

Comparing Cooperative Principles of the U.S. Department of Agriculture and the International Cooperative Alliance



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ABSTRACT

The cooperative principles of the U.S. Department of Agriculture (USDA) and those of the International Cooperative Alliance (ICA) trace their origins back to the Rochdale statement developed in 1860, but they have evolved in slightly different directions. This report makes selective comparisons

between two sets of contemporary cooperative principles in regard to how they distinguish that form of organization from other forms of business.

Keywords principles, organization, members, values, solidarity

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Bruce J. Reynolds
Economist

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PREFACE

This report was presented at the North Central Extension Research Activity -210 (NCERA-210) meeting on November 6, 2013 (<http://ncera.aae.wisc.edu/>). Cooperative principles have been revised at various times by different organizations since they were first articulated by the Rochdale weavers in 1860.

By the 1980s, many cooperative leaders and academic researchers believed that cooperative principles needed to be articulated in a way that established their distinctiveness from other forms of organization. As part of several nationwide panel discussions that focused on how to best position farmer cooperatives for the future, USDA defined three core cooperative principles in a 1987 statement. Its approach was to eliminate “principles” that were actually “best practices.” The USDA co-op statement is a concise definition of a distinctive form of business organization that is controlled by users or producers, rather than investors.

The International Cooperative Alliance (ICA) took a different approach to articulating the distinctiveness of cooperatives with its statement of principles in 1995. Leading up to the 1995 statement, a concern of ICA was that this distinctiveness was being lost as some cooperatives were identifying themselves as being comparable with investor-owned businesses in their respective industries. Another concern was that the public was viewing tax-reduction efficiency as the primary value of a cooperative. ICA’s approach was to draft a cooperative identity statement that reflected values that were either lacking in, or irrelevant, to organizations other than cooperatives.

This examination of the two sets of co-op principles will explain why they differ in particular attributes, while recognizing that both contribute to a better understanding of the unique nature of cooperatives.

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Introduction

The cooperative principles defined by the U.S. Department of Agriculture (USDA), as well as those of the International Cooperative Alliance (ICA), both trace their origins back to the Rochdale statement, developed in 1860. But the USDA and ICA definitions evolved in slightly different directions. Throughout their history, cooperatives have not departed from the Rochdale ideas about the importance of democratic control by members and that the primary purpose of a co-op is to serve the interests of members.

Yet, cooperative principles have been re-stated over time by different groups, with slight variations occurring in these definitions of the attributes of a cooperative.

USDA provided a statement of three cooperative principles in 1987. ICA issued a revised statement of seven cooperative principles in 1995. This report makes some selective comparisons between the two sets of contemporary cooperative principles in regard to how they distinguish a co-op from other types of business organization, particularly from business entities focused on maximizing return on investment.

While these two sets of principles do not contradict each other, they do have several differences. This comparison will examine why they are different by contrasting the justifications used by those who developed these alternative statements. It will also consider how successful they are in describing the uniqueness of cooperatives.

Using the term “principles”

The cooperative principles of USDA and those of the ICA purport to apply to all cooperatives and are not sector specific. Both sets of principles set out to

provide a distinct identity to the cooperative form of business. A major source of the difference between them resides in their respective use of the term “principle.” How the two sets of principles use the term is the first factor to consider. From that point, we examine the different philosophical orientations and beliefs they represent.

A principle can be defined as follows: “A principle is any such generalization ... which provides a basis for reasoning, or... a guide for conduct or procedure.” (Webster’s Dictionary, as reported by Schaars).

This definition is split between “a basis for reasoning” and “a guide.” The word “principles” is commonly used in these two different ways, such as:

- (a) Scientific explanations of phenomena, or the essential methods of a science;
- (b) Necessary and sufficient conditions for an entity to have distinct identity or be a type;
- (c) Behavioral guidance for morality or for civic virtues;
- (d) Behavioral guidance for efficiency and success.

The “reasoning” approach of (a) and (b) and the “guidance” purposes of (c) and (d) are combined, to some extent, in all statements of cooperative principles. Yet, USDA’s reasoning approach to principles focuses on definition, while the ICA takes more of a guidance approach, with a separate statement for defining a cooperative.

How cooperative members have understood the meaning of the term “principle” may have influenced the ways in which the statements of principles have been applied. British cooperative leader and author, Edgar Parnell, argues that in retrospect a strict adherence to principles has been detrimental to the growth and wider use of cooperatives

(Parnell 1995). He recommends applying rules that guide rather than principles that assert “indisputable truth.” Parnell understands the term “principle” in its methodological reasoning sense and believes that guidance is what matters for cooperatives. Hence, he understands the term “principles” in the sense of items (a) and (b), not (c) and (d) as described above.

The Rochdale statement of nine cooperative principles became an international standard. Parnell observes that the Rochdale pioneers regarded their statement as being rules, and it was not until the ICA adopted a slightly revised version in 1937 that they became enshrined as “principles.” Yet, there are references to the Rochdale Cooperative Principles well before 1937.

In the decades following the U.S. Civil War, the Grange and then the Alliance movements, followed by organizations such as the Farm Bureau, actively promoted farmer cooperatives. They adopted and made various adaptations to what they regarded as the Rochdale Principles (Nourse). Some of the principles were included in U.S. State incorporation statutes. While having some similarities, they were often stated with slight variations (Baarda 1979).

Drawing from Abrahamsen’s textbook, Dave Barton, in a later textbook, specifies the emergence of eight so-called traditional cooperative principles that prevailed in U.S. agriculture during the 20th century until the 1980s. Six of the eight principles are derived from Rochdale.

The Traditional 8 in concise form, are:

1. Voting is by members on a democratic (one-member-one-vote) basis;
2. Membership is open;
3. Equity is provided by patrons;
4. Ownership of voting stock is limited;
5. Net income is distributed to patrons as patronage refunds on a cost basis;
6. Dividend on equity capital is limited;
7. Business is done primarily with member-patrons;
8. Duty to educate.

By the 1980s, much of the “Traditional 8” were regarded as either “practices” or as archaic. Principle 4 was redundant if Principle 1 were applied. Principle 2, open membership, was viewed as

impractical, particularly for U.S. agricultural cooperatives when dealing with mounting surpluses. However, the ICA has retained the open principle, meaning that a cooperative should not discriminate in its membership on the basis of gender, race, or religion (MacPherson, 1995).

USDA principles

The need to update the principles was a topic of the mid-1980s meetings with leaders in the U.S. cooperative community, held to help prepare a report to Congress in 1987: “Positioning Farmer Cooperatives for the 21st Century.” Although the report was directed to farmer cooperatives, its statement of a new set of principles was developed to apply to all types of cooperatives.

The USDA statement of three principles of cooperatives (USDA 3) is as follows:

- **User-Owner Principle:** Those who own and finance the cooperative are those who use the cooperative.
- **User-Control Principle:** Those who control the cooperative are those who use the cooperative.
- **User-Benefits Principle:** The cooperative’s sole purpose is to provide and distribute benefits to its users on the basis of their use.

The USDA 3 provides a concise statement by eliminating what were viewed as practices, rather than principles. When best practices are identified to routinely follow, they may become principles, in the sense that they offer guidance. USDA wanted principles that provided a precise definition.

USDA’s “economic reasoning” approach sought universal validity through necessary and sufficient conditions for an organization to be a cooperative. In using the “reasoning” approach, the USDA 3 principles are more of a definition of cooperatives than they are a guide for their conduct. Hence, the USDA 3 follows the (a) and (b) examples.

The Traditional 8 are edited below to reflect the USDA 3 (crossouts denote practices deleted from USDA principles):

1. Voting is by members on a democratic (~~one-member-one-vote~~) basis;

2. ~~Membership is open;~~
3. Equity is provided by patrons;
4. ~~Ownership of voting stock is limited;~~
5. Net income is distributed to patrons as patronage refunds ~~on a cost basis~~ (*based on their use*);
6. ~~Dividend on equity capital is limited;~~
7. Business is done primarily with member-patrons;
8. ~~Duty to educate.~~

Principle 1 is “user-control,” with “one-member, one-vote” deleted. Principle 3 is “user-owner.” Principles 5 and 7 can be combined to form the “user-benefits” principle of the USDA 3.

The principles in USDA 3 are universal and timeless in the sense of not being influenced by periodic changes in socio-economic conditions or in cultural norms. By contrast, those who developed the ICA principles embrace social and historical experience as a source for defining the distinctive purposes of cooperatives. As a result, the ICA statement requires lengthier explanation. USDA 3 focuses on the essential difference—cooperatives are businesses established for users and do not serve the interests of non-user investors.

Indeed, the USDA 3 is often expressed as a definition of a cooperative rather than as a set of principles. “A cooperative is a user-owned, user-controlled business that distributes benefits on the basis of use” is a restatement of USDA 3 as a definition of a cooperative (Zeuli and Cropp). But even as a definition, it is questionable whether the USDA 3 excludes other types of organizations that may satisfy its criteria, but which are neither incorporated as, nor which self-identify as, cooperatives. Several types of private businesses have no non-user owners.

In other words, USDA 3 may not sufficiently differentiate cooperatives with the emergence of non-cooperative entities that are user-owned, user-controlled, and user-benefited.

Such businesses are found in professional services and in the booming technology industries and are analogous to worker cooperatives. Farmers have also actively organized limited liability companies (LLCs), with many of these having no non-user owners, and some do not regard their organizations as cooperatives. These “user” entities can be defined

as cooperatives if they satisfy USDA 3. But why increase the inclusiveness of a definition when the individuals who organize these entities do not self-identify as cooperatives?

Economics Interpretation

The reduced form approach of specifying the minimum principles is an immediate indication that USDA 3 was developed by looking through the lens of economics. USDA 3 is reduced to the essential elements of people working together for their mutual interests. While the ICA is willing to accept general best practices that have stood the test of time, USDA 3 draws a line between a practice and a principle (Dunn).

Another feature of economics is that the individual is the basic unit of analysis. Economists have traditionally asserted the postulate that the individual is the fundamental basis of a cooperative (Schaars). In an influential application of economic theory, Emelianoff conceptualized cooperatives as an aggregation of individuals (Emelianoff 1942). This interpretation was recently discussed in *Rural Cooperatives* magazine (Ling). The individualist postulate is reflected in discussions of USDA 3 by pointing out that a cooperative serves the interests of the “current” user and is not for perpetuating the organization or collective entity (Dunn).

Economists believe that assertions about common goals must, at a minimum, be validated by processes of aggregating individual choices, but not on a priori grounds. In fact, one of the major contributions of the individualist postulate of economics is to understand how group commitments and practices can lead to conditions that increase individual incentives to act alone or to form dissenting coalitions (Schelling, Olson, Buchanan, and Tullock).

A third aspect of economics that is reflected in USDA 3, but not in other statements of cooperative principles, is the assumption of *wertfrei* (value-free), also referred to as the positivist approach (Robbins, Friedman). Economists avoid asserting social values, yet this cautiousness when applied to principles may exclude attributes that contribute to further differentiating cooperatives from other forms of organization.

The intention of theorists such as Emelianoff,

among others, was to define the cooperative in a way to preserve distinctiveness from other forms of business in so far as that served the requirements for applying economic analysis and methodology. An economics approach, however, may not satisfy other requirements necessary for defining a unique cooperative identity.

ICA 7

Turning to the seven principles of the International Cooperative Alliance (ICA 7), the idea of individual self-interest is operative but social theory is also applied to defining and guiding cooperatives. The ICA had issued statements of cooperative principles in 1937 and 1966; by the early 1980s they were already considering a re-statement that finally came in 1995 (Hoyt). When revisiting the ICA principles of 1966, it was deemed critically important to combine principles within an identity statement.

ICA 7 set out to establish a unique identity for cooperatives. But applying the ICA identity statement as criteria is more complicated than the concise definition of USDA 3.

The importance of identity was in reaction to the earlier ICA principles and the drift of some cooperatives away from a focus on serving member activities – not as a reaction to USDA 3. To that end, it is worth listing the 1966 statement in abbreviated form:

1. Open, voluntary membership.
2. Democratic governance; one-member, one-vote in primary cooperatives.
3. Limited return on equity.
4. Surplus belongs to members.
5. Education of members and public in cooperative principles and practices.
6. Cooperation between cooperatives.

Many of ICA's members had regarded these as a rigid doctrine, as pointed out by Parnell, rather than living principles for direction and guidance. By setting the new principles within the context of an identity statement and a definition of unchanging cooperative values, they are pragmatic and not doctrinaire guidelines (MacPherson 1995). Some of the ICA 7 principles are clear lines to follow, such

as voluntary and open membership or democratic member control. But others leave room for interpretation.

The statement of identity is in three parts: a definition of a cooperative, a list of cooperative values, followed by the statement of seven principles.

Definition: A cooperative is an autonomous association of persons united voluntarily to meet their common economic, social, and cultural needs and aspirations through a jointly owned and democratically controlled enterprise.

Values: Cooperatives are based on the values of self-help, self-responsibility, democracy, equality, equity, and solidarity. In the tradition of their founders, cooperative members believe in the ethical values of honesty, openness, social responsibility, and caring for others.

Principles:

1. **Voluntary and Open Membership** – Cooperatives are voluntary organizations, open to all persons able to use their services and willing to accept the responsibilities of membership, without gender, social, racial, political, or religious discrimination.
2. **Democratic Member Control** – Cooperatives are democratic organizations *controlled by their members*, who actively participate in setting their policies and making decisions. Men and women serving as elected representatives are accountable to the membership. In primary cooperatives, members have equal voting rights (one member, one vote), and cooperatives at other levels are also organized in a democratic manner.
3. **Member Economic Participation** – *Members contribute equitably to, and democratically control, the capital of their cooperative.* At least part of that capital is usually the common property of the cooperative. Members usually receive limited compensation, if any, on capital subscribed as a condition of membership. Members allocate surpluses for any or all of the following purposes: developing their cooperative, possibly by setting up reserves, part of which at least would be indivisible; *benefitting members in proportion to their transactions* with the cooperative; and supporting other activities approved

by membership.

4. ***Autonomy and Independence*** – Cooperatives are autonomous, *self-help organizations controlled by their members*. If they enter into agreements with other organizations, including governments, or raise capital from external sources, they do so on terms that ensure democratic control by their members and maintain their co-operative autonomy.
5. ***Education, Training, and Information*** – Cooperatives provide education and training for their members, elected representatives, managers, and employees so they can contribute effectively to the development of their cooperatives. They inform the general public – particularly young people and opinion leaders – about the nature and benefits of cooperation.
6. ***Cooperation Among Cooperatives*** – Cooperatives serve their members most effectively and strengthen the cooperative movement by working together through local, national, regional, and international structures.
7. ***Concern for Community*** – Cooperatives work for the sustainable development of their communities through policies approved by their members.
(Source: <http://ica.coop/en/what-co-op/co-operative-identity-values-principles>)

The ICA definition of a cooperative, while expressed in different words from the USDA statement, is concise and readily understandable by the general public.

The ICA's statement of cooperative values establishes a universality and timelessness, as the USDA 3 principles do without asserting values. These values were articulated in a 1992 ICA publication by Sven Book. He drew these values, working in a team, out of studying the history and traditions of cooperatives throughout the world (Book).

The sections of the principles' statement (in italic type, above) denote where ICA 7 has commonalities with USDA 3. But while ICA 7 covers user control and benefits, it does not offer an explicit statement about user or member ownership, which is the first principle of USDA 3.

The ICA 7 principles are considered to be a living document that develops over time from shared

learning and experience (MacPherson, 2004). They provide a basis for determining what is, and what is not, a cooperative, but they are more expansive criteria than USDA 3. Yet, their purpose is not entirely to serve as criteria. By including a definition in the identity statement, the ICA principles function as a guide to realize and follow the values that cooperatives have established throughout their history.

There are at least three topics that are particularly relevant for comparing ICA 7 with USDA 3: (1) individual member ownership, (2) concern for community, and (3) member solidarity as an identifying trait of cooperatives.

The user-owner of the USDA 3 is not explicitly stated as a principle in and of itself in ICA 7. Furthermore, nothing is stated about common or collective property in USDA 3.

The 3rd principle of ICA 7 draws a distinction between the common property of the cooperative, while the idea of individual ownership is described in terms of subscriptions for membership and in the allocation of surpluses to members in proportion to use. Yet, as discussed by David Ellerman, in many cooperatives, individual capital accounts have an essential role in assigning ownership for a member's past contributions. This equity is returned to members after their participation in the cooperative ends (Ellerman).

Furthermore, the 3rd ICA principle states that a cooperative may want to set aside unallocated surpluses for an indivisible reserve. In the event a cooperative were sold to investors, the indivisible reserve would not be distributed to members but instead delivered to other cooperative associations. Indivisible reserves are essentially a constraint imposed at an earlier point in time by former members who have retired from participation in the cooperative. Such reserves would conflict with the explanation of USDA principles as recognizing the interests of current members without regard to those in the future (Dunn).

The point being made by this comparison is that these two sets of principles are in sharp contrast on the idea of ownership; it is not intended as a recommendation for changes in either statement.

A second point of contrast with USDA 3 is the ICA's seventh principle, "concern for community," which was entirely new in 1995, whereas the other

principles were revisions of previously existing statements. The late Ian Macpherson¹ explained the background to its adoption and provided several justifications (2012). He references a substantial history throughout the world where individuals organized cooperatives in their communities to improve their well-being in the context of often harsh economic conditions.

MacPherson makes an “origins” argument, that cooperatives arise out of communities and are not the creation of national governments or international institutions. The concerns of communities are the impetus to start cooperatives so this concern is essential to their existence.

In addition, MacPherson argues that all the cultural connections of community are what makes cooperatives work well and provides their distinctiveness. In his words: “It (the cooperative movement) was based on bonds of association that were different from those that characterized joint stock and partnership firms” (2012). Cooperatives are both businesses and providers of services based on member needs, in addition to market demand. Meeting unmet needs is a distinctive feature of cooperatives that MacPherson considers as demonstrating their concern for communities.

Some experts criticize this principle for extending the mission beyond the boundaries of cooperative membership and of offering nothing that is distinctive to cooperatives (Davis). Clearly, there are many organizations with concern for community that are not cooperatives. MacPherson’s discussion of the importance of community to cooperatives explains the motivations for the ICA to adopt the seventh principle. But it is different from the other principles in its external focus.

The final point to consider is “solidarity” as one of the ICA’s values of cooperatives and its potential for providing a key to creating distinctive identity. Similar to community, solidarity might be important to cooperatives but not be regarded as distinctive or essential. Yet, it may have distinctiveness if it is tied to the essential workings of members’ relationship with, and responsibility to, one another.

Some help in this regard may come from con-

sidering a statement by Cooperative Business New Zealand: “What We Mean by a Cooperative” (<http://nz.coop/understanding-co-ops/>). It accomplishes identity by emphasizing attributes of member solidarity and mutuality. Following Parnell, the New Zealand statement is not expressed as principles. It starts with a definition: “An enterprise, freely established, that is owned and controlled by a group of legal persons for the purpose of equitably providing themselves with mutual benefits arising from the activities of the enterprise, and not primarily from investment in it.”

Each phrase of the definition is then given explicit detailed statements. For example, “... the solidarity of the group needs to be maintained and developed.” In addition, a cooperative is “not based on one set of members gaining benefits from other members of the group.”

The word “solidarity” is widely used. But the idea of cooperative “members’ solidarity” involves reciprocations and consensus within a distinct group and is different from the application of the term for socio-economic classes or national identities.

Transparency about earnings, distributions, policies, and decisions about new strategic directions is a feature that is common to all user owned and controlled businesses, whether constituted as cooperatives or as alternative business organizations. Transparency, in turn, often leads to internal disagreements by users, which is a result that firms without transparency can avoid (Reynolds).

The cooperative difference is in the practice of solidarity as a commitment to resolving differences to prevent departures or exiting by members. In contrast, user firms, such as those organized by lawyers or small technology businesses, will often have departures over conflicts in policy or strategic directions with member solidarity noticeably absent.

The cooperative identity offered by the USDA 3 definition would be improved by asserting the users’ commitment to consensus and to each other’s fair treatment. Member solidarity requires more user action than just having mutual economic interests. While this attribute falls under member governance, the user-control principle is not equivalent to the necessity of voice for all members, and their commitment to keep one another in the membership rather than let the exit option run its course (Hirschman).

¹ Ian MacPherson had led the ICA project on revising the cooperative principles. He passed away on November 16, 2013.

Cooperative solidarity is also operative when a membership leaves behind a financially sound business for younger members to continue. When cooperatives maintain a commitment to not demutualize, they exhibit solidarity that is not present in many other types of user-owned and controlled businesses.

Principles and the distinctiveness of cooperatives

Commenting and critiquing cooperative principles is a far easier task than having to prepare such statements. The two sets of definitions of cooperatives and principles discussed above have all made important and different contributions.

USDA 3 exhibits the virtues of being a concise definition that includes essential attributes of cooperatives. Whether or not additional attributes are needed for a distinctive identity was examined in this paper.

For most intents and purposes, the expression of USDA 3 as a definition is satisfactory. It is suggested that the attribute of solidarity, meaning the members' concern for one another's economic interests in the cooperative, would convey a decisive distinctiveness. Member solidarity supports, and does not conflict with, an individualist perspective, unless the latter is defined in the narrow sense of atomistic individualism.

The ICA took up the issue of cooperative identity. Its identity statement seeks differentiation of cooperatives from other forms of business and from the command systems of governments. The argument was made above that while individual ownership is a common element of all businesses, it has specific forms that deserve to be more highlighted in the ICA statement.

It was also pointed out, drawing upon comments of cooperatives experts, that Principle 7, "concern for communities," may not offer much distinctiveness. If cooperatives accomplish a concern for the benefits of all members and an active democratic consensus on decisions, they will set an example that communities around the world will want to emulate.

In closing, the effort to understand the history of, and apply critical analysis to, the definitions and principles is an important part of keeping cooperatives relevant and successful. This intellectual

pursuit is definitely a legacy of Ian MacPherson.

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