be omitted! You can often learn more about candidates from the questions they ask than from the answers they give to your questions.)
9. Based on this interview and what you have learned today, what is your level of interest in this position now? Why? (Look for a definite high level of interest.)

Whatever open-ended questions you decide to use, make sure you ask all the candidates the same questions. Doing so will help maintain consistency and will make ranking the candidates easier after the interviews. And do not forget to inform candidates of the next step(s) in the selection process before they leave.

Example

Candidate Rating Form

Candidate's Name: ______________________________

Open Position: ______________________________

Interview Date: ______________________________

- Communication Skills *(ability to listen plus express self verbally and in writing)*
- Decision-making Skills *(ability to make choices considering various impacts)*
- Problem-solving Skills *(ability to identify key issues and bring resolution)*
- Financial Skills *(ability to make cost-efficient decisions)*
- Leadership Skills *(ability to motivate and show initiative)*
- Interpersonal Skills *(ability to interact effectively with others)*
- Flexibility *(ability to adapt to changes and to see the "big picture")*
- Job Know-how & Demeanor *(ability to perform duties in a professional manner)*

☐ **Recommend Hiring**
Comments: ______________________________

☐ **Do Not Recommend Hiring**
Comments: ______________________________

Interviewer's Name: ______________________________

Retaining Employees

You can have a major impact on employee retention. Begin by:

1. Recognizing turnover as a problem that has solutions. Employees are now expected to change jobs an average of seven times during their lifetimes, and, according to Harvard University, 80 percent of turnover is due to hiring mistakes.
2. Acknowledging that people are your most important asset. Are employees in your organization viewed as assets to be maximized or as costs to be minimized? Does management treat workers as disposable or easily replaced units or capital that has gained investment value?
3. Accepting that job security and open communication will decrease employee turnover. If employees feel respect and a commitment from management, they will be more likely to return the loyalty. Show employees that you genuinely care about them. Employees often say the least satisfactory elements of their jobs include a perceived lack of management ethics, recognition and communications (Towers Perrin, Irvine, CA). Companies willing to increase communication have seen increased employee commitment.

Credit

Bob Tvrdik, a consultant on business management practices, wrote this article. Tvrdik has extensive experience working with industry on a variety of human resources issues, particularly hiring practices. He also worked for many years as an industrial specialist with the Center for Industrial Research and Service (CIRAS) at Iowa State University. Tvrdik is located at 1714 N. 129 Street, Omaha, NE 68154; (402) 496-9512; btvrdik@tconl.com.

Management

Incentives for Key Employees

Key employees are often asked by newly formed companies to work for less salary than they can command in the marketplace. They do so in order to participate in the upside potential of the company. The form of that participation may vary depending on the circumstances of the employee and the company, and it can include incentive stock options, nonqualified stock options, phantom stock and grants of restricted stock.

Incentive Stock Options

Incentive Stock Options are options to purchase the stock of the employer. Incentive options are the most common form of equity sharing. They have the advantage of tax simplicity. The key employee pays no tax as a result of receiving the option until he or she exercises it and sells the stock acquired. The price to be paid for this simplicity comes in two forms: first, the option must have an exercise price not less than the fair market value of the stock at the time of the grant. The option is thus "out of the money" when it is granted. Second, the appreciation in the underlying stock that occurs between the time that the option is granted and when it is exercised is eventually taxed at ordinary income tax rates.

Nonqualified Stock Options

Nonqualified Stock Option can avoid the problems inherent in incentive stock options, but at the cost of greater tax complexity. The holder of a nonqualified stock option incurs taxable income when he or she exercises the option. If the exercise is followed quickly by a sale of the stock, the problem is minimized. If the option must be exercised (lest it expire) before there is a market for the stock, the option holder faces a cash squeeze. For that reason, executives frequently seek nonqualified stock options with a long term. Companies, however, typically want to avoid having too many options outstanding in order to avoid cluttering up their capital structures.

Phantom Stock

Phantom Stock can be offered where the founders do not want to dilute their equity ownership, but want to provide key employees with incentives tied to bottom-line performance. Phantom stock does not involve the issuance of actual stock, but is rather a system of paying bonuses based upon increases in the company's value. This value can be established in the phantom stock plan at the book value of the company, some multiple of earnings or a combination of the two.

Grants of Restricted Stock

Grants of Restricted Stock can be particularly effective if there is a public market for the company's shares. Restricted stock is a term of art that includes stock acquired from a company in a private transaction rather than a public offering. The SEC has reduced the period of time that a holder of restricted stock must hold the stock before being able to resell it without potential liability under the Securities Act of 1933 for persons who are deemed not to be part of the "control" group of the company.

Grants of restricted stock have the same potential tax problem that nonqualified options have: a tax liability may arise before the key executive can sell any of the shares. There are tax planning measures available to address this problem in some circumstances. They may involve subjecting the stock to restrictions on transfer and a risk of forfeiture so as to defer the deemed receipt of income, or having the company pay a cash bonus to the employee to help pay the tax bill. The appropriateness of these techniques will vary depending on the circumstances of the employee and the company.

Management

Should I Join a New Processing Cooperative?

A renewed interest in cooperative agri-businesses is sweeping across the Northern Plains. These new cooperatives are structured differently than traditional farm supply and elevator cooperatives. They are focused on processing and marketing processed products rather than supplying production inputs or marketing raw agricultural commodities. They require producer members to supply raw commodities for processing through marketing contracts and tie the amount of commodity supplied to the purchase of equity stock in the cooperative. The new cooperatives are selling enough equity stock shares and related delivery rights to meet the cooperatives' financial needs and ensure peak use of processing facilities.

A combination of factors makes the decision about becoming a member in a new venture cooperative unique and complex. This article is designed to identify the key aspects of that decision by asking five questions.

1. What are the potential returns from membership in a cooperative?
2. To what risks is the cooperative business exposed?
3. How will cooperative membership influence the farm/ranch operation?
4. How will a lender view involvement in the cooperative?
5. How will cooperative membership impact personal and business goals?

Questions 1 and 2 focus on the new venture cooperative and the industry it will be involved in. These questions are asked to determine if the expected returns from cooperative membership are great enough to justify the risks surrounding the cooperative's operations and your equity stock investment. These questions are often difficult for farm/ranch managers to answer because they go beyond the more familiar market factors that affect raw agricultural commodities. Questions 3 and 4 are intended to identify the short-term and long-term impacts the cooperative's marketing contract and equity stock investment have on your farm/ranch operation and finances. Question 5 deals with your unique personal and business goals and how those goals may influence a decision about cooperative membership.

Cooperatives can return financial benefits to members in the form of favorable prices, net returns from operations (both cash and retained) and appreciation in equity stock.

What are the Potential Returns from Membership in a Cooperative?

Accurately estimating the financial returns of cooperative membership is not as easy as it may seem, because returns appear in several forms and are received at different times. Cooperatives can return financial benefits to members in the form of favorable prices, net returns from operations (both cash and retained) and appreciation in equity stock. Most new venture cooperatives choose to offer competitive, rather than favorable, prices to members and pass on benefits in the form of operating net returns and equity stock appreciation. Therefore, we will focus on these two forms of benefit.

Cooperatives distribute net returns to members based on patronage, or use. A portion of the net returns are distributed in cash, while the remainder is retained by the cooperative to be used in continuing business operations. This retained portion is returned to the member, but at some time in the future. Also, because there is a limited supply, equity stock typically appreciates in value if the cooperative is successful. However, equity stock appreciation is not realized until it is sold at a future date.

The time between the purchase of equity stock and when all financial benefits are received in the future is typically overlooked when analyzing potential returns. This oversight can have considerable impact on a cooperative investment evaluation and final membership decision.

A process called “net present value” is used to compare the outflow of money today with the inflow of money in the future. The basic concept is that income received today is worth more than income received in the future. This is because the income received today could be invested now, earn interest and be worth more in the future. To compare the flow of money that occurs at different times on an equal basis, you must adjust the future cash flows downward to correct for the fact they are not available for use today. A brief example should demonstrate this important concept.

■ Example

A new venture processing cooperative is requesting a $200 common stock, or membership, fee plus a minimum purchase of 500 shares of preferred stock at $20 per share. This results in a minimum total investment of $10,200. Each share of preferred stock requires the member to deliver one unit of commodity to the cooperative for processing. In this example, the member plans to sell the equity stock in 20 years for an estimated value of $32,500. A 30 percent marginal income tax rate was also used.

Table 1 shows the annual after-tax net cash flow without considering the influence of time on the inflow and outflow of money. The false impression is that cooperative membership will result in a net benefit of $34,414 (Column E, Table 1) after 20 years. However, this is not the number that should be used to make a membership decision.

The annual after-tax net cash flow including the influence of time is shown in Table 2. This example uses an 8 percent discount factor, which will be discussed in more detail shortly. The correct analysis shows a positive $1,214.67 net present value. This means that the money invested in the cooperative will generate at least an 8 percent after-tax return.

If the net present value had been negative, the cooperative would provide something less than an 8 percent after-tax return, and your money may generate a higher return within your current farm/ranch operation or in other ways. A negative net present value does not mean that you should not become a member in the cooperative, only that the cooperative will not generate the selected rate of return. Your personal and business goals, as well as the potential impacts on the farm/ranch, should also be considered.

As you can see, the impact of time on the outflow and inflow of money can be dramatic. It is critical that the influence of time be included in your analysis, and that a net present value process be used.

The Sources of Information

The cooperative’s business plan is the source of information we will use to evaluate both its risks and returns. This manual offers information and options in pulling together your business plan.

Information in the plan is summarized and published in a prospectus, or offering circular, which is provided to potential members during equity drive meetings. The prospectus is usually the only document available to make a membership decision, unless more information is obtained from the interim board of directors or steering committee.

Net After-Tax Cash Flow for a Cooperative Investment, without Time Value

Year	Total Patronage Refund (A)	Cash Patronage Refund (B)	Estimated Tax (30 %) (C)	Redeemed Retained Refund (D)	Net Cash Flow (E)
Present					$-10,200.00
1	$0.00				$0.00
2	$0.00				$0.00
3	$500.00	$100.00	$-150.00		$-50.00
4	$1,000.00	$400.00	$-300.00		$100.00
5	$1,625.00	$975.00	$-487.50		$487.50
6	$1,625.00	$975.00	$-487.50		$487.50
7	$1,625.00	$975.00	$-487.50		$487.50
8	$1,625.00	$975.00	$-487.50		$487.50
9	$1,625.00	$975.00	$-487.50		$487.50
10	$1,625.00	$975.00	$-487.50		$487.50
11	$1,625.00	$975.00	$-487.50	$0.00	$487.50
12	$1,625.00	$975.00	$-487.50	$0.00	$487.50
13	$1,625.00	$975.00	$-487.50	$400.00	$887.50
14	$1,625.00	$975.00	$-487.50	$600.00	$1,087.50
15	$1,625.00	$975.00	$-487.50	$650.00	$1,137.50
16	$1,625.00	$975.00	$-487.50	$650.00	$1,137.50
17	$1,625.00	$975.00	$-487.50	$650.00	$1,137.50
18	$1,625.00	$975.00	$-487.50	$650.00	$1,137.50
19	$1,625.00	$975.00	$-487.50	$650.00	$1,137.50
20	$1,625.00	$975.00	$-487.50	$650.00	$1,137.50
	Stock Sale	$32,500.00	$-7,136.00*	$6,500.00	$31,864.00
				Net After-Tax Cash Flow	$34,414.00

*Capital Gains Taxed at 28%

After-Tax Net Present Value Calculation for New Venture Cooperative Investment

Year	Per-Unit Patronage Refund (A)	Total Patronage Refund (B)	Percent Cash Refund (C)	Cash Patronage Refund (D)	Estimated Tax (30 %) (E)	Redeemed Retained Refunds (F)	Net Cash Flow (G)	Discount Factor (8 %) (H)	Present Value (I)
Present	Initial Investment						$0.00	0.9259	$0.00
1	$0.00	$0.00					$0.00	0.8573	$0.00
2	$0.00	$0.00					$-50.00	0.7938	$-39.69
3	$1.00	$500.00	20	$100.00	$-150.00		$100.00	0.7350	$73.50
4	$2.00	$1,000.00	40	$400.00	$-300.00		$487.50	0.6806	$331.79
5	$3.25	$2,625.00	60	$975.00	$-487.50		$487.50	0.6302	$307.22
6	$3.25	$2,625.00	60	$975.00	$-487.50		$487.50	0.5835	$284.46
7	$3.25	$2,625.00	60	$975.00	$-487.50		$487.50	0.5403	$263.40
8	$3.25	$2,625.00	60	$975.00	$-487.50		$487.50	0.5002	$243.85
9	$3.25	$2,625.00	60	$975.00	$-487.50		$487.50	0.46.32	$225.81
10	$3.25	$2,625.00	60	$975.00	$-487.50	$0.00	$487.50	0.4289	$209.09
11	$3.25	$2,625.00	60	$975.00	$-487.50	$0.00	$487.50	0.3971	$193.59
12	$3.25	$2,625.00	60	$975.00	$-487.50	$400.00	$887.50	0.3677	$326.33
13	$3.25	$2,625.00	60	$975.00	$-487.50	$600.00	$1,087.50	0.3405	$370.29
14	$3.25	$2,625.00	60	$975.00	$-487.50	$650.00	$1,137.50	0.3152	$358.54
15	$3.25	$2,625.00	60	$975.00	$-487.50	$650.50	$1,137.50	0.2919	$332.04
16	$3.25	$2,625.00	60	$975.00	$-487.50	$650.00	$1,137.50	0.2703	$307.47
17	$3.25	$2,625.00	60	$975.00	$-487.50	$650.00	$1,137.50	0.2502	$284.60
18	$3.25	$2,625.00	60	$975.00	$-487.50	$650.00	$1,137.50	0.2317	$263.56
19	$3.25	$2,625.00	60	$975.00	$-487.50	$650.00	$1,137.50	0.2145	$243.99
20	$3.25	$2,625.00	60	$975.00	$-487.50	$6,500.00	$31,864	0.2145	$6,834.83
20		Stock Sale	$32,500.00	$-7,136.00*					
								Net Present Value	$1,214.67

*Capital Gains Taxed at 28 %

The cooperative's prospectus will provide most of the information needed for a net present value calculation. It will include the amount of the initial membership fee, the value of each share of stock and any minimum stock requirements. An economic feasibility study should include projected per-unit net return for several years of operation into the future. And, the cooperative's by-laws should explain how the net returns will be distributed and how retained patronage earnings will be refunded.

The decision about the division of net returns between cash refunds and retained refunds is left to the cooperative's board of directors. The percentage of cash versus retained refunds normally changes from year to year depending on the cooperative's net returns and strategic business plan. This makes the net present value analysis more difficult because estimates of this division need to be made for each year of membership.

Typically, cooperatives return net income to members based on patronage. These cooperatives must distribute at least 20 percent of their net income in cash, unless the cooperative is paying the income tax. Many new venture processing cooperatives attempt to distribute larger cash patronage refunds because of the initial membership investment. Therefore, a 20 percent cash patronage refund should be considered a minimum, and a larger percentage is reasonable to expect.

Typically, cooperatives return net income to members based on patronage. These cooperatives must distribute at least 20 percent of their net income in cash, unless the cooperative is paying the income tax.

Other cooperatives distribute net income on a per-unit basis. Net income is distributed periodically in cash with a portion, called a per-unit capital retain, being withheld for use by the cooperative. The amount of cash payments and capital retains will change from one year to the next depending on the cooperative's operations and long-term business goals.

Another important fact to include is that the cooperative's allocated net returns are considered taxable income to the member. This includes both the cash and retained portions. This element can have significant impacts on short-term cash flow, as well as the final net present value. In some cases, cooperatives have not returned a large enough cash refund to cover all of the member's current income tax liability.

Selecting a Discount Factor

Selecting an appropriate discount factor is important because it has considerable impact on the results of the analysis. For instance, if the discount rate in our example is increased from 8 to 9 percent, the net present value would decrease from $1,214.67 to -$429.93.

There are two common approaches to selecting an appropriate discount rate. One approach is to choose a discount rate that is equal to the highest interest rate paid on debt capital. This approach emphasizes the fact that there are alternative uses of money. It assumes that the cooperative membership investment funds would be used to pay farm/ranch debt if it were not used within the cooperative. Therefore, the cooperative should generate at least the same rate of return as the next best use of the funds.

An alternative approach is to choose a discount rate that reflects your desired rate of return on investment. This allows you to incorporate all of the risk factors surrounding the cooperative business into the analysis; the higher the risk, the larger the discount factor. This approach is more subjective but allows you to compare the cooperative membership investment to other investments with similar risks. This leads to the next question.

To What Risks Is the Cooperative Business Exposed?

Determining the risks surrounding a new venture cooperative is one of the most difficult things to do, because there are many sources of risk, and each is hard to measure. To make things easier, the sources of risk can be grouped into two broad categories: business risks and financial risks.

Business risks are those associated with conducting business operations, without considering the financial structure. The five sources of business risk are:

1. Production (including both construction and operation)
2. Market or price
3. Technological
4. Legal and social
5. Human

Financial risk is the magnification of business risks caused by debt financing. This includes the uncertainties surrounding the availability of borrowed capital, credit terms and changing interest rates.

The Cooperative's Business Risk

Each of the five sources of business risk should play a role in your analysis of the new venture cooperative.

Production risk refers to the unforeseen events that can change the projected construction, start-up and operating costs and efficiencies. These events can influence both product quantity and quality. A realistic and thorough economic feasibility analysis will provide information about projected construction and startup costs, typical operating costs and efficiencies, and operating margins. The projected operating margins should be based on realistic forecasts and be sufficient to cover unforeseen cost overruns and operating problems. Typically, the cost projections for the first several years of operation are larger than average to compensate for these risks.

Market or price risk refers to both sales volume and product price. The fundamental information needed to analyze price or market risk is included in the marketing plan. The marketing plan should discuss the size of the current market, the market growth factors, the major competitors, the cooperative's market advantage, how market share will be established and how co-products from processing will be marketed. Once again, it is not unusual to see lower than normal price projections for the first several years. This allows the cooperative to establish market share and customer loyalty, and compensate for unforeseen reactions by competitors.

Another aspect of market risk is the ability of the cooperative to adjust its product, or product line, to meet changing customer preferences. The ability to profitably adjust products is directly tied to the technology used, which leads to technological risk.

Technological risk is the potential for current efficiencies to be offset by improvements in future technology. The cooperative must consider the tradeoffs between adopting the most current technology to gain possible efficiencies with the increased cost of that technology and the risk that the new technology is not completely tested and proven.

Legal and social risks are those which refer to changes in local, state and federal laws and regulations governing the cooperative business and its industry. These include changes in tax law, environmental regulations, interstate commerce, import/export regulations or industry subsidies. The key is to look at how sensitive the cooperative's business plan, and resulting net return, is to changes in relevant laws and regulations. The cooperative's business plan should be flexible enough to adjust to changing legal and regulatory conditions.

The final source of business risk is human risk. Human risk is associated with the availability and quality of labor, management and board of directors. The first human risk is the selection of high quality personnel. The second human risk is the impact on the cooperative if one, or several, of the key people leave the business.

Human business risks are frequently underestimated. One of the most commonly cited reasons for a successful business is the abilities of the people on the management team. The management team of a cooperative, both hired managers and the elected board of directors, is especially critical. The cooperative management team must not only be concerned with the efficient operation of the business, but also with the sometimes conflicting needs of the members/patrons. Always remember, it's the people who make the plan work.

The Cooperative's Financial Risks

Financial risk is the second category of risks and is defined as the increase in business risk caused by debt financing. The lowest risk situation for the cooperative is to be completely equity financed and not borrow any money. However, this is difficult to accomplish, especially for large projects, and may put unwanted restrictions on the cooperative's business plan.

From a member's point of view, financial risk may not seem large, relative to the business risks discussed earlier. However, financial risk and the ability of the cooperative to adjust to business risks using borrowed capital can have a substantial impact on performance and ability to succeed.

It is important that the cooperative have a lender or lenders who have experience with the unique aspects of financing cooperatives. It is also important that the total financing package, both debt and equity, meet the needs of the cooperative and leave it flexible enough to adjust to changing business conditions. This usually means that the business plan needs to have solid member investment capital and sufficient operating funds or working capital.

It is important that the cooperative have a lender or lenders who have experience with the unique aspects of financing cooperatives.

How Will Cooperative Membership Influence the Farm/Ranch Operation?

The impacts of new venture cooperative membership on the farm/ranch operation can range from minor to far-reaching, depending on your current farm/ranch operation and the structure of the cooperative and its membership agreement. To capture all of the potential consequences, we evaluate the impacts on farm/ranch production, marketing and finance individually.

Production

In most cases, a new venture processing cooperative requires its members to deliver consistent, high quality commodities. High quality products allow the cooperative to capture and maintain market share. Because of this, the cooperative may develop recommended production practices to increase overall quality and quantity and to reduce quality variation among members.

It is important to determine if these production practices are voluntary or mandatory. You must gauge how easy it is to incorporate proposed changes into your current operation and estimate changes in the commodity's per-unit cost of production.

Changes in production practices could be as simple and low cost as changing animal vaccinations, or as complex and expensive as altering machinery complements or building and facility configurations.

The spin-off impact on the production and cost efficiencies of other enterprises on the farm/ranch is typically underestimated or even overlooked. A common example is an increase on the demands of the farm/ranch's labor and management. If changes in production practices increase the demands on labor and management at the expense of another enterprise, the net result may not be positive.

The timing of delivery and final point of delivery for the commodity can also have significant impacts on the cost of production. If the commodity must be stored from the time of production until delivery, the added costs of storage, handling, interest and the risk of reduced quality should be included. The cost of transporting the commodity from the point of production to the point of delivery should be adjusted if delivery is required outside your normal trade area.

Some farmers have found that the cooperative's recommended production practices have improved enterprise and whole-farm efficiencies.

Marketing

It is important that the terms and conditions of any marketing agreement are completely understood. In most cases, the responsibility for profitably marketing the commodity is turned over to the cooperative through its processing activities. This allows the farm/ranch to diversify its commodity marketing activities.

It is not unusual for the cooperative's business plan to provide partial payment for the commodity at the time of delivery, with the remainder received as cash and retained patronage at some time in the future. The timing and level of these payments can have a significant impact on the farm/ranch cash flow. It may be necessary to alter the normal marketing plan of other commodities or change short-term borrowing needs to adjust to the cooperative's payment schedule.

Another important issue is what happens if you are unable to deliver the specified quantity or quality of product listed in the marketing contract. Some cooperatives have established a member marketing pool to fill shortfalls. In this case, the cooperative buys the commodity from the pool, in your name, and reduces your payments by that amount, plus a handling fee. Other cooperatives require the delivery of the commodity, and you are responsible to purchase and deliver any shortfalls.

Finances

There are both long-term and short-term impacts on farm/ranch finances. The extent of these impacts will vary greatly from one farm/ranch operation to the next. The best way to capture all of the long-term financial impacts is to use whole farm/ranch budgeting. This process provides estimates of the long-term profitability of the operation and gives an indication of its financial progress and staying power.

Two long-term budgets should be prepared. The first reflects business as usual and includes normal farm/ranch operating practices, machinery replacement and building or facilities renovation. The second will add the new cooperative investment with all of the adjustments to production and marketing for each enterprise on the farm/ranch. These two estimates should be prepared assuming that changes are fully implemented. This means that the cooperative is in operation and is generating and distributing returns as projected. We are trying to assess what the farm/ranch business may look like in the future.

The main objective of this process is to estimate the net effect of cooperative membership on the long-term financial health of the farm/ranch. By comparing the results of the two budgets, we see the influence the cooperative has on net farm income, change in net worth and long-term cash flow. It is the combination of these three measures that provides an indication of long-term financial health. If the long-term benefits are positive, we need to make sure that the farm/ranch can meet all of its short-term cash flow needs.

It is not unusual for a new venture cooperative to need several years of start-up and operation before its net returns are positive. Because of this, members typically will not receive returns from the cooperative until several years after the initial investment has been made. It is critical that the farm/ranch operation be able to meet all of its financial obligations on time during this period. A short-term cash flow projection will show if this is possible.

Every farm/ranch operation has some level of short-term borrowing and cash flow limitations. Because of this, the cooperative membership investment must compete with other uses for limited short-term capital. If a conservatively prepared short-term cash flow is positive, the chance of major cash flow problems is small. However, if the cash flow is slightly positive or negative, decisions must be made between the alternative uses of money.

Preparing whole farm budgets and cash flows is not a small process and will take some time and effort. However, these statements will ensure that all direct and indirect impacts of changes in production, marketing and financing are included. Time spent now, with a sharp pencil, could prevent problems in the future.

■ How Will My Lender View the Cooperative Investment?

It is important to discuss the new venture cooperative investment with your lender. This should be done regardless of whether the investment is self-financed or debt-financed. The investment in a new venture cooperative typically results in a notable change in your financial condition and should be reviewed with your lender to maintain good working relations.

One of the most commonly cited personal benefits of cooperative membership is the ability to have a voice in the operation of the business.

Your lender will have many of the same questions we already have discussed. There are two additional questions the lender may have which are important to you and may influence a loan decision and credit terms. The first is, “How will possible losses from the cooperative be distributed?” and second, “How easy or difficult is it to transfer membership stock?”

The first question concerning distribution of losses is important because it helps define the maximum loss potential. In some cases, the method for distributing cooperative losses is defined in the by-laws. In other cases, this decision is the responsibility of the board of directors. In either situation, it is important to understand what may happen to your initial investment and any retained earnings if the cooperative sustains losses.

The second question concerning stock transfer is important because your lender is trying to determine the liquidity of the stock. If the cooperative stock is easily transferred from one producer to another, the lender views it as more liquid and lower risk. This is because the stock could be sold quickly and easily if it is necessary to limit losses.

Every lending institution or system treats a loan for cooperative membership investment differently. Some lenders have even developed special loan terms that meet the unique cash flow needs of a membership investment.

If you are requesting a loan, these four key issues need to be discussed:

1. The annual interest rate of the loan and whether it is fixed or variable.
2. The length of the loan.
3. The number and timing of payments.
4. The source(s) and amount of collateral.

The first three issues will determine the annual loan payment and influence the farm/ranch cash flow. The final issue, concerning collateral, will influence solvency and future borrowing capacity. Some lenders use only the cooperative stock as security for a loan. However, most lenders require that additional farm/ranch assets be pledged. The amount of needed collateral will depend on the current financial strength of the farm/ranch, your credit history and the risks surrounding the cooperative business.

How Will Cooperative Membership Impact My Personal and Business Goals?

Up to this point, we have focused primarily on the financial aspects of cooperative membership. However, there are several nonfinancial factors that may play a role in your final decision.

One of the most commonly cited personal benefits of cooperative membership is the ability to have a voice in the operation of the business.

Many local communities, regions and even states are actively involved in the development and promotion of new venture processing cooperatives. Their goal is to bring economic development and more jobs into their area. In some situations, the cooperative has already selected a specific site to locate facilities and headquarters. In other situations, the site has not yet been decided.

Many cooperative members list community economic benefits and increased job prospects as factors in their membership decision. However, it is also important to realize that the cooperative may not locate in your area and that not all of the community impacts are positive.

It is true that a new business creates more jobs, more people living within the community and increased retail business volume. However, some communities have found that increased business activity and larger populations strain the community infrastructure, such as water, sewage, fire fighting, police, medical services and schools. An expanded job market can also increase the competition for labor and put additional financial pressure on existing businesses.

Because of the long-term nature of agri-business development and growth, some farmers and ranchers will not enjoy the complete benefit of cooperative membership during their farming/ranching career. Yet, they are active participants in the process. The desires to improve communities and assist the next farming/ranching generation are factors that influence their membership decision.

Sources of Additional Information

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