

NEW GENERATION CO-OPERATIVES

Resource Materials

FOR BUSINESS DEVELOPMENT PROFESSIONALS
AND AGRICULTURAL PRODUCERS



Centre for the Study of Co-operatives
University of Saskatchewan

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CARD aims to facilitate the efforts of Canada's agriculture and agri-food sector to respond positively to changes by taking advantage of new opportunities, fostering industry self-reliance, meeting future challenges, and becoming more competitive in the changing domestic and international policy environments and global market. We are grateful for the CARD funding that made this initiative possible.



The pilot project activities undertaken in Saskatchewan and southwestern Manitoba in connection with this research were organized and overseen by the Centre for the Study of Co-operatives at the University of Saskatchewan. The project benefited from the expertise and dedication of a number of individuals.

Murray Fulton, a professor in Agricultural Economics and Fellow in Agricultural Co-operation at the Centre for the Study of Co-operatives, University of Saskatchewan, oversaw the project from beginning to end, his expert guidance a natural extension of the work he has been doing for a number of years around NGCs.

Roger Herman, a consultant working for the Centre for the Study of Co-operatives at the University of Saskatchewan, was the NGC Pilot Project Co-ordinator. His organizational skills and tireless dedication kept the project on track and ensured the highest quality of professional results.

The Centre for the Study of Co-operatives also hired a number of consultants to assist with various phases of the work. These included **Heather McNeill**, who recently completed a master's degree relating to NGCs and member commitment; **Mary Ellen Hodgins**, a management consultant with close ties to the legal and accounting communities; **Martin Chicilo**, Community Development Manager with the Saskatoon Credit Union, who has experience developing co-operatives in the agricultural sector in Saskatchewan; and **Wendy Farrington**, who provided administrative support.

An Introduction

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The New Generation Co-operative (NGC) concept is attracting attention as a means of increasing farm income and offsetting some of the negative impacts of recent changes in agriculture. Saskatchewan has new legislation that makes it possible to achieve all the benefits of the NGC model. The purpose of this introduction is to provide a brief summary of the characteristics of the New Generation Co-operative model.

The agricultural system is undergoing dramatic change. Changes in technology, institutional structures, regulations, the integration of value chains, and the globalization of agricultural markets are resulting in an integrated system in which the family farm is increasingly interwoven with the food distribution chain. Consumers today are increasingly demanding choice, quality, consistency, and value. Producers and the food industry are capable of providing what the consumer wants, but only if changes are made to the structure of agriculture. Advances in biotechnology and information technology make it possible to engineer food at every level, from farm gate to dinner plate. Biotechnology enables the isolation and incorporation of specific traits in plants and animals, effectively providing what the consumer wants. Information technology enables the industry to monitor consumer preferences and track products throughout the value chain, incorporating this information at all levels.

These technological changes also necessitate changes in marketing channels. The preservation of product identity is required to assure that the character-specific product reaches the consumer who is demanding it. Commodity markets (where products are gathered, mixed, and passed to processors who produce generic food goods) are not structured to accommodate the designer products of the modern food chain. More direct marketing channels, such as production contracts and vertical integration, are required to maintain the identity of genetically altered or organically grown agricultural products. Experts predict that the vertical integration of marketing channels will continue to escalate.

Another change that profoundly affects Saskatchewan farmers is the loss of the WGTA, or “Crow” subsidy. Farmers now shoulder the full cost of transporting their raw commodities to distant ports. Saskatchewan producers half-way between Vancouver and Thunder Bay have witnessed the result of this change. The net effect of all these changes is obvious to the farmers: lower returns for primary production. Farmers have done everything in their power to adjust to these changes. They have increased their acreage, diversified into special crops and livestock, and reduced costs wherever possible. New strategies, different organizational structures, and new attitudes are necessary if Saskatchewan agriculture is to survive.

Farmers can exploit their position within a vertically integrated agricultural system if they retain ownership of their products beyond the farm gate and invest in ventures that add value to those products. The New Generation Co-operative model offers farmers the opportunity to join together to move up the value chain and capture some of the profits. The success of this structure has been witnessed in Minnesota and North Dakota, where sugar beet (since 1974), bison, and durum (since 1990) producers have owned processing facilities and gained returns, in the form of dividends, from those ventures. Other examples of NGCs include facilities to process organic grains, soybeans, eggs, specialty cheeses, and edible beans.

The NGC structure is unique, particularly in its share structure, which is characterized by three classes of shares: membership, equity, and preferred. The membership share gives the holder the right to vote and to purchase equity shares, which are attached to delivery rights. NGCs are organized to add value to an agricultural commodity such as bison or durum. Only producers of the commodity can hold membership shares, thereby ensuring that control of the venture remains in the hands of the producers. NGCs adhere to the basic principle of co-operation set out by the Rochdale Society of Equitable Pioneers in 1844: democratic control, and one member, one vote. Voting rights are tied to membership, independent of the level of investment. This ensures that no one member can exercise control over the group.

The equity share allocates delivery rights to the co-operative and raises the capital necessary for establishing the venture. Each equity share purchased gives the member the right and the obligation to deliver one unit of product (i.e., one bison or one bushel of durum) to the co-operative for processing. This is a two-way contract: the member is committed to deliver, and the co-operative is committed to take delivery. The contract sets out the standards for quality, and delivery is regulated to keep the plant running at capacity. In today's market, quality and consistency are extremely important. Therefore, the delivery contract sets out specific quality conditions. The co-operative can reject deliveries if the products do not meet these quality standards. Rarely is this necessary, however, because the members contract only a portion of their production to the co-op, and they select the highest quality product for delivery to their own processing plant. In the event that a member is unable or unwilling to make delivery, the co-operative will purchase the amount of the product covered by the contract and charge the cost towards the member's equity account. This strategy ensures that the co-op will have a consistent quality and quantity of product, and can focus on developing markets.

The purchase of delivery rights (equity shares) represents a significant investment on behalf of producer-members and a significant equity infusion for the co-opera-

tive. In 1990, for example, the North American Bison Cooperative sold 180 membership shares at a cost of US\$100 each. These 180 members purchased a minimum of ten equity shares at a cost of US\$250 each, a minimum investment of US\$2500. The sale of delivery rights is a mechanism for securing start-up capital. Member equity investment represents 35–50 percent of the start-up costs. The obvious benefit to the co-operative of low debt is augmented by the benefit of member commitment. The loyalty of members is locked in through the contract and the investment; the member has made a large investment and will act to ensure the success of the venture. The equity shares are tradeable and transferable. The shares have value and can be sold to other producers with the approval of the board of directors. Shares can be passed on to the next generation along with other assets.

The preferred share allows the co-operative to invite investment from non-producers. Preferred shareholders cannot vote except in certain circumstances, as described in the legislation. The preferred share offers a limited, fixed rate of return. Communities and non-producers choose to purchase preferred shares because they want to support development in their communities and encourage job and wealth creation close to home.

NGCs are select- or closed-membership co-operatives. The feasibility study determines the most efficient plant size, which, in turn, determines the amount of product the plant can accept. Equity shares are issued to members based on the capacity of the plant. Once the allotment of shares is sold, the membership is closed. New members will be accepted and additional equity shares issued if the plant expands. Comprehensive feasibility studies and business plans are critical to the success of these ventures. NGCs often operate in niche markets, where it is important to understand the type, quality, and quantity of product demanded. A clear understanding of markets and consumers has enabled these ventures to serve markets that large corporations cannot.

Although some co-operatives have actually increased the price of the raw commodity, the primary economic benefit to members flows from the dividends of processing and marketing. Producers are paid market price for the delivery of their raw commodity, but because they own the processing plant, they gain returns from processing activities as well. They have vertically integrated upwards in the food industry and captured the returns to primary and secondary processing.

The vertically integrated structure encourages the effective use of market and production information. The structure enables market information to be combined with local production knowledge to produce the type of product required to serve lucrative niche markets.

The term New Generation Co-operative is not a magic structure, and it should not be applied to ventures that do not incorporate the strategies of two-way delivery contracts and high member equity investment. Producers must be willing to commit time to the development process, to invest sufficient equity to capitalize the project, and to contract product to supply the plant, or the project will not succeed. If producers are not committed through delivery contracts and investment, it will be difficult to leverage other investment funds, either as debt or outside investment capital. If the two-way contracts are replaced with softer delivery agreements, the risks to the co-operative increase because it will not have a secure supply of product.

Why NGCs?

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There are two questions that need to be addressed: first of all, “Why a co-op?” and second, “Why a New Generation Co-op structure?”

Simply stated, a co-op is an organization in which the owners are the users and the users are the owners. For producers, the most important reason for forming a co-op is when there is something a group can accomplish that individuals cannot accomplish on their own. There must be some benefit from collective action; by producing in larger volumes, for instance, a group of farmers might be able to reduce their costs and access a different market.

A second reason for choosing a co-operative structure is when the activity a group of farmers wishes to undertake involves a highly specific asset. I will return to this later.

The third point is: choose a co-op when relationship risk is important. One of the key characteristics of any co-op is the principle of “one member, one vote.” If a group of farmers is putting money into a particular activity, the principle of “one

member, one vote” allows each participant to feel that he or she has some involvement in the organization. It is also a way of dealing with the mistrust of one another that farmers often feel. Our research has shown that it is often the case that when farmers realize that they have to do something jointly, they concurrently realize that they don’t quite trust the other parties. “One member, one vote” becomes a means of developing the trust that will be necessary to carry on the activity, because everyone knows that they will each have a say in the operation. They also realize, of course, that everyone else has a say in the operation, and the only way to make the undertaking work is if they can find consensus.

The alternative is not to form a co-op but to create a standard corporation in which voting is on the basis of investment. This can create problems of its own, as it can potentially allow a small group of people to take control based on the size of their investment. When a small group of investors wants to control a particular activity or process and brings in others simply to supply product, that is an excellent reason not to form a co-op. Any number of other organizational structures would work better. Indeed, ownership and control by a small group, with the majority of individuals in a supplemental role, is not a co-operative.

The key characteristics of a New Generation Co-operative (NGC) are: it involves some kind of processing or transformation; it has a closed membership; it requires fairly substantial investments by the members at the beginning; there is a two-way delivery right signed between the member and the co-op; and, finally, delivery rights are tradable. Producers should look at a New Generation Co-op model when a transformation of the product—whether in time, space, or form—is being carried out, and when either quality or quantity is important in this transformation.

As suggested above, one of the key questions in forming an NGC is, “Is there a highly specific asset in place, in either production or processing?” And the key question in defining a highly specific asset is, “What is the value of the asset or the investment in its next best use?” If the value is low, then the asset is specific. In

other words, if what you can get for the sale of this asset is significantly below what it cost you to purchase it, then you have a highly specific asset. One example would be a new production process that nobody else has invested in; if you invest in it and then try to resell it, you likely won't get 25¢ on the dollar. Large research and development expenditures, high advertising costs, and the purchase of specialized equipment are all examples of highly specific assets. If the co-op is going to be investing in these kinds of assets, an NGC is likely the most appropriate organizational structure.

If a group has made a substantial investment in a highly specific asset, it wants to be sure that it will receive the necessary volume of production from its farmer members in order to make the operation work. As both producer and processor, each NGC member has an incentive to provide the proper quantity and quality of product. Indeed, under the delivery contracts of the NGC model, each member is obligated to deliver the product regardless of market conditions, so that the co-op will be guaranteed a product source. The organization is thus assured that it will be able to carry on and not have to sell off its assets.

A New Generation Co-op can be formed purely for marketing purposes if two criteria are met. First, the co-op must do something that the members cannot do individually, such as supply a consistent product year-round. Second, the NGC structure must aid in undertaking the co-op activity. Does the delivery contract enhance the consistency of supply? Are quality and quantity of product critical factors in the co-op's operations? If so, the New Generation Co-op is a model for bringing those factors into the equation.

To summarize, form a co-op when a group can do something that individuals are unable to do, when input from all members of the group is important, and when one segment of the group is not looking for control. For an NGC when the investment that the group must make is highly specific, when an assured supply of product (often of a high quality) is important, and when a sense of ownership by *all* members will aid in assuring supply and in ensuring good governance of the co-op.

New Generation Co-operatives and the Law in Saskatchewan

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Co-operative law in Saskatchewan underwent a significant change with the introduction of the *New Generation Co-operatives Act* (hereinafter the *Act*) in January 2000. The *Act* provides a mechanism for agricultural producers to join together to jointly market and/or process their products. New Generation Co-operatives (NGCs) have been formed in the US as a way for farmers to increase their share of the consumer dollar and as a means of revitalizing rural areas. Yet despite their success in the US, they have been slow to develop in Canada. The introduction of legislation specifically accommodating the main elements of the NGC is expected to increase the adoption of the model in Canada.

The purpose of this paper is to highlight the key features of the *New Generation Co-operatives Act* and to explain their importance. The paper is designed to be used by individuals who wish to create an NGC and thus take advantage of its strengths as a business vehicle. The paper will focus primarily on the differences between the *New*

Generation Co-operatives Act and the more general *Co-operatives Act*. It is assumed that readers have a basic knowledge of the *Co-operatives Act* and of co-operatives.¹

Although the *NGC Act* contains a number of elements that distinguish it from the *Co-operatives Act*, these elements are largely concentrated in four areas: articles and by-laws; marketing contracts; finance; and fair dealing. This paper highlights the relevant points in each of these areas, as well as offering a broader picture of the *NGC Act*.

Articles and By-Laws

Every corporation and co-operative must set parameters and guidelines for its governance through articles and by-laws. The *New Generation Co-operatives Act* addresses a number of important issues surrounding the articles and by-laws and provides direction when applicable. These fall into the following areas:

- The dividends on common shares must have a maximum value set in the articles (s.6(2)(l)).
- The co-operative must indicate whether it intends to issue preferred shares, and it must delineate the rights and restrictions ascribed to each class of shares (s.6(2)(d)).
- The articles may specify the rules for distribution of property on dissolution of the co-op (s.6(2)(m)). The *Act* further clarifies this issue by allowing for the distribution to members either equally or on the basis of patronage (s.262(12)).
- The members' power to manage the co-operative and to restrict the authority of the directors may be established in the articles (s.6(2)(n)).

The *New Generation Co-operatives Act* also contains some unique features:

¹ Due to the relative newness of the *New Generation Co-operatives Act*, there are few sources that examine the differences between this *Act* and the *Co-operatives Act*. A good source of information is the speaking notes and outline presented by J.J. Dierker, QC, at the New Generation Co-operatives Experts Workshop of March 2001, available in the binder of materials circulated to workshop participants.

- The *Act* generally provides for more flexible share transferability. The transfer rights of common shares and s.35 membership-only preferred shares, however, must be listed in the by-laws as per s.7(1)(a)(iii).
- The by-laws of the co-operative may establish the obligation of the members to provide goods or to use its services where this is a condition of membership (s.7(1)(a)(v)).

Marketing Contracts

A key element in co-operative organizations is the relationship between the co-operative and its members. In an NGC, this relationship takes form and is rooted in the marketing or supply contract, which is an agreement with the members to sell or deliver raw goods for sale, processing, or preparation. The marketing contract is critical to the operation of an NGC, since it determines the supply of the raw product that is marketed and/or processed by the co-operative. The agreement may outline special characteristics and/or relevant details.

The *NGC Act* also provides additional direction to the relationship between the co-operative and its members. The co-operative may act as an agent on behalf of the members (s.215(2)(b)), and hold the goods in pools (s.215(4)). If the co-operative holds the goods, there is no transfer of title (s.215(2)(a)). Members' goods in the co-operative's possession are also precluded from liability attaching on behalf of the co-operative's creditors (s.215(3)). Other significant details of the contract may include the payment to members for goods sold or delivered, the manner of charging for the co-operative's expenditures, and the deduction of a loan to the co-operative or money used to buy shares in it (s.215(5)). The co-operative may also advance part payment to the members for goods delivered, or to be delivered, as per the contract (s.214(1)).

Because the *Act* provides NGCs a high degree of flexibility in arranging them, marketing contracts can take many forms and be structured in numerous ways. The articles and by-laws may house the marketing contract between the co-operative and the member (s.6(6); s.7(2)), or the contract may exist as a separate entity as laid out

in s.215. Where it is foreseen that an ongoing relationship with little deviation from the initial terms will exist, the contract may be built into the articles or by-laws. Contracts located in the articles are strongly entrenched. Any alteration of the contract would constitute a fundamental change to the articles and trigger the dissenter's rights of the members and preferred shareholders (s.259). Marketing contracts in the by-laws allow for increased flexibility, though modifications face significant restrictions. Any change to the terms of a marketing contract in the by-laws, including termination, would require a special resolution by the membership (s.201(1)). A marketing contract peripheral to the articles and by-laws offers the most flexibility. It may be structured as a uniform contract for all members, or customized for each particular member, which would make it easier to effect changes to the contract since consent need only come from the NGC and the individual member. Changing the contracts of certain members and not others, however, can give rise to issues of fairness.

In the event of a breach of the marketing contract, the *NGC Act* allows for several remedies. The innocent party is entitled to seek an injunction preventing further breaches (s.214(2)(a)), which is a particularly notable remedy because it enables the innocent party to bypass the burden of proving irreparable harm. Also available is any equitable relief specified in the contract and specific performance (s.214(2)(b), (c)). Even member withdrawal does not discharge the duty to perform. The wide range of remedies at the disposal of the innocent party reinforces the NGC's emphasis on performance of the contract and consistency in the delivery and acceptance of product.

Financing

The financing of a co-operative often draws on numerous resources, including the assumption of debt and the issuance of shares. The New Generation Co-operative identifies its membership and obtains capital for its operations through its financing structure. The NGC share scheme is dictated by its capital requirements. Each co-

operative will have common shares—essentially membership shares—but it may also issue preferred shares in any number of classes (s.6(2)(d)). Common shares are restricted to members only (s.243(1)(g)) and are sold at a par value (s.47(3)) established in the articles (s.6(2)(b)). Common shares do not represent a significant source of capital for the NGC because the members' required contribution is typically set quite low.

Preferred shares are a more valuable source of capital for New Generation Co-operatives, largely because of their flexibility and versatility. Of particular importance are the delivery right shares, which are at the core of the NGC model and are described in more detail below.

An advantage of preferred shares is that their classes may be structured with different rights and limitations, subject of course to the *Act*. Important elements in a share class include voting rights at the directors' election (s.34(1)) and the availability of shares to the public (s.33(1)(a)). Public preferred shares are pivotal because they allow the community to support the venture and to indirectly participate in developing the local economy. These shares also make the NGC accessible to a much wider pool of investors, though a public offering requires full securities disclosure.

Preemptive rights and the use of proxies are two other features of the *NGC Act* open to preferred shareholders. Preemptive rights established in the articles (s.37(1)) allow shareholders the first right to any new offering of their respective class, up to the percentage of interest held prior to its offering (s.37(2)). These rights provide preferred shareholders some certainty of maintaining their interest in the NGC in the event of another offering, thus discouraging squeeze-outs by the board. Preferred shareholders who have the right to vote may also use proxies to represent them at meetings. This right does not extend, however, to common shares (s.217(1); s.216(2)).

Although preferred shares may be structured with a number of rights and restrictions, the *NGC Act* establishes specific guidelines. Preferred shares are issued with stated capital and maintain a stated capital account (s.48(1)). Both stated capital and par value are subject to reduction, but only through special resolutions by members and affected preferred shareholders (s.61(1)). Limitations are placed on any individual shareholder's interest, which is intended to prevent excessive power being held in the hands of single parties and to ensure membership control, thus maintaining the co-operative character. In s.40(1)(a), a preferred share class with director voting rights attached has an interest ceiling of 10 percent on each holder, and the directors elected by preferred shareholders cannot exceed 20 percent of the board (s.34(2)). All other classes of preferred shares are limited to 25 percent interest by one holder (s.40(1)(b)). Preferred shares are fully transferable, although transfers still require the board's consent (s.66(b)).

Within the preferred share category, the *NGC Act* specifically identifies and makes available an important class of member-only shares—delivery-right shares—in s.35. These shares are intrinsically connected to the marketing contract, together forming the unique relationship between the NGC and its members. The marketing contract establishes the obligation between the member and the co-operative, while s.35 shares delineate the scope of the duty. S.35 shares serve two key purposes: they provide a large share of the capital for the NGC and they are the primary means for earnings participation. Members who subscribe to such shares are obligated to provide or deliver a specified good or service, or have the right to receive a good or service in accordance with the contract between themselves and the co-operative (s.35(d)). This represents a critical departure from a traditional co-operative, where patronage is generally voluntary. In the NGC, the supply of product from the members is predetermined quantitatively and usually qualitatively, and performance of the obligation is mandatory.

S.35 shares are also closely linked to the processing emphasis of an NGC. Typically, each share represents one unit of product the member must deliver to the co-operative. The obligation is usually different for each member, depending upon the number of shares owned. However, it is common for minimums and maximums to be imposed on s.35 share interests, an action undertaken to maintain a certain degree of homogeneity among members. The price of the share is established by first determining the optimal efficiency of the processing facility and the product necessary to meet that capacity. The capital required for operational start-up is then divided by the amount of product needed for processing; the resulting figure is the share price. Due to the fixed number of units the facility can accommodate, and the s.35 shares based on those units, membership is consequently restricted. Thus, with s.35 shares, marrying the producer's capital contribution to delivery rights and obligations ensures a consistent supply of product for the co-operative and a guaranteed market for the producer, with the producer's patronage being directly proportionate to his or her equity.

Several additional rights and restrictions apply to s.35 shares. The shares must belong to a preferred share class (s.35(b)), are accessible only to members (s.35(a)), and the articles cannot be amended to allow nonmembers to hold them (s.243(1)(g)). In addition, s.35 shares carry no voting rights on director elections (s.35(c)), but shareholders may vote on the basis of their membership. Special participation rights, enumerated in s.35(e), allow holders to receive the surplus by way of patronage dividends or bonuses, to receive reserve amounts through dividends, and to have access to the remaining property on the co-operative's dissolution. The profits from the processing operation are usually distributed through the patronage dividends of s.35 shares. Like standard preferred shares, s.35 shares are fully transferable (s.66(a)), subject only to the board's approval (s.68).

The *Act* also provides guidelines for the regulatory bodies governing securities. Any co-operative issuing or trading securities initially falls under the jurisdiction

of the Co-operative Securities Board (s.318(1)), which has the option to direct the matter to the Saskatchewan Securities Commission (s.317(2)). Conversely, under s.317(3), the co-operative itself may elect to be governed by the commission. Any securities issuance or trade for membership shares, or exchanges involving bonds or debentures with financial and governmental bodies, are exempted from the jurisdiction of the Co-operative Securities Board (s.320(1)), although each co-operative must file a disclosure document with the board for a securities offering (s.319(4)).

Fair Dealing

The *NGC Act* addresses extensively the termination of the relationship between the NGC and its members, and the standards for fair dealing. When the relationship between the co-operative and a member has become untenable, the *Act* provides a number of means for members to leave the organization: withdrawal; expulsion by the board; or expulsion by members. In the event that a member voluntarily withdraws, the *Act* outlines proper conduct and procedure. A member may withdraw if notice is given (s.209(1)), and the co-operative has five years from the date of the notice to buy back the shares. Common shares are purchased at par value and the s.35 shares are purchased at the formula price set in the articles. If the articles are silent in this regard, then the buy back must be at fair market value (s.209(2)(a)). Loans to the co-operative by the member must be repaid, along with any amount held to the member's credit (s.209(2)(b)). Even though the member has withdrawn from the co-operative, however, he or she is still obligated to fulfill the marketing contract (subject to the board's discretion) until another suitable buyer can be found to take on the obligation (s.209(4)).

The *Act* provides a similar process for dealing with member expulsion from the co-operative. Termination of membership by the board requires a special resolution (s.210(2)), while expulsion at the hands of the members must be approved by a two-thirds majority (s.211(1)(b)). Upon an effective expulsion, the marketing contract between the member and the co-operative is terminated (s.210(8)(a)). However, the

co-operative must buy back all s.35 shares at the price described in the articles, or at fair market value if the articles are silent (s.210(7)(a)(ii); s.211(2)(c)). The co-operative is also obligated to purchase the member's common shares at par value, and pay out all outstanding loans to the member or credit held on the member's behalf (s.210(7)(a)(ii); s.210(7)(b); s.211(2)(c)). The *NGC Act* ensures members are dealt with in a fair manner and includes an appeals process to the registrar (s.212).

If a co-operative resolves to pursue fundamental change, the *NGC Act* addresses this in the form of dissenter's rights. Members or preferred shareholders have standing to dissent where the co-operative moves to: amend the articles in such a way that it will adversely affect their interest or adjust the restrictions on business activities; amalgamate; seek a continuance; or drastically alter its property holdings (s.259(1)). Preferred shareholders affected by an article amendment as per s.246 may dissent on significantly broader grounds, outlined in s.243 and s.244 (s.259(2)). This right to dissent is excluded on issues of a co-operative name change and/or an increase in the number of directors. A dissenting member or preferred shareholder may object to a proposed resolution (s.259(3)); if the resolution passes, the objection is deemed to be notice of intent to withdraw (s.259(4)). Once the impugned resolution has passed, the dissenting party may issue an actual notice to the co-operative. This notice demands withdrawal, payment of fair market value for common shares, repayment of any other interest outstanding, and the set price as established in the articles, or fair market value, on preferred shares (s.259(6)(c)). The co-operative is then obligated to pay the applicable amounts.

Joint membership provisions in the *Act* protect the co-operative from any shortages and allow producers to distribute some of the risk and obligations of marketing contracts. A membership jointly held places full rights and responsibilities of membership upon all parties (s.70(1)(a)). In addition, the *Act* stipulates that all parties holding a membership jointly have joint and several liability on all obligations respecting the membership (s.70(3)(b)).

Memberships and their respective rights are given more flexibility in the *NGC Act* than in traditional co-operatives. Each membership is fully transferable (s.66(a)) subject to the directors' approval (s.68). On the death of a member, the membership can be transferred to a beneficiary or executor regardless of their membership status (s.69(3)(a)), but although the beneficiary may enjoy most member rights and honour the obligations, voting is excluded (s.69(11)). The membership may also be subject to certain additional restraints. For example, the co-operative has the right to put a lien on a member's interest where monies payable to the co-operative pursuant to the articles or by-laws are considered debt (s.64); this practice can also apply to other types of shares (s.65).

In terms of dissolution, the *NGC Act* stays fairly true to the *Co-operatives Act*. A key difference, however, is worth noting. The *NGC Act* specifies that the articles may indicate how the property of the co-operative is to be distributed upon dissolution (s.6(2)(m)). In the event of the articles being silent, the property is to be distributed to a charity, another co-operative, or anyone the registrar designates (s.262(13),(8)).

Conclusion

The New Generation Co-operative holds promise as an effective vehicle for agricultural producers to move beyond pure production to access processing and preparation markets. The template for the NGC model is specifically outlined in the recently legislated *New Generation Co-operatives Act*, which details the items that distinguish it as a distinct business organization: the articles and by-laws, marketing contracts, the method of financing, and fair dealing. Each element contributes to the NGC's unique character and gives it the capacity to more efficiently provide producers the opportunity to move up the food value chain. Showing significant potential

for producers and practitioners on a corporate level, the NGC model is also another resource to be tapped in the future development of rural Saskatchewan.²

² Readers will find more material on this subject in another research paper prepared by and available from the Centre for the Study of Co-operatives titled *A Comparison of New Generation Co-operative Legislation in Alberta, Saskatchewan, and Manitoba*.

Taxation Issues

Brian J. Taylor, FCA
Deloitte & Touche LLP

How Are Members and Holders of Preferred Shares Taxed?

Purchase of Shares

The purchase of shares is not a tax deduction.

Patronage Dividends

Members pay personal (or corporate) income tax on all (allocated and deferred) patronage dividends received from an NGC. The income is taxed in the year it is received by the member.

Dividends on Preferred Shares

Holders of preferred shares pay tax on dividends received from an NGC.

Dividend Tax Credit

The dividend tax credit applies to taxable dividends received by individuals but excludes patronage dividends.

Withholding Tax

An NGC is required to deduct and withhold 15 percent tax on the portion of patronage payments (or sum of) exceeding \$100. The NGC remits the tax to the Receiver General on account of the member's tax liability. When the member files a personal (or corporate) income tax, the tax withheld will either reduce

taxes otherwise payable or increase the tax refund.

Capital Gains Tax

If a member sells shares, only 50 percent of any gain is taxable. If the member is a Canadian-controlled private corporation as defined in the *Income Tax Act of Canada* (the *Act*), the nontaxable portion of the capital gain can be paid on a tax free basis to its shareholders if prescribed conditions are met.

How Are NGCs Taxed?

Incorporated organizations, such as NGCs, follow corporate income tax laws.

Unallocated Net Income

Unallocated net income is taxable at the corporate rate, while deferred patronage allocations are taxed at the member level.

Dividends on Preferred Shares

NGCs may choose to pay dividends to holders of preferred shares. Dividends on preferred shares are not deductible in computing the income of the NGC.

More information regarding dividends on share capital is available at www.cera-adrc.gc.ca/E/pub/tp/i362ret/i362re.txt.html.

Federal Large Corporations Tax (LCT)

NGCs will be subject to LCT if capital (as defined in the *Act*) net of eligible investments exceeds \$10 million. Capital includes debt, unallocated retained earnings, and other items. The tax rate is presently 0.225 percent of capital in excess of \$10 million. Associated corporations must share the \$10 million exemption.

What Tax Deductions and Credits Apply to NGCs?

Tax deductions reduce an organization's taxable earnings. Tax credits reduce the amount of tax an organization pays.

Patronage Dividends

Patronage dividends are a tax deduction for a corporation such as an NGC. However, a patronage payment is deductible only if it is paid within the year, or within twelve months of the end of the year, to customers. A patronage payment is also deductible if it was made in a previous year in which such payments were not deductible.

Credit is not given to those customers to whom the patronage allocation would be less than \$5.00, and no deduction is allowable to the NGC in computing income for such credits not given.

More information regarding patronage dividends is available at www.cera-adrc.gc.ca/E/pub/tp/i362ret/i362re.txt.html.

Interest on Loan Capital

Interest on loan capital is deductible in computing income provided it is paid or payable in accordance with the *Act*. However, interest is not deductible unless it is paid pursuant to a legal obligation to pay the interest.

More information regarding interest on loan capital is available at www.cera-adrc.gc.ca/E/pub/tp/i362ret/i362re.txt.html.

Small Business Deduction

The small business deduction is an annual tax reduction on up to \$200,000 that may be claimed by a Canadian-controlled private corporation (CCPC) for carrying on an active business in Canada other than a “specified investment business” or a “personal services business.” In Saskatchewan, it reduces the effective corporate tax rate from 45 percent to 20 percent. Corporations with LCT capital in excess of \$15 million are not eligible for this tax reduction.

More information regarding the small business deduction is available at www.cera-adrc.gc.ca/E/pub/tp/i73r5et/i73r5e.txt.html.

Tax Considerations for NGCs in Saskatchewan

Saskatchewan Manufacturing and Processing Investment Tax Credit Corporations filing a T2 Corporation Income Tax (CIT) Return may be eligible for the Saskatchewan Investment Tax Credit (ITC) for Manufacturing and Processing. The ITC is a nonrefundable income tax credit that is designed to encourage plant and equipment investment for use in manufacturing and processing activities in Saskatchewan. The ITC applies as a percentage of the total capital cost of eligible building and machinery and equipment purchases. The current rate is 6 percent of eligible new or used acquisitions. The ITCs can only be used to offset Saskatchewan income tax otherwise payable.

More information on the ITC is available at www.cbsc.org/sask/sbis

Saskatchewan Corporation Capital Tax (CCT)

The CCT provides exemption for “natural product” co-ops where at least 90 percent of the members are individuals or other co-operative corporations and none of the members, apart from other co-operative corporations, has more than one vote.*

The capital tax rate is currently 6 percent of paid-up capital in excess of \$10 million. This \$10 million is available to every corporation, and does not have to be shared with associated corporations.

*This exemption may not apply to NGCs because preferred shareholders have limited voting rights (the Saskatchewan Department of Finance is apparently working on this issue).

When Do NGCs Pay Income Tax?

Annual Payments

An NGC only has to make one annual income tax payment if the federal taxes payable for the year or the prior taxation year are \$1,000 or less. An NGC will also make annual income tax payments if the corporation is in its first taxation year and is not a continuation of a predecessor corporation.

Instalment Payments

After the first year of taxation, and if the prior year's federal taxes were \$1,000 or more, NGCs pay income tax in monthly instalments. Instalment payments are due on the last day of every complete month of an NGC's taxation year. The first payment is due one month minus a day from the starting date of the corporation's taxation year. The rest of the payments are due on the same day of each month that follows.

Late Returns and Penalties

Penalties may apply if an NGC files the return late. The penalty for filing a late return is 5 percent of the unpaid tax that is due on the filing deadline, plus 1 percent of this unpaid tax for each complete month that the return is late, up to a maximum of twelve months. In exceptional cases, interest and penalties on late payments can be waived or cancelled.

Interest

Interest is charged on late instalments and late tax payments. The current rate charged is 10 percent. This interest expense is not deductible for tax purposes. Interest is also paid to the taxpayer on refunds. The rate is 2 percent less than the rate charged. The current rate is 8 percent. This interest income is taxable.

Filing a Corporate Tax Return

NGCs based in Alberta, Manitoba, and Saskatchewan mail the T2 Corporate Income Tax Return to: Tax Centre, Winnipeg MB, R3C 3M2.

Record Keeping

Books and records or electronic records, including related accounts and vouchers, must be kept for at least six years from the end of the last year to which they relate. Books and records or electronic records must be kept until two years after the date the corporation is dissolved.

Key Steps Relating to the Issuance of Securities¹

Ian McIntosh²
Saskatchewan Securities Commission

Definition

A security is defined under *The New Generation Co-operatives Act* (hereinafter referred to as the *New Gen Act*) as including a preferred share, a debt obligation of a co-operative, and a certificate evidencing that share or debt obligation, and, for the purposes of Parts XVI, XIX, and XXII, includes a common share and member loan.

Why Do NGCs Issue Securities?

NGCs will need to assemble sufficient financing to develop and initiate the operation of their businesses. It is unlikely that the total capital required could be borrowed from financial institutions; therefore, the co-operative must seek investment from its members, and possibly the public. Capital raised in this manner involves the issuing of securities. These securities can be in the form of:

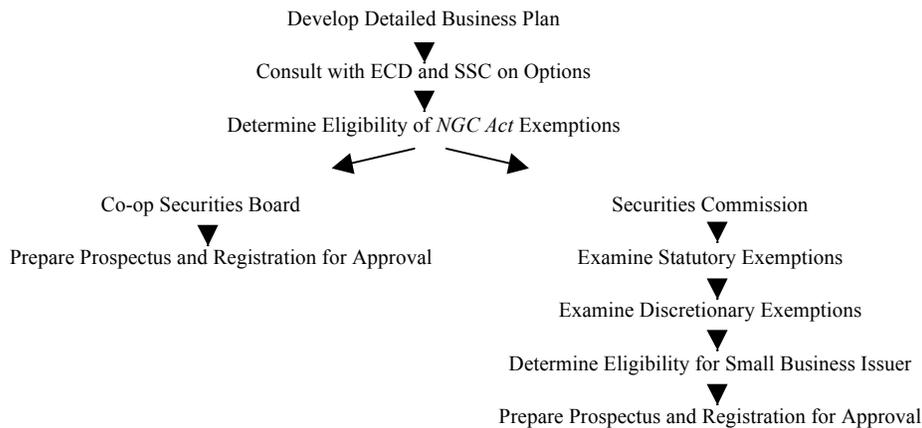
- *Common shares*, which may be sold only to members;
- *Preferred Shares*, which include the following two types:

¹ This paper does not necessarily represent the views of the Saskatchewan Securities Commission, nor does it constitute a legal opinion. Readers are advised to seek professional legal advice before proceeding.

² With acknowledgement to previous materials prepared by staff of Economic and Co-operative Development.

- *Member Right Shares*, which may only be sold to members, which carry no vote on election of a director, and which obligate its holder to provide the co-operative a specific good or services or give the holder the right to receive from the co-operative a specific good or service; and
- *Preferred Shares in a Series*, which may be sold to members and the general public, and may include specified rights and restrictions;
- *Member Loans*, including any agreement by which a member agrees to loan money to the co-operative; and
- *Other Debt Instruments*, including bonds and debentures issued to members or the general public by which the co-operative agrees to repay, with or without interest.

Part XXII—Security Issues of the *New Gen Act*, together with the Regulations, set out the rules governing how an NGC can issue securities:



Develop a Business Plan

Complete a business plan, including details of sources of financing and a detailed explanation of the business operations. For larger offerings, conduct a feasibility study.

Consultations

The author encourages advance consultation with issuers and their professional advisors to discuss their proposal, and for assistance in determining whether the securities qualify for existing exemptions or if a prospectus may be required. Please contact the Deputy Director, Corporate Finance, at (306) 787-5867.

Steps to Obtain Approval to Issue Securities

Approval to Issue Securities

Unless the security is exempt under the *New Gen Act* or Regulations, the co-operative must apply to the Co-operative Securities Board (the Board) regarding the issuance of securities. (The Board has the legislated responsibility for reviewing and approving the securities offerings of co-operatives and setting such terms and conditions on the approval as it sees necessary.) A co-operative also has the option under the *New Gen Act* to advise the Board by written notice that all trades by the co-operative in a proposed offering of the securities specified in the notice will comply with *The Securities Act, 1988* (hereinafter referred to as the *Securities Act*). This option is an important change from how securities offerings are dealt with under *The Co-operatives Act, 1996*.

As a first step, a co-operative should determine if the proposed issue of securities is exempt from any review under the *New Gen Act*.

New Generation Co-op Act/Regulation Exemptions

Examine the possibility of whether the offering of the securities could be exempt under the *New Gen Act* or Regulations. Exemptions include:

- A. bonds, debentures, or other indebtedness of or guarantees by a trust corporation or a loan corporation licensed pursuant to *The Trust and Loans Corporations Act* or an insurance company licensed pursuant to *The Saskatchewan Insurance Act*;
- B. certificates or receipts of a trust corporation or a loan corporations licensed pursuant to the *Trust and Loan Corporations Act*;
- C. bonds, debentures, or other indebtedness guaranteed by the government of Canada or of any province or territory of Canada;
- D. any securities where the purchase is a requirement of membership in the New Generation Co-operative as set out in the by-laws and the total value of those securities purchased by the member does not exceed \$1,000;
- E. securities sold to a trust or loan corporation, an insurance corporation, a credit union, or a bank;
- F. prepaid accounts where a member pays for goods and services in advance of delivery;
- G. shares issues in payment of a dividend, or interest payment on shares, or a patronage dividend;
- H. securities sold only to members of the co-operative, where all the members are also directors of the co-operative;
- I. securities sold only to members of the co-operative where:
 - i. the proceeds are used to purchase assets that are used solely by or for members, and
 - ii. the cumulative amount raised using this exemption does not exceed \$100,000;
- J. securities sold only to members of the co-operative where:
 - i. the proceeds are used to pay any of the following costs:

- a. costs related to the preparation of feasibility studies, business plans, and other similar documents, and
 - b. costs related to the preparation of any materials used or costs incurred in relation to an offering of securities by the co-operative; and
- ii. the cumulative amount raised using this exemption does not exceed \$100,000.

If the co-operative is unable to make use of these exemptions, it should look to the exemptions available under *The Securities Act*.

As previously indicated, the co-operative has the ability to have its trades done in compliance with the *Securities Act* if it wishes.

Saskatchewan Securities Commission

The Securities Act, 1988—Statutory Exemptions

If the co-operative determines that a statutory registration and prospectus exemption under the *Securities Act* could be applicable to the proposed offering of securities, the co-operative can elect, by written notice to the Board, to have all trades in the proposed offering specified in the notice comply with the *Securities Act*. These exemptions are included in detail in the “How To Raise Capital Using Exemptions” paper prepared by the Securities Commission. To receive a copy of this paper, contact the Saskatchewan Securities Commission at (306) 787-5299; alternatively, the information is available on the Saskatchewan Securities Commission web site at: www.ssc.gov.sk.ca.

Discretionary Exemptions

If the issuance of the securities does not fit within the statutory exemption from the registration and prospectus requirements of the *Securities Act*, then the co-operative can apply to the Commission under Section 83 of the *Act* for a discretionary exemption waiving the registration and prospectus requirements of the *Securities Act*. The Commission has the power to grant a discretionary exemption from both the prospectus and registration requirements of the *Act* under this section. To apply for a

discretionary exemption, the co-operative must follow the procedure set out in Saskatchewan Policy Statement 12-601, “Applications to the Saskatchewan Securities Commission.” To receive a copy, contact the Saskatchewan Securities Commission at (306) 787-5299; alternatively, the information is available on the Saskatchewan Securities Commission web site at: www.ssc.gov.sk.ca.

It is possible to apply to the Board for a discretionary exemption under *The New Generation Co-operatives Act*. As guidance in preparing the application, the New Generation Co-operative should follow the procedures set out in Saskatchewan Policy Statement 12-601. The application should be sent to the attention of the Secretary to the Board, c/o The Saskatchewan Securities Commission.

Before granting a discretionary exemption under Section 83 of the *Securities Act*, the Commission must first be satisfied that it is not prejudicial to the public interest to do so. There is no guarantee that the Commission will grant a discretionary exemption when applied for. The Commission will consider whether there are other factors in place for public protection, making prospectus and registration requirements of the *Securities Act* unnecessary.

Discretionary exemptions are often granted where a trade almost meets the requirements of a statutory exemption and the policy considerations behind that statutory exemption are met, but, for a technicality, the trade does not fall within the statutory exemption.

The Commission may grant a discretionary exemption in cases where there is a special relationship between the NGC and the investors, and, through this special relationship, the investors have a special knowledge both about the NGC and its promoters. In this case, the investors may not require the protection afforded by registration or the disclosure normally made in a prospectus.

Discretionary exemptions may be granted in cases where the Commission is satisfied investors are knowledgeable, sophisticated, can protect themselves, and don't require the protection of the *Securities Act*.

In general terms, the Commission is open minded as to when it will grant a discretionary exemption. It must be satisfied that the results will be that the same level of public protection is provided, albeit in a different manner, as would be present if the registration and prospectus requirements of the *Securities Act* had been complied with. Discretionary exemptions usually have terms and conditions attached to them, and may, or may not, require the use of an offering memorandum.

The sale of securities by an NGC pursuant to a discretionary exemption does not in and of itself trigger any Continuous Disclosure Requirements or Resale Restrictions unless such requirements are built into the terms and conditions of the discretionary exemption received from the Commission. Therefore, an NGC will only become subject to those Continuous Disclosure Requirements and Resale Restrictions that are imposed as a term of the discretionary exemption. An issuer should look to the terms of the discretionary exemptions for its requirements in this regard. It is usual for the Commission to build in these types of requirements. This is the same with respect to the report of sales that must be filed with the Commission after the use of the discretionary exemption. The terms of the discretionary exemption received must be reviewed to find the NGC's requirements in this regard.

The most common discretionary exemption under Section 83 that could be used for an NGC would be the Community Ventures Exemption.

Community Ventures Exemption

This policy statement allows the NGC to apply for and the Commission to exempt the NGC from the registration and prospectus requirements of the *Securities Act*.

The conditions that apply under the Community Ventures Exemption are:

- a. the project must be located in a small community;
- b. the co-operative cannot raise more than \$1 million;
- c. the investors must live within a certain geographic area of the small community;
- d. all salespersons and promoters must live within the small community;
- e. there is no limit on the number of investors; and
- f. an offering memorandum approved by the Commission.

For complete information on this exemption, refer to the Community Ventures Information Package available by contacting the Saskatchewan Securities Commission at (306) 787-5299.

For information about the use of exemptions, call (306) 787-5879 (Legal Branch).

Prospectus Distributions

Should the New Generation Co-operative find that there are no statutory or discretionary exemptions available for its proposed security offering, then it is probable that a prospectus will be required.

A prospectus is a legal document by which securities are offered for sale. The prospectus must contain full, true, and plain disclosure of all material facts relating to the securities issued. It provides prospective investors with sufficient information to enable them to make an informed decision about whether or not to purchase any of the securities offered. The Securities Regulations establish the details as to the form and content of the prospectus.

If this is the avenue taken, the co-operative again has a choice to make: whether the offering will be subject to the *New Gen Act*, or whether an election will be made to have the offering reviewed and subject to the *Securities Act*. In either case, the co-operative needs to do a fair bit of work in advance of preparing and filing a prospectus. This work would include a detailed business plan and a feasibility study.

The Disclosure Document

The information disclosure requirements for a prospectus filed under the *New Gen Act* and the *Securities Act* are essentially identical. The form to be followed in preparing a prospectus for a New Generation Co-operative is the same in either case, Form 13—Information Required in Prospectus of Industrial Company. This form is found in The Securities Regulations. The Board has directed that this form is to be followed if the prospectus is filed under the *New Gen Act*, and subject to review and approval by the Board. This same form is compulsory if the New Generation Co-operative elects to have the distribution subject to the *Securities Act*.

The Review Process

The review process for prospectus filings is the same under the *Securities Act* and under the *New Gen Act*. The materials are to be filed with the Deputy Director, Corporate Finance, with the Commission. The Deputy Director also serves as Secretary to the Co-operative Securities Board. The prospectus and any supporting materials will be reviewed in detail by the staff of the Commission. A letter requesting changes or additional detail will normally be provided within ten working days of receiving the prospectus. Thereafter, it will be up to the New Generation Co-operative to resolve the comments. A revised prospectus incorporating the changes will then be required for further detailed review. Additional comments may be raised once more, with a further draft filed for review. This review process can take from six to eight weeks.

Once the staff are satisfied with the disclosure, and the selling process, as outlined below, has been appropriately addressed, approval to sell the securities will be given by one of two means. If the filing was made under the *Securities Act*, the Deputy Director, Corporate Finance, will issue a final receipt for the prospectus and selling may then proceed. If the filing has been made under the *New Gen Act*, the deputy director will provide a copy of the final prospectus along with a recommendation to the Board. Conditions of approval may also be provided to the Board. If the Board is

in agreement with the recommendations, they will approve the prospectus, and sales may commence.

For further information on the prospectus processes, contact the Deputy Director, Corporate Finance, at (306) 787-5867.

Registration and the Selling Process

A major consideration for a New Generation Co-operative will be the manner in which it contemplates the selling of the securities offered by prospectus. Under the *Securities Act*, the securities must be sold by a registrant company. Further, individuals selling the securities must also be registrants.

Frequently, smaller issuers are unable to make arrangements with a registrant to sell the securities offered by their prospectus. To assist these smaller issuers, the Commission has approved General Ruling Order (GRO) 31-902—Saskatchewan Small Business Security Issuer. This GRO relaxes the normal registration requirements and allows the issuer to register as a security issuer; in other words, it will be offering its own securities for sale. The individuals designated by the issuer to sell the securities on its behalf will be required to take a one-day sales course provided by the staff of the Commission, and then must write and pass an examination, taken the same day as the course. This course provides basic information on the dos and don'ts of selling securities. Additional detail on this GRO follows.

The Board has indicated, in meetings held to discuss New Generation Co-operatives, that the selling issue is also of concern to them. They have indicated that they, too, will have concerns with how the securities may be sold, and it is likely that they will require the New Generation Co-operative and its sales force to follow the same requirements as set out in GRO 31-902.

To date, there are no precedents in this area.

Ongoing Continuous Disclosure Requirements

Once a New Generation Co-operative has raised money by prospectus, it will be required to communicate with its security holders on a regular basis. If the offering has been done under the *Securities Act*, the ongoing reporting requirements are statutory, and would include providing interim quarterly financial statements and annual audited financial statements, as well as annual proxy and information circular materials.

If the offering has been done under the *New Gen Act*, co-operatives should anticipate that the Board will make similar reporting mandatory as a condition of approval for the offering. Again, at this time there are no precedents to which we can refer for additional guidance.

Multijurisdictional Issues

It is possible that a New Generation Co-operative will wish to raise capital in more than one province, for a variety of reasons. In these scenarios, it is important that careful consideration be given as to which legislation the offering will be filed under in Saskatchewan. If the same prospectus is to be filed in other provinces, it will be reviewed under securities legislation in those provinces. There are co-ordinated mutual reliance review systems for reviewing offerings filed in more than one province, provided that the offering is filed under securities legislation in all provinces. This type of co-ordinated review is not possible if it is filed in Saskatchewan under the *New Gen Act*, but filed elsewhere under the securities legislation of the other provinces. This will create a significant problem for the review of the securities filing. We encourage discussion of this issue with the officers of the New Generation Co-operative well in advance of filing a prospectus. Contact the Deputy Director, Corporate Finance, at (306) 787-5867.

General Ruling Order 31—902
Saskatchewan Small Business Securities Issuer

If your NGC does not fit the criteria for the exemptions above, this general ruling order can be used to relax the registration requirements of the *Securities Act* where the directors, officers, or others will be selling the securities, and the NGC meets the following criteria:

- a. is incorporated, continued, organized, or established pursuant to the laws of the Province of Saskatchewan;
- b. has its registered office and head office located in Saskatchewan;
- c. carries on a substantial part of its businesses in Saskatchewan, in that 75 percent of its business assets are or will be located in Saskatchewan, and 75 percent of its expenses will be incurred in Saskatchewan;
- d. is controlled by residents of Saskatchewan, in that 75 percent of its voting securities are held by residents of Saskatchewan; and
- e. two-thirds of its promoters and directors are residents of Saskatchewan.

While this General Ruling Order relaxes the registration requirements for the NGC, it would still require the use of a prospectus to issue the securities. For complete information on this exemption, refer to the Saskatchewan Small Business Securities Issuer Package that is available by contacting the Saskatchewan Securities Commission at (306) 787-5876 (Registration Branch) and on the Saskatchewan Securities Commission's web site at www.ssc.gov.sk.ca

The Secondary Trade¹

Dean Murrison
Saskatchewan Securities Commission

Introduction

This paper builds on the paper “New Generation Co-operatives: Key Steps Relating to the Issuance of Securities” (the Primary Trade Paper), which describes the process for a **primary trade** of securities of a New Generation Co-operative (NGC). A primary trade is a sale of securities of an NGC by the NGC from its treasury to investors.

A **secondary trade** is a sale of securities of the NGC by the holders of those securities (having acquired the securities from the NGC under a primary trade). This paper discusses if and how a holder of securities in an NGC, having purchased securities from an NGC, can resell them. An additional term of note is that, if there is a market for the securities of an NGC, organized (like an exchange such as the Canadian Ventures Exchange (CDNX) or not organized (like sales directly between individual holders of the securities of the NGC), those sales are referred to as being made in the **secondary market**.

¹ This paper does not necessarily represent the views of the Saskatchewan Securities Commission, nor does it constitute a legal opinion. Readers are advised to seek professional legal advice before proceeding.

Background

The first thing to note is that securities of an NGC are securities within the meaning of *The Securities Act, 1988* (hereinafter the *Securities Act*). But for the provisions of *The New Generation Co-operative Act* (hereinafter *New Gen Act*), a trade or sale of securities of an NGC, whether it be a primary trade or a secondary trade, would be subject to the *Securities Act*.

The *New Gen Act* contains a waiver or exemption provision that says the *Securities Act* does not apply to a primary trade of securities of an NGC (although the NGC can elect to move its offering of securities or primary trade back under the provisions of the *Securities Act* if it wishes, or the Co-operative Securities Board (CSB) can direct that such offering be subject to the *Securities Act* if the CSB feels that it would be in the public interest to do so). There is no similar waiver or exemption provision in the *New Gen Act* for a secondary trade of securities of an NGC by a holder of those securities. In short, the secondary trades of securities of an NGC by the holders of those securities are subject to the *Securities Act*. This is true whether the primary trade with respect to the securities was carried out under the *New Gen Act* or the *Securities Act*.

When considering the application of the *Securities Act* to a disposition of a security like a security of an NGC (whether a primary trade or secondary trade), there are always two questions to consider. The first question is, Is the disposition of the security a **trade** within the meaning of the *Securities Act*? This generally means, is the disposition a sale or other disposition for valuable consideration? If the disposition is a trade, the person or company selling the security, whether it be a primary trade or secondary trade, must:

- be registered under the *Securities Act* to do the trade;
- find a statutory registration waiver or exemption in the *Securities Act* from the requirement to be registered under the *Securities Act* to do the trade; or

- apply for and obtain from the Saskatchewan Securities Commission (SSC) a discretionary registration waiver or exemption from the requirement to be registered under the *Securities Act* to do the trade.

The second question to be considered if the disposition of the security is a trade under the *Securities Act* is, Is the trade a **distribution** within the meaning of the *Securities Act*? This generally means, is the disposition a sale or other disposition for valuable consideration—

- from the treasury of the issuer of the securities (in other words, a primary trade); or
- from the holdings of a control person, promoter, incorporator, organizer, or underwriter of the issuer of the security (most are terms defined in the *Securities Act*) or from the holdings of persons or companies who acquired their securities under a statutory prospectus waiver or exemption in the *Securities Act* (see discussion of statutory prospectus waivers or exemptions below), in other words certain types of secondary trades.

A distribution does not include a disposition of a security by a person or company that acquired the security in an offering where the person or company received a prospectus under the *Securities Act* when they acquired the security as long the person or company is not a control person, promoter, incorporator, organizer, or underwriter of the issuer of the security.

If the disposition is a distribution, the person or company selling the security, whether it be a primary trade or the type of secondary trade discussed above, must:

- prepare and provide the purchaser of the security with a prospectus approved under the *Securities Act* to do the trade;
- find a statutory prospectus waiver or exemption in the *Securities Act* from the requirement to prepare and provide the purchaser of the security with a prospectus approved under the *Securities Act* to do the trade; or
- apply for and obtain from the SSC a discretionary prospectus waiver or exemption from the requirement to prepare and provide the purchaser of the security with a prospectus approved under the *Securities Act* to do the trade.

An additional matter to be considered when working with the *Securities Act* is that the use of a statutory prospectus waiver or exemption in the *Act* to sell a security triggers **resale restrictions** with respect to that security under the *Act*. Resale restrictions are restrictions on the purchasers of the security's ability to resell the security. These resale restrictions (sometimes referred to as **hold periods**) are generally indefinite unless the purchaser can find a statutory prospectus waiver or exemption in the *Securities Act* to sell the security, or the issuer of the security is or becomes a **reporting issuer** within the meaning of the *Act* (usually by filing a prospectus under the *Securities Act*). Resale restrictions are also usually imposed by the SSC in any discretionary prospectus waiver or exemption granted by the SSC with respect to an offering of securities. Resale restrictions under the *Securities Act* are not triggered by trades of securities under the *New Gen Act*.

For more information on the workings of the *Securities Act*, the waivers or exemptions, and the resale restrictions discussed above, consult "How to Raise Capital Using Exemptions," prepared by the SSC. This paper is available online at www.ssc.gov.sk.ca or by calling the SSC at (306) 787-5299.

The *New Generation Co-operative Act* works differently from the *Securities Act*. The *New Gen Act* does not contain registration or prospectus requirements similar to those discussed above under the *Securities Act*. Nor does it contain resale restrictions (although, as noted earlier, the resale of securities of an NGC—that is, a secondary trade of securities of an NGC—is subject to the *Securities Act*).

As noted in the Primary Trade Paper, the *New Gen Act* provides that, with respect to a primary trade of securities of an NGC, the *Securities Act* does not apply unless the NGC chooses that it should apply, or the CSB directs that it should apply. If the *Securities Act* does not apply (if it did apply, the requirements discussed above would be triggered), an NGC must file with the CSB the information the CSB requires with respect to the primary trade and receive the approval of the CSB to do the trade. This is unless the NGC can fit itself within one of the waivers or exemptions from

these requirements in the *New Gen Act* or the regulations to that statute or has obtained a discretionary waiver or exemption from these requirements from the CSB. If the approval of the CSB is required, the approval may contain such terms and conditions as the CSB feels are suitable, a common one being that the NGC prepare and provide to the purchaser of the security a prospectus similar to that which would be required under the *Securities Act*. To date, it has been rare for the CSB to grant a discretionary waiver or exemption from the requirements of the *New Gen Act*.

For more discussion of the workings of the *New Generation Co-operatives Act* with respect to a primary trade of securities of an NGC, consult the Primary Trade Paper.

The Secondary Trade

As noted above and in the Primary Trade Paper, a holder of securities of an NGC could have obtained their securities by one of the following methods:

- *Method 1*—by way of a prospectus offering under the *Securities Act*;
- *Method 2*—by way of an offering approved by the CSB, which approval has to date often included the requirement to use a prospectus similar to that which would be required under the *Securities Act*;
- *Method 3*—by way of statutory registration and prospectus waivers or exemptions contained in the *Securities Act*;
- *Method 4*—by way of statutory waivers or exemptions contained in the *New Gen Act*;
- *Method 5*—by way of a discretionary waiver or exemption applied for and granted by the SSC; or
- *Method 6*—by way of a discretionary waiver or exemption applied for and granted by the CSB, which, to date, have been rarely granted.

Regardless of the method by which the securities were acquired, the *Securities Act* applies to the secondary trade of the securities, although how the *Act* applies varies somewhat depending on the method used to acquire the securities. In considering the application of the *Securities Act* to a disposition of securities of an NGC, consider the two questions discussed above.

Registration (Is the Disposition a Trade?)

Assuming the disposition is a sale or other disposition for valuable consideration, as opposed to a gift, which is not trade, it is a trade under the *Securities Act* no matter which method was used to acquire the security. As a trade, unless you are registered to sell securities, can find a statutory registration waiver or exemption in the *Securities Act* to sell the security, or have obtained a discretionary waiver or exemption from the SSC to sell the security, you cannot sell the security. You must continue to hold it.

For a discussion of statutory and discretionary waivers or exemptions please consult “How to Raise Capital Using Exemptions,” prepared by the SSC. This paper is available online at www.ssc.gov.sk.ca or by calling the SSC at (306) 787-5299.

A statutory registration waiver or exemption in the *Securities Act* that might be helpful in some circumstances would be the isolated trade statutory registration waiver or exemption (the corresponding isolated trade statutory prospectus waiver or exemption differs from the statutory registration waiver or exemption and will be less helpful in the context of a prospectus).

There is also a statutory registration waiver or exemption in the *Securities Act* that allows for trades through a registrant under the *Act*. This may not be useful in the initial stages of development of an NGC, but should an NGC grow to a size where a registered dealer under the *Securities Act* runs an over-the-counter market for the securities of the NGC, or the securities of the NGC are listed on an exchange like the CDNX, this may provide a method for a holder of the securities of the NGC to sell them. This is not discussed in the above paper, but the provision can be found in clause 39(1)(j) of the *Securities Act*. In such cases, the holders of the securities would be holding freely tradable securities.

Prospectus (Is the Disposition a Distribution?)

Assuming the disposition is a trade, the next question is, Is the trade a distribution? If it is, then the sale of the securities of an NGC will be subject to resale restrictions under the *Securities Act*. Only the use of a statutory prospectus waiver or exemption in the *Act* to trade securities will trigger resale restriction under the *Act* on those securities in the hands of the purchaser of those securities. Whether the sale is a distribution depends on the method under which the securities were acquired. Should you find that your sale would not be a distribution under the *Securities Act*, you are holding **freely tradable securities** in the prospectus context, **although you still need to consider the registration requirements discussed above.**

Method 1—If you acquired the securities under this method, unless you are a control person, promoter, incorporator, organizer, or underwriter of the issuer of the security, the disposition will not be a distribution, and the securities you hold are freely tradable.

Method 2—If you acquired the securities under this method, unless you are a control person, promoter, incorporator, organizer, or underwriter of the issuer of the security, the disposition will not be a distribution, and the securities you hold are freely tradable.

Method 3—If you acquired the securities under this method the securities you hold are subject to the resale restrictions set out in the *Securities Act*. Consult “How to Raise Capital Using Exemptions,” available online at www.ssc.gov.sk.ca or by calling the SSC at (306) 787-5299. You may be subject to additional requirements if you are a control person, promoter, incorporator, organizer, or underwriter of the issuer of the security.

Method 4—If you acquired the securities under this method, unless you are a control person, promoter, incorporator, organizer, or underwriter of the issuer

of the security, the disposition will not be a distribution, and the securities you hold are freely tradable.

Method 5—If you acquired the securities under this method, the securities you hold are subject to whatever resale restrictions the SSC imposed on you in the waiver or exemption it granted with respect to the trade of the securities to you. You may be subject to additional requirements if you are a control person, promoter, incorporator, organizer, or underwriter of the issuer of the security.

Method 6—If you acquired the securities under this method, the securities you hold are subject to whatever resale restrictions the CSB imposed on you in the waiver or exemption it granted with respect to the trade of the securities to you. You may be subject to additional requirements if you are a control person, promoter, incorporator, organizer, or underwriter of the issuer of the security.

Trades of securities of an NGC by a control person, promoter, incorporator, organizer, or underwriter of the NGC will always be a distribution under the *Securities Act*.

In addition to the application of the *Securities Act*, you should always consider:

- the *New Gen Act*, which may contain provisions that affect a sale of the securities of an NGC; and
- the articles and by-laws of the NGC, which may contain additional restrictions on the sale of the securities of an NGC.

The Market-Making Mechanism

It may be that an NGC has grown to a size where it has a large number of freely tradable securities outstanding held by a large number of security holders, but there is no registered dealer under the *Securities Act* running an over-the-counter market for the securities of the NGC, and the securities of the NGC are not listed on an

exchange like the CDNX. In this situation, an NGC may consider running its own market-making mechanism to provide liquidity to its security holders.

The market-making mechanism is a means whereby an NGC can create a secondary market for its securities. It does not provide a way for holders of its securities to avoid the resale restrictions discussed above; it just provides them with a place to go to find someone to buy them.

An issuer usually conducts a market-making mechanism by:

- constructing and regularly maintaining a list of all persons who would like to buy or sell the securities of the issuer;
- ensuring that all persons have an equal opportunity to put their name on the list as a buyer or a seller;
- ensuring that the list is publicly available;
- ensuring that the same corporate and financial information about the issuer is equally available to all persons on the list so that everyone involved in the process is on a level playing field;
- ensuring that historical sale prices for its securities are equally available to all persons on the list, to ensure transparency in the process;
- providing no investment advice to those involved in the process;
- not soliciting any person's involvement in the process;
- only carrying out activities of a purely administrative nature in the process; and
- since the process is a service to its security holders, charging no fee for participation in the process.

Under the *Securities Act*, this activity by an issuer of securities requires the issuer to become registered under the *Act* to carry it out or obtain from the SSC a discretionary waiver or exemption of the registration requirement in the *Act*. A number of issuers have obtained such a waiver or exemption, and the SSC instituted General Ruling/Order 45-903 for Community Bond Corporations to carry out this activity. The SSC will shortly institute a General Ruling/Order to allow all issuers to carry out these activities.

Because the *New Generation Co-operatives Act* provides that the *Securities Act* does not apply to trades by an NGC of its own securities, these activities by an NGC, as long as it deals only with its own securities and does not provide any investment advice (which is a registrable activity under the *Securities Act* not exempted under the *New Gen Act*), are not subject to the *Securities Act*, and no registration or discretionary waiver or exemption from the registration requirement in the *Act* is needed from the SSC.

Although it may not be clear, it appears by the wording of the *New Gen Act* that the approval of the CSB or a discretionary waiver of exemption from the CSB would be necessary for an NGC to carry out these activities, unless the NGC chooses or the CSB directs that the trades be subject to the *Securities Act*. Once the SSC has its General Ruling/Order in place for these activities for all issuers (which will occur shortly), this may be a reasonable course of action. As far as the writer is aware, the CSB has not yet considered this issue.

A Note on the Strategic Alliances

Centre for the Study of Co-operatives
University of Saskatchewan

When a producer group is thinking about forming a New Generation Co-operative (NGC), they may encounter several problems. One problem is that a producer group often lacks sufficient resources to form a successful value-added processing facility on its own. A second problem is lack of expertise, such as processing or marketing, which are necessary for value-added activities.

The purpose of this article is to discuss the ways in which a producer group can address the problems of lack of capital and lack of expertise. The first section discusses two ways that an NGC can access outside capital. The second section suggests how a strategic alliance may alleviate the lack of expertise as well as capital.

Outside Investment

One way for an NGC to address the issue of access to capital is by inviting outside investment. This can happen through the sale of preferred shares or by investment directly at the producer level.

Preferred Shares

The Saskatchewan *New Generation Co-operatives Act* allows nonmembers to purchase preferred shares in an NGC. The investment in preferred shares and investment by members in equity shares represents the total equity in an NGC (described in Figure 1). Preferred shares may be issued to members or nonmembers. An NGC may offer several classes of preferred shares, all of which carry no par value. The formula for determining the value of no-par value shares is described in the organization's Articles of Incorporation.

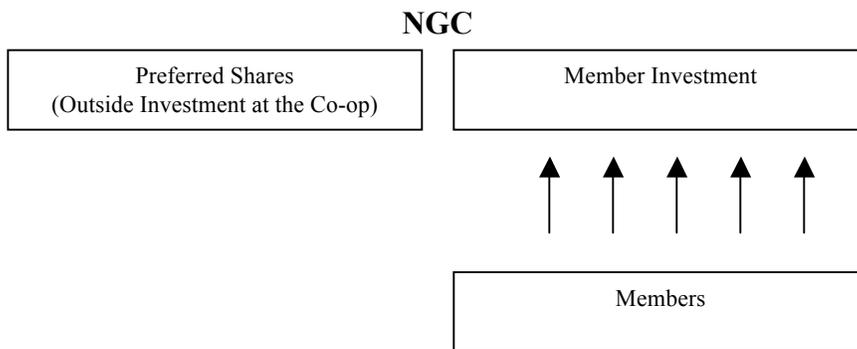


Figure 1: An NGC with Investment by Preferred Shareholders

Holders of preferred shares may be entitled to elect up to 20 percent of the NGC directors. If the class of preferred shares has voting rights then any one shareholder can hold up to 10 percent of the total preferred shares. This may be a problem if members are unwilling to forgo some control to nonmembers. It is possible to structure a class of preferred shares with no voting rights. If the class of preferred shares does not have voting rights, then any one shareholder can hold up to 25 percent of the total preferred shares. However, this also causes a problem—would people be willing to invest without control?

A second challenge with preferred shares is determining the rate of return. The rate of return can be fixed or it can be tied to the profitability of the co-op. If the rate of return is fixed, then the preferred shareholders have no incentive to influence the

business of the co-op. This may be good if the co-op management is successful and does not need to be monitored. However, if management is poor, then the co-op may benefit from pressure by preferred shareholders to improve performance. Moreover, investors may not want to invest if the fixed rate of return is too low.

If the rate of return is tied to the profitability of the co-op (a fluctuating rate of return), then preferred shareholders have an incentive to encourage the co-op to maximize its profits and therefore maximize the return to preferred shareholders. While members can benefit from the co-op's profitability (through patronage dividends), the benefit may come at their own expense, at times, if the co-op raises profits by offering a lower product price.

This tension between the goals of the shareholders and the producers can be a significant problem in situations where preferred shareholders earn a return based on profitability. This can lead to demands by the preferred shareholders for greater control and transformation of the co-op to an investor-owned and -controlled firm.

Investment at the Producer Level

A second way to access outside capital is for investment to occur at the producer level. The nature of the agreement between a member and an investor would be determined by the two parties, independent of the co-op and other members. The advantage of this arrangement is that the interests of the investor and the member are aligned—if the member is profitable, the investor also benefits. Investing at the producer level is a way of bringing in capital without creating the tension outlined above. Figure 2 (next page) illustrates this type of arrangement.

Strategic Alliances

Producers tend to be experts in production, but they may lack the expertise to process and market their product. One way an NGC can access necessary resources is by forming a strategic alliance with a partner firm or firms. A strategic alliance is an association between people or organizations that provides mutual benefits to both

parties. The benefits of a strategic alliance may include access to capital, excess processing capacity, processing expertise, or access to existing markets.

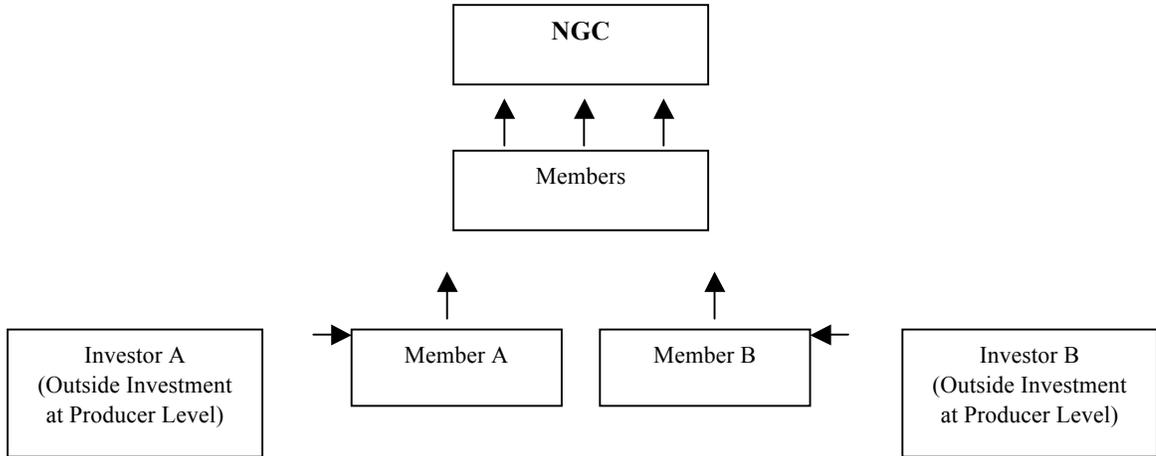


Figure 2: Outside Investment at the Producer Level

Before forming a strategic alliance, it is desirable for producers to organize as an NGC. Collectively, as an NGC, producers have more bargaining power in the alliance than they would individually. It is also desirable for the partner firm that the producer group forms an NGC. An alliance with an NGC eliminates the processor’s need for individual contracts with each producer. The delivery contract is built into the NGC’s By-Laws of Incorporation. By-laws are not easily renegotiated. This means that the delivery contracts with producers in an NGC are more enforceable than individual delivery contracts would be. Aligning with an NGC group, therefore, would mean that the processor is more likely to receive the quantity and quality of product agreed to.

There are a variety of ways an NGC might structure a strategic alliance. One way is for an NGC to invest in an existing business. A second way is for an NGC to partner with another firm or firms to form a new business entity.

NGC Investment in an Existing Processor

It may be desirable for an NGC to partner with an existing processor or other type of business. This type of arrangement enables the NGC to process its product and the processor to fill excess processing capacity and/or to access capital. This type of arrangement is illustrated in Figure 3.

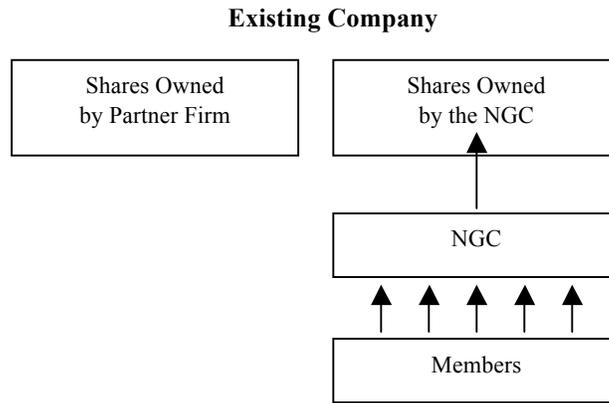


Figure 3: Alliance between NGC Producer Group and an Existing Company

The number of shares owned by the NGC may reflect the processor's excess processing capacity. One example of this type of strategic alliance is the relationship between US Premium Beef and Farmland National Beef Packing Company.

Example: US Premium Beef and Farmland National Beef Packing Company

Farmland National Beef Packing Company is the fourth largest processor of beef in the United States, and is a subsidiary of Farmland Industries. US Premium Beef (USPB) is a co-operative representing producers in all segments of the beef industry.

USPB and Farmland National Beef Packing Company formed an alliance in 1997, when USPB purchased an undisclosed number of shares in Farmland National Beef

Packing Company. USPB formed the alliance to avoid the high costs of building a new plant. USPB wanted to have equity ownership interest and equal control with its partner. This would allow USPB to develop its own ideas while protecting its shareholders' interests.

Farmland National Beef Packing Company was one of several processors eager to form an alliance with USPB, which could fill the packer's excess processing capacity and offer an assured supply of high quality beef.

New Business Entity

A second way of constructing a strategic alliance is to form a new business entity, such as a corporation. An NGC may partner with a firm or firms that offer such things as financial support, marketing or manufacturing expertise, or established markets. Figure 4 illustrates a new corporation formed from an alliance between an NGC, a processing firm, and a marketing firm. As a corporation, the profits generated by the new business entity would be allocated to the NGC and the partner firms in proportion to investment. Trilogy Ltd. is one example of this type of alliance.

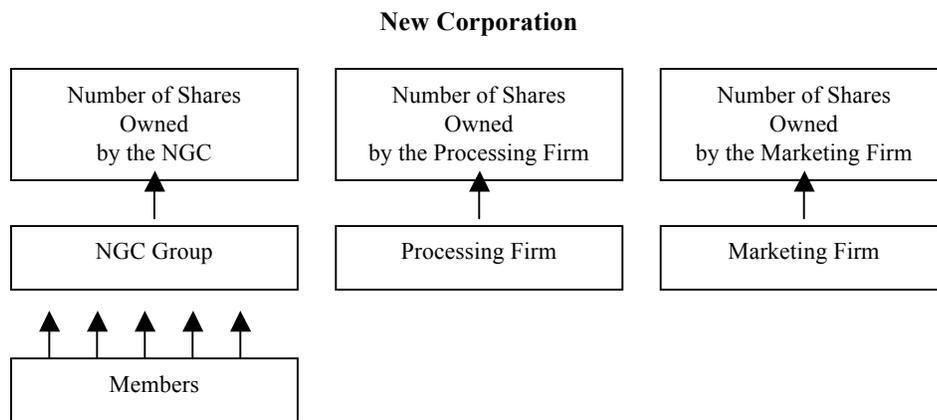


Figure 4: Alliance between NGC Producer Group and Expertise Groups

Example: Trilogy Ltd.

Trilogy Ltd. is a Manitoba-based company that is preparing to produce egg products such as extended shelf-life liquid eggs, precooked egg patties, omelettes, and egg substitutes for the Canadian market. This new organization is the result of a strategic alliance between the Manitoba Egg Producers Co-op (an NGC), Michael Foods, and Canadian Inovatech. Each firm invested one-third of the cost of developing Trilogy.

The Manitoba Egg Producers Co-op Ltd. is an NGC owned by 115 egg producers in Manitoba. The co-op offers a consistent supply of quality eggs to Trilogy. Canadian Inovatech, Canada's largest processor of egg products, will break the eggs at its Winnipeg plant and process them in an adjacent plant. Michael Foods is a food processor from Minnesota with access to established markets for processed egg products.

Trilogy offers mutual benefits to each party. For the Manitoba Egg Producers, partnership with Canadian Inovatech and Michael Foods creates a chance to share the risks and benefits of processing and adding value to their product

A Note on the Multiple-String Structure

Centre for the Study of Co-operatives
University of Saskatchewan

Traditionally, co-operatives have been formed by a relatively homogeneous group of producers to meet a common set of needs. With a homogeneous group of members, a co-op can provide relevant services and clear benefits to its members. As the co-op matures, however, its membership often becomes more heterogeneous and its members' needs more diverse. The co-op may diversify into a broad range of activities in an attempt to meet the needs of a heterogeneous membership.

On the other hand, co-ops that offer too broad a range of services often struggle to make a clear link between the needs of members and the benefit of membership. Profits from one activity may subsidize a less profitable activity. As a result, all members will pay for a certain service that only a few will use. This leads to a situation where the benefits of membership in the co-op are unclear to its members. If the co-op fails to provide clear benefits, members may have no reason to use the co-op and commitment falls.

The purpose of this article is to explore how the application of the multiple-string or umbrella structures can help co-ops avoid or mitigate the problem of cross-subsidi-

zation. In a multiple-string co-op, each product or service line represents one of a number of multiple *strings*, or activities, within the co-op. The co-op may also offer common or umbrella services—such as processing, transportation, or marketing—to each product line. Each product or service line uses some combination of the co-op’s services to meet its needs. One way to clarify the link between services and benefits is to organize each product line as a New Generation Co-operative (NGC).

This paper describes four examples of multiple-string co-ops. The first is a case in which a traditional co-operative evolved to employ an umbrella structure. The second illustrates a case in which co-operatives were created anew using the umbrella structure. The third example describes a proposed venture that would have seen a traditional co-op evolve into a multiple-string structure composed of “finger” NGCs. The final example is a hypothetical model that could be applied to emerging NGCs.

Danish Crown

Danish Crown, the largest pork processing and slaughtering company in the European Union, is an example of a traditional co-op with a multiple-string structure. This organization separates its pig slaughter into heavy pigs, UK pigs, and various types of pigs for the Danish market.

Members of Danish Crown understand that there is a clear mechanism to account for the revenues received from each type of pig. A member can expect to receive the total benefits from the type of pig he or she delivers; there is no cross-subsidization between different types of pigs. Danish Crown pays a premium based on the farm-level costs of production. In some cases, the premium is a means of encouraging producers to move from one type of pig production to another. For example, Danish Crown offers a premium or subsidy to farmers who convert to raising organic pigs.

CUMA Co-operatives

The Coopérative d’Utilisation de Matériel Agricole (CUMA) Co-op is a type of farm

machinery co-op being adopted in Québec. CUMAs enable producers to buy and maintain farm machinery co-operatively. The CUMA owns the equipment and rents it to members at the lowest possible cost.

A CUMA is composed of activity branches that correspond to individual pieces of farm machinery. A member can join one or more branches; the costs associated with one branch are separate from all other costs. Therefore, a member of one activity branch knows that the cost she or he pays entirely supports that piece of machinery.

Figure 1 outlines a CUMA that offers spraying, seeding, and raking services. Member 1 belongs to each of the NGCs, Member 2 belongs to two, and the rest of the members each belong to one activity.

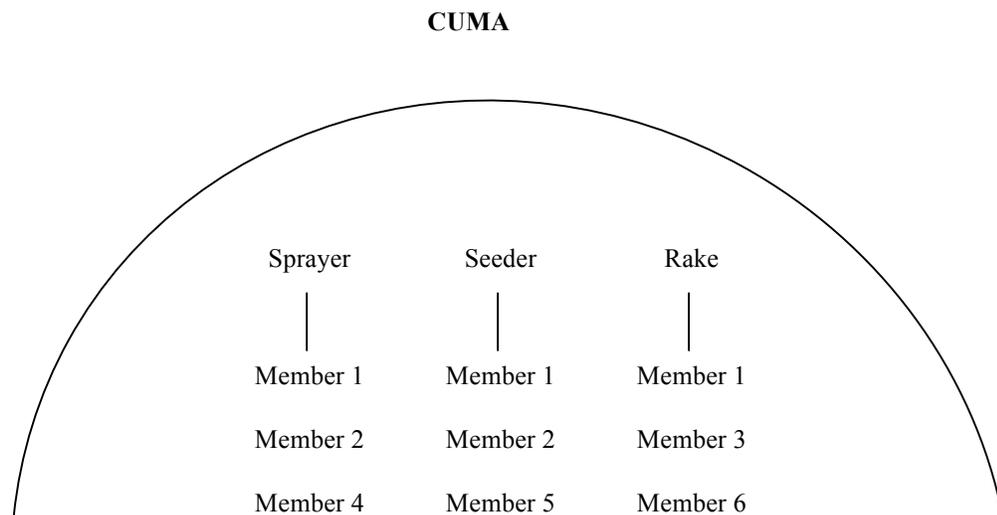


Figure 1: A CUMA Co-operative

United Country Brands

United Country Brands was to be the outcome of a proposed merger between two large, farmer-owned co-operatives—Cenex Harvest States and Farmland Industries. United Country Brands was going to be an umbrella co-op for eleven to fifteen individual organizations, or “fingers.” It was proposed that each finger would be a New Generation Co-op. Members could choose to invest and do business with one or more finger NGCs. In each finger NGC, members would invest an amount proportional to their intended use. By organizing the fingers as NGCs, the co-op would have relied on member equity for financing.

A Model for Emerging Co-ops

The multiple-string structure may be useful for a group of producers who share a number of common needs. Emerging co-ops represent one situation in which a large number of producers may have common needs.

Figure 2 (next page) outlines a hypothetical example of a multiple-string fruit and vegetable co-op composed of three finger NGCs. The co-op markets three crops: cantaloupe, cabbage, and carrots. It offers marketing, transportation, processing, and cleaning services to all product groups. However, each product group has unique needs in terms of transportation, processing, and cleaning services. Cantaloupes require transportation; cabbages require cleaning, processing, and transportation; and carrots require cleaning and transportation.

Producers become members of one or more product groups according to the type of production in which they are engaged. As NGCs, each producer group requires its members to invest in the co-op in proportion to the amount of product they deliver.

Multiple-String Fruit and Vegetable Co-op

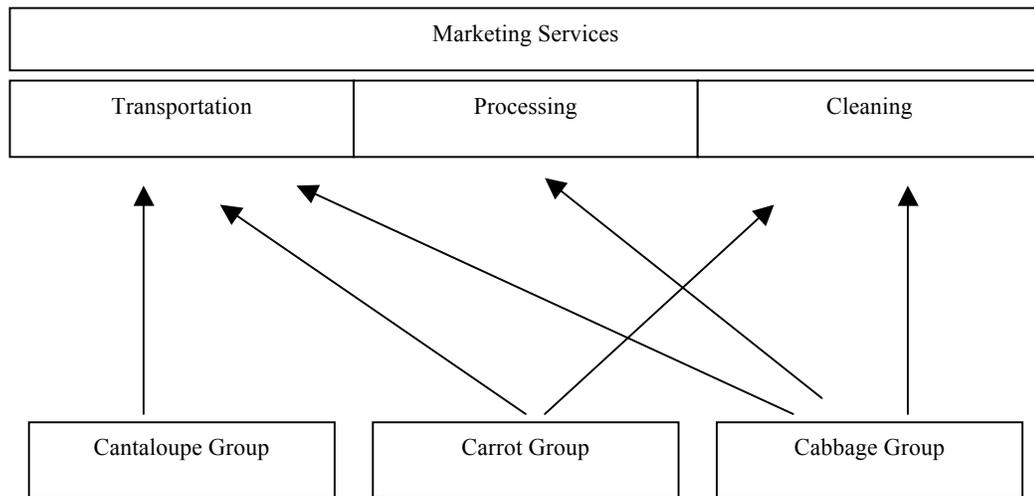


Figure 2: A Multiple-String Field Fruit and Vegetable Co-op

The costs associated with services for each group are allocated exactly to that group. In this way, each member of a product group knows that she or he is paying only for the services that are used for that particular product. No member is concerned that she or he is paying for services rendered to another group. A member of the cantaloupe group, for example, knows that the price she or he pays for transportation services is not higher or lower due to cross-subsidization among the producer groups.

This example of a multiple-string structure shows how a co-op can offer a range of services to groups with both different and common needs. At the same time, the NGC producer groups allow the co-op to provide clear benefits to its members.

Marketing Contracts

The Supply Contracts between Members and the Co-operative

James H. Gillis
Stevenson, Gillis, Hjelte, and Tangjerd

Introduction

The economic power of the New Generation Co-operative is its ability to provide value-added processing and marketing to the commodities supplied by its members, and to direct the financial benefit of these activities back to the members. In some cases, the members' products will be differentiated (or specialized) in some way from similar commodities sold on the open market, giving them a higher raw value when used in the co-operative's finished product than they would have in any other use. In other cases, the value added by the co-operative is a result of the technology possessed by the co-op or the skills and knowledge applied by the members. The patronage dividends from the co-operative's value-added activity, combined with the enhanced price reflecting the commodity's specialized value (where applicable), provide the members the return needed for their investment in setting up the co-operative and (where applicable) specializing their commodities.

The two legal relationships with the co-operative of economic value to its members are (1) their memberships, and (2) their marketing contracts with the co-operative.

The co-operative can function only if its members commit to providing it with a reliable supply of the commodity sufficient to meet its quality, quantity, and timing requirements. The marketing contract is the legal tool that secures this commitment.

The main difference between the marketing contract and a regular contract is that since the marketing contract comes automatically with membership in the co-operative, each party has a built-in interest in the success of the other. While the marketing contract deals primarily with the arm's length part of the relationship, it has features that one would not expect to see in a contract with an unrelated third party. For example, some marketing contracts will contain terms allowing the co-operative to unilaterally change certain terms from time to time to give it the flexibility it needs. Members are expected, within reason, to accept and work with these changes for the good of the organization. The degree of give and take required in some marketing contracts could not operate effectively in contracts where the parties function strictly at arm's length.

The purpose of this paper is to give some guidance to organizers of New Generation Co-operatives in designing their marketing contracts. As the business of every co-operative (and the way it does its business) is unique, there is no one format that will fit all co-operatives. This paper will identify the things that need to be covered in the marketing contract, and will show by example how particular issues affecting the business of a co-operative can be addressed.

Marketing Contracts—How Big? How Many? How Often?

In developing a general format for the marketing contract, the author has tried to combine the principle that simpler is better with the idea that the marketing contract should be a thorough, meaningful working document for guidance and clarification.

Some of the terms of the contract will be unique to each member, while others will be the same for all. Some will remain constant over time, while others will change periodically. Of the changeable terms, some will be reviewed on an annual or cyc-

lical basis, while others will change on an irregular basis. The draft format attempts to minimize the number and frequency of contract documents, allowing as far as possible for a single document to cover years of dealings between the member and the co-operative, accommodating numerous transactions occurring under a variety of terms and conditions. Where periodic changes or fresh arrangements need to be documented, there has been an attempt to keep the amending document short and simple, while preserving its legally binding effect.

With these features in mind, the author has devised the following three documents, which are intended to work together to cover all the contractual aspects of the purchase/supply relationship between the member and the co-operative:

- The *Marketing Agreement* is a standard-form document that the co-operative enters with every member. It will be the same for everyone, and is not intended to change over time. It contains all the general rights and obligations of each side, and governs how the other two documents below operate in the overall context of the contract.
- The *Quality Standards and Management Practices Schedule* (Appendix A to the Marketing Agreement) is also a standard form applying to all members, but created with the intent that it will be modified from time to time to reflect better practices, new standards, technological innovations, or other changes required by the co-operative to sustain its competitive position. The Marketing Agreement will stipulate that the co-operative can “reasonably and in good faith” change the terms of the Schedule as may be required from time to time, and that the members agree in advance to such changes being made.
- The *Delivery Notice* is the document issued by the co-operative to individual members. Each one contains information specific to the member to whom it is directed, specifying the prices, quantities, and delivery schedule for that member for the production period covered in the Notice. The Notice will establish a specific contract between member and co-operative for that production period, with

the detail as stated in the Notice and the general terms as stated in the Marketing Agreement, as modified in the Schedule.

The author has resisted the temptation to provide a fill-in-the-blanks-model marketing contract, and has chosen instead a fictitious sample, so that the reader can better see how to address the issues that must be dealt with in any real-life situation.

Please note that the sample is in no way intended to recommend any business content, or to reflect any technical or commercial realities of such an operation, but merely to show a workable format in which those things can be addressed in the contract documents.

Real-life situations may be either more or less complex than the sample provided. In some cases, other Schedules may also be included, such as, for example, the contract between the co-operative and the purchaser of the finished product, which may contain pricing or other terms that impact on the members' contracts. If the commodity being supplied by the members is generic, it may be unnecessary to include any schedules or other stipulations as to methods or quality of production.

Readers should keep this note of caution in mind when reviewing the following guide to the sample.

The Recitals

To provide a contextual understanding of the contractual relationship created in the Marketing Agreement, it is important to say something of a general nature about the type of activity that the co-operative will be undertaking, the roles of the participants, and the overall objectives of the business venture. The sample gives an example of how to do this.

Terminology

While it may seem overly legalistic to begin an agreement with definitions, it is useful to define key concepts in order to maintain precision and consistency throughout the document. The idea of “Delivery Obligations,” for example, is central to the sample contract because of the co-operative’s need to be able to enforce them. The enforcement provision in Section 13.1 is clear and straightforward because the defined term is used there and in every other relevant part of the document.

The drafters of any real-life contract should identify the ideas that are key to their business relationships, develop careful and complete descriptions of these ideas, and have them appear first in the contract as definitions, with the defined terms then used in every other place in the document where they need to be addressed. Some of the defined terms in the sample, such as “Quota,” will be useful in most real-life situations, while others in the sample may not. As a rule, a term should not be defined unless it encompasses a fairly specific idea and will be used at least twice in the body of the document.

Drafters should consider introducing the idea and definition of “Rules” into their contracts, as the sample does. This allows the co-operative some flexibility to control the quality of the product it receives from its members.

Using the Delivery Notice as a feature and defined term of the Marketing Contract is also recommended. This allows the co-operative to create future legally binding delivery obligations without the need of entering into further agreements with the member. The recommended form of Delivery Notice provides for signature and return by the member, but this is for acknowledgment purposes only. The delivery obligation exists whether or not the member signs or accepts it.

Obligations of the Member and the Co-operative

The details of such obligations will be specific to the co-operative's business. The key things to be included for the member, however, are:

- a clear and specific statement of his/her delivery obligations (see 2.1 of the sample); and
- warranties as to quality, tying these to the Rules and Delivery Notices if these are used (see 2.3 of the sample).

The key things to be included for the co-operative are statements of its obligation:

- to adequately perform the service it undertakes for its members (see 3.1, 3.2, 3.4, and 3.5 of the sample);
- to accommodate all members fairly in their deliveries (see 3.3 of the sample); and
- to pay the members for their deliveries in a well-defined way (see 3.6 and 4 of the sample).

Price and Payment

The method of calculating the payments due to the members, and the terms of payment, should be specified (see 4 of the sample).

Duration and Termination Provisions

The provisions in the sample (Sections 5 and 6) are fairly common-sense and will likely be directly usable in any real-life marketing contract. It is important to include them, as failure to do so will leave scope for great difficulty in the event of a dispute with a member.

Other Documents Being Part of the Agreement

It is particularly important in the co-operative/member relationship to ensure that the mutual duties and responsibilities of both parties under the Articles and By-Laws are

also contractual duties owed to one another in their business dealings. A provision such as 7.1 is thus recommended.

If Rules and Delivery Notices are features of the Marketing Contract, then terms such as 7.2 and 7.3 are necessary to ensure that they remain contractually binding over time.

Default and Remedies

The ideas behind these provisions are recommended for all co-operative situations.

Dispute Resolution

Sections 15 and 16 of the draft provide for arbitration, a form of ADR (alternate dispute resolution), for day-to-day disputes that may arise between the co-operative and a member. These will typically involve a member's failure to deliver as required, or the co-op's rejection of a delivery. Arbitration of these types of matters will in most cases provide a faster and more inexpensive resolution than if they were taken to court. If the drafters wish to provide for this method of ADR, they might also consider identifying a bank of arbitrators acceptable to all members to create confidence in the level of fairness and expertise that will be brought to bear if disputes of this nature arise.

If the Marketing Contract includes a provision such as Section 15, then court will not be an option for the kinds of disputes it covers. There will be some disputes, however, where access to the courts is necessary. A co-operative needs the right to get an injunction, for example, if a member is refusing to deliver. A member will need court intervention if the co-operative is behaving in an unfair or oppressive manner towards him/her on a matter other than day-to-day operation under the contract (e.g., if the co-operative changes the Rules in a way that is unfair to the member, or issues a Delivery Notice that places the member under a hardship not experienced by others). The sample exempts matters of this nature from the arbitration process (see Section 16).

General Terms

Please refer to the comments made above in relation to the Duration and Termination Provisions.

Final Comment

While the sample may be useful as a guide, and while some parts of it may be applied unchanged in a variety of situations, the drafters of each co-operative's marketing contract documents must carefully consider the nature of the business it is in and the specific needs and concerns of its participants. They must be ready and willing to customize these documents to meet those needs and concerns.

SAMPLE NGC MARKETING AGREEMENT

BETWEEN:

GRASSY MEADOW CATTLE FINISHING AND MARKETING CO-OPERATIVE LTD. (“the Co-operative”), a co-operative duly incorporated pursuant to the provisions of *The New Generation Co-operatives Act* of Saskatchewan (“the Act”)

AND:

_____, (“The Member”), a member of the Co-operative

RECITALS

The Co-operative is duly incorporated under the laws of the Province of Saskatchewan, and owns and operates a large scale feedlot (“the Feedlot”) in the R.M. of Dusty Plain No. 1234 in the Province of Saskatchewan.

The Member owns or rents land, corrals, barns, and related equipment sufficient to enable the Member to raise feeder cattle to be finished by the Co-operative, with ownership thereof to be retained by the Member until such cattle are finished and sold on the Member’s behalf by the Co-operative.

The Co-operative has the capacity to feed feeder cattle for its members, and has developed contacts and methods to market finished cattle for the benefit of its members.

This Agreement, together with the Articles, By-Laws, any reasonable policies of the Co-operative, and any schedules or other documents incorporated by reference into this Agreement, establishes the legal relations between the member and the Co-operative.

NOW THEREFORE IN CONSIDERATION of the mutual obligations undertaken in this Agreement, the Co-operative and the Member agree as follows:

TERMINOLOGY

- 1. The words and phrases identified in this Section will have the meanings ascribed to them as follows:
 - 1.1. “Animal” means a cow, bull, or calf;
 - 1.2. “Articles” means the Articles of Incorporation of the Co-operative, as they may be duly amended from time to time;

- 1.3. “By-Laws” means the By-Laws of the Co-operative, as they may be duly amended from time to time;
- 1.4. “Delivery Notice” means a notice issued by the Co-operative to the Member under the provisions of Section 7.3;
- 1.5. “Delivery Obligations” means the Member’s obligation to deliver cattle to the Co-operative as specified in Section 2.1, and as otherwise provided in this Agreement;
- 1.6. “Fiscal Quarter” means a period of three months in a Production Year commencing on April 1, July 1, October 1, or January 1 in that Year;
- 1.7. “Production Year” means a period commencing April 1 of a given calendar year and ending on the March 31 next following;
- 1.8. “Quota” means the number of Animals which the Member is required to deliver to the Co-operative in a Production Year as determined by the number of Member Right Shares held by the Member within the meaning of Section 35 of the Act;
- 1.9. “Rules” means the provisions in the Quality Standards and Management Practices Schedule annexed as Appendix “A” hereto, as the same may be amended from time to time as permitted in this Agreement;
- 1.10. “this Agreement” includes all the terms and conditions in this document, the Articles, the By-Laws, the Rules, any Delivery Notice issued by the Co-operative, and any other document which may now or hereafter be incorporated by reference into the dealings between the parties hereunder;

and wherever a Section number is identified herein without any other identifying reference, that Section is contained in this document.

OBLIGATIONS OF THE MEMBER

2. Throughout the term of this Agreement the Member shall:
 - 2.1. over the course of each Production Year deliver the Member’s Quota to the Feedlot, at his/her expense. The Member shall deliver all cattle in accordance with the schedule stipulated in the Delivery Notice for each Fiscal Quarter of that Production Year;
 - 2.2. maintain such staffing, land, pasture, buildings, feed, veterinary services, and equipment as are required to raise sufficient cattle to meet the Member’s Delivery Obligations on an ongoing basis;

- 2.3. provide the following warranties to the Co-operative in relation to all cattle delivered or to be delivered to the Co-operative under this Agreement:
 - 2.3.1. that such cattle are of merchantable quality;
 - 2.3.2. that the Member has used reasonable skill and judgment in selecting suitable cattle to deliver to the Co-operative;
 - 2.3.3. that such cattle conform to the quality standards set by the Co-operative from time to time as set forth in the Rules or specified in the applicable Delivery Notice;
- 2.4. manage and care for the Member's cattle, obtain necessary permits; maintain records relating to the Member's operation; manage waste and meet environmental and health requirements on the Member's facility; maintain insurance; and meet any other requirements as may be imposed in the Rules; and
- 2.5. permit representatives of the Co-operative to enter upon the lands comprising the Member's facility to inspect the Member's operation for the purpose of confirming that all terms, duties and obligations under this Agreement are being complied with.

OBLIGATIONS OF THE CO-OPERATIVE

3. Throughout the term of this Agreement the Co-operative shall:
 - 3.1. maintain such staffing, land, pasture, buildings, feed, veterinary services, and equipment as are required to custom feed and market cattle for its members;
 - 3.2. use its best efforts to secure, maintain and increase the market for finished cattle for the benefit of its members;
 - 3.3. accommodate and accept the Member's delivery of all cattle which the Member is required to deliver to the Co-operative under this Agreement, and which meet the warranties specified in Section 2.3, all in accordance with the delivery schedule stipulated in the current Delivery Notice. The delivery schedule in any Delivery Notice shall, insofar as possible, accommodate reasonable ongoing availability of space at the Feedlot for cattle being delivered by all members, while allowing the Member to conduct his/her operation with the level of predictability and convenience

generally afforded to other members of the Co-operative under their Delivery Notices;

- 3.4. feed, maintain and finish all cattle delivered by the Member under Section 3.3;
- 3.5. use its best efforts to market and sell all cattle delivered by the Member under Section 3.3 at the most advantageous terms available at the time of prospective sale;
- 3.6. pay the Member for cattle sold by the Co-operative on the Member's behalf in accordance with the terms of Section 4.

PRICE AND PAYMENT

4. The Co-operative shall pay the Member for each Animal delivered by the Member, accepted by the Co-operative, and sold by the Co-operative on the Member's behalf, in accordance with the following provisions:
 - 4.1. The price payable by the Co-operative for the Animal shall be the price actually obtained by the Co-operative for that Animal, less the Finishing Cost thereof as prescribed in Section 4.2. The price shall be paid by the Co-operative to the member no later than 5 business days after the Animal is sold by the Co-operative.
 - 4.2. The Finishing Cost for each Animal shall be calculated by the Co-operative by applying that fraction of the price received by the Co-operative for that Animal which covers the estimated average cost per Animal for all cattle finished by the Co-operative over the month in which that Animal is sold by the Co-operative, taking into account:
 - 4.2.1. the cost of feed, labour, veterinary care, and other variable costs incurred by the Co-operative on an ongoing basis in order to finish cattle;
 - 4.2.2. the fixed costs, administrative costs, and other costs related to operation of the Feedlot incurred by the Co-operative on an ongoing basis; and
 - 4.2.3. the amount set from time to time by the Co-operative to cover contingencies and to provide for patronage dividends to the members.

The Co-operative shall adjust the fraction to be applied in the foregoing calculation on or before the first day of each month by reference to its cost

experience in the preceding month and its assessment of prospective changes in its costs for the new month.

DURATION AND TERMINATION OF THIS AGREEMENT

5. This Agreement has an indefinite term, and shall continue until terminated as provided in Section 6, or until cancelled as provided in Section 10 or 14.
6. This Agreement may be terminated in any of the following ways:
 - 6.1. By the written consent of the Member and the Co-operative as an incident to the Member's transfer of all of his/her Shares in accordance with the By-Laws, effective on the date the Member no longer owns the Shares;
 - 6.2. By written notice from the Member, at his/her sole discretion and without any reason being required, with such termination to be effective on the last day of the Production Year next following the Production Year in which in which such notice is given;
 - 6.3. By election of the Member effective at the end of a Production Year in which the Co-operative has voluntarily commenced bankruptcy proceedings or has become insolvent within the meaning of the *Bankruptcy and Insolvency Act (Canada)*;
 - 6.4. Upon termination of the Member's membership in the Co-operative for any reason permitted in the Articles or By-Laws, effective on the date agreed by the parties, or failing such agreement, on the last day of the Production Year in which termination of the Member's membership occurs.

OTHER DOCUMENTS WHICH ARE PART OF THIS AGREEMENT

7. In addition to the terms set forth in this Agreement, the parties agree:
 - 7.1. to be bound by the Articles and By-Laws of the Co-operative, and where any provision in either the Articles or By-Laws conflicts with a provision in this Agreement, the provision in the Articles or By-Laws shall prevail;
 - 7.2. that the Rules are part of this Agreement, provided that if any Rule is inconsistent with the Articles, the By-Laws, or the terms of this document, then the Articles, By-Laws, or terms of this document shall prevail. The Co-operative, so long as it acts reasonably and in good faith, may amend any portion of the Rules at any time, provided that the Co-operative shall wherever possible provide the Member with reasonable notice of its

intention to make such amendment. Subject only to Part XIX of the Act, and until action is taken by the Member thereunder, the Member is deemed to have agreed to be bound by any such amendment to the same extent as if the amendment was reflected in the Rules at the date of execution of this document;

- 7.3. to be bound by the terms and conditions contained in any Delivery Notice issued by the Co-operative to the Member, provided that any such Delivery Notice shall be substantially in the form set out in Appendix "B" hereto, and shall not be inconsistent with the Rules or the terms of this document.

DEFAULT AND REMEDIES

8. Either of the following acts or omissions shall constitute default by the Co-operative of its obligations under this Agreement:
 - 8.1. Failure to accept any cattle delivered by the Member in accordance with his/her Delivery Notice, provided such cattle satisfy the warranties of the Member set forth in Section 2.3;
 - 8.2. Failure to pay the Member as required in Section 4.
9. Upon breach by the Co-operative of any obligation referred to in Section 8, the Member may sell any cattle thereby affected to any other person, and shall be entitled to receive from the Co-operative any difference between the price thereby obtained and the price which the Member would have obtained from the Co-operative if the breach had not been committed. The Member may not claim or recover any other incidental or consequential damages from the Co-operative.
10. Upon breach by the Co-operative of any obligation set forth in Section 3 other than a breach referred to in Section 8, the Member may give notice to the Co-operative, specifying such failure and requiring the Co-operative to remedy the same within a reasonable time thereafter. If the Co-operative shall fail to remedy the same within such reasonable time, the Member may cancel this Agreement effective the last day of the Production Year in which such failure occurred. The Member may not at any time claim or receive any incidental or consequential damages from the Co-operative by reason of any breach to which this Section applies.
11. The Member shall not be entitled to withhold any future required delivery of cattle by reason of any present or apprehended breach of this Agreement by the Co-operative.

12. Either of the following acts or omissions shall constitute default by the Member of his/her obligations under this Agreement:
 - 12.1. Failure to make any delivery of cattle within the time or times required in a Delivery Notice;
 - 12.2. Failure of any Animal to satisfy any of the warranties specified in Section 2.3.

13. The Member understands and agrees that the success of the Co-operative is dependent upon his/her adherence to the terms and conditions of this Agreement, and in particular, compliance with his/her Delivery Obligations. The Member further understands that the Co-operative will suffer irreparable harm not adequately compensable in damages if the Member fails to meet his/her Delivery Obligations, and that, so long as the Member is capable of meeting such obligations, the balance of convenience will always favour the Member being required to meet such Delivery Obligations, leaving for later resolution any differences between the parties which led to the Member's refusal to deliver. Accordingly the Member agrees that, if he/she fails or refuses at any time during the term of this Agreement to meet his/her Delivery Obligations to the Co-operative, the Co-operative shall be entitled, in addition to any other legal remedies it may have, to do any one or more of the following:
 - 13.1. to obtain immediate interim injunctive relief from Court against the Member restraining him/her from further breach of his/her Delivery Obligations, or requiring him/her to specifically perform such obligations;
 - 13.2. to claim liquidated damages against the Member in the amount of \$10 for each Animal which the Member was required to deliver and which he/she failed to deliver, or which, when delivered, did not satisfy any one or more of the warranties specified in Section 2.3;
 - 13.3. to deduct the amount of such liquidated damages from any other amount then or thereafter owing from the Co-operative to the Member.

14. Upon the failure by the Member to meet any obligation set forth in Section 2 other than a breach referred to in Section 12, the Co-operative may give notice to the Member, specifying such failure and requiring the Member to remedy the same within a reasonable time thereafter. If the Member shall fail to remedy the same within such reasonable time, the Co-operative may cancel this Agreement effective the last day of the Production Year in which such failure to remedy occurred.

DISPUTE RESOLUTION

15. Subject to Section 16, all matters of difference between the parties in relation to this Agreement shall be referred to the arbitration of a single arbitrator, if the parties agree upon one, otherwise either party may apply to the Queen's Bench Court of Saskatchewan for appointment of the arbitrator. The award and determination of the arbitrator shall be binding upon the parties and their respective heirs, executors, administrators and assigns. Any arbitration under this Part shall be governed by the following:
 - 15.1. Except where inconsistent with this Article, the provisions of *The Arbitration Act, 1992* of Saskatchewan applies to the resolution of all disputes to be resolved under this Part.
 - 15.2. The parties specifically adopt the current Rules of Procedure For Commercial Arbitration published from time to time by the Arbitration and Mediation Institute of Canada Inc. as the rules of procedure to govern any arbitration taken under this Agreement, and where any such rule of procedure conflicts with any provision of *The Arbitration Act, 1992*, the rule of procedure shall prevail.
16. Notwithstanding Section 15:
 - 16.1. the Co-operative may apply to a Court of competent jurisdiction to obtain the injunctive relief specified in Section 13.1; and
 - 16.2. the Member may apply to a Court of competent jurisdiction for any remedy available to him/her in Part XIX of the Act relating to an act or omission of the Co-operative or any director, officer, employee or agent thereof other than a determination that the Member has failed to meet his/her Delivery Obligations, has breached a warranty given in Section 2.3, or has otherwise breached this Agreement.

GENERAL TERMS

17. The Co-operative shall have a lien on all cattle delivered to the Feedlot by the Member for all costs incurred by the Co-operative to feed and finish such cattle.
18. Title to and risk of loss of all cattle delivered to the Feedlot shall remain with the Member until such cattle are sold by the Co-operative on the Member's behalf. In all of its duties and functions for the Member under this Agreement, the Co-operative acts solely as agent of the Member, with authority to feed, finish, market and sell the Member's cattle, and to do all other things on behalf of the Member which are necessary to achieve the intent and purpose of this Agreement.
19. The Member may not assign this Agreement without the prior written consent of the Co-operative.

20. This Agreement constitutes the entire agreement between the Co-operative and the Member, and there are no oral or other conditions, promises, covenants, representations, or inducements in addition to, or at variance with, any of the terms of this Agreement.
21. No waiver of a breach of any of the provisions of this Agreement shall be construed to be a waiver of any subsequent breach of the same or any other provision of this Agreement.
22. The language in all parts of this Agreement shall be construed as a whole and not strictly for or against any party. In the event that any part of this Agreement is held to be invalid or void, the invalidity shall not affect any other part of this Agreement.
23. Subject to the other provisions of this Agreement, all of the terms and conditions of this Agreement shall inure to the benefit of and shall bind the parties and their successors and permitted assigns.
24. The Co-operative reserves the right to unilaterally alter any provision of this Agreement for which amendment is not otherwise specifically provided in this Agreement, provided that any alteration made under this Section shall be first approved at any regular or special meeting of the Members of the Co-operative, at which a quorum is registered as being present or represented by mail vote, by a majority of members so preset or represented by mail vote, where the notice of such meeting contains a statement of the proposed alteration. A copy of such alteration shall be duly delivered to the Member in accordance with Section 26.
25. This Agreement shall be construed in accordance with the laws of the Province of Saskatchewan.
26. Any Notice required or permitted in this Agreement may be given by regular mail, facsimile transmission, or by Email transmission (where addresses or contact information is provided):

to the Co-operative at:

Box 123,
Dusty Plain, SK
S0L 9X0
fax: (306) 222-3344
Email: *admin@grassymeadow_ngc.sk.ca*

to the Member at:

DATED at Dusty Plain in the Province of Saskatchewan, this ____ day of _____, A.D. 20__.

**GRASSY MEADOW CATTLE FINISHING AND
MARKETING CO-OPERATIVE LTD.**

President

Secretary

DATED at Dusty Plain in the Province of Saskatchewan, this ____ day of _____, A.D. 20__.

Witness

Member's name (please print)

Member's signature

APPENDIX “A”
Quality Standards and Management Practices Schedule

Feeding and Management Guidelines

To maximize production efficiency and to capture all the benefits of building design and quality genetics, an all in-out production cycle is essential. This is necessary to break disease cycles, allow time for cleanup and disinfection, and to optimize feeding management. Though it is expected that a herd health and nutrition expertise will be engaged by the Co-operative to provide strict guidelines for overall herd management, herd health, and feeding, the following guidelines will represent a method of operation until such times as other specific guidelines can be established.

General Management Practices

There must be no exposure to cattle owned by persons other than the Member for biosecurity purposes.

Maintain strict personnel biosecurity for admittance to facilities. Rendering trucks should never enter the premises.

Keep dogs, cats, and other domestic animals out of facilities.

Conduct a daily observation of all cattle on an individual basis for health problems, and treat appropriate animals with proper medications.

Power wash and disinfect inside of facilities and feeders prior to admittance of each lot.

Record all cattle deaths and sickness on a report form provided by the Co-operative.

Maintain facilities and all equipment in proper functioning order.

Implement rodent- and fly-control procedures in and around facilities.

Mixing and regrouping of cattle should be avoided.

Emergency plans should be in place that include veterinary assistance, equipment malfunction, and fire protection.

Cattle should be kept reasonably clean in comfortable, healthy surroundings.

Maintain accurate records concerning parentage, mortality, and morbidity of all cattle in the Member's cattle operation.

Manage, store, and dispose of wastes, and land-apply animal wastes as required by all applicable laws and regulations and consistent with best management practices.

Maintain up-to-date animal waste management plans and records in compliance with all applicable laws and regulations.

Dispose of all dead animals in accordance with applicable laws and regulations and public-health laws, and consistent with best management practices.

Obtain and maintain all permits necessary in connection with the raising of cattle.

Take all reasonable measures to assure that no cattle owned by other persons are placed on the property and facilities employed in the Member's cattle operation, and that cattle owned by other persons are not allowed to commingle with the Member's cattle.

Insurance Requirements

The Member shall maintain at his/her expense a general liability insurance policy providing a minimum of \$500,000 single-limit bodily injury and replacement value property damage coverage for the Member's facility, and shall provide the Co-operative with the current certificate evidencing such coverage. The Member recognizes and accepts the risks and hazards inherent in any livestock venture, and shall be responsible to obtain at his/her option and expense any disability, business interruption, or income replacement insurance as the Member may wish to carry.

Breeding Requirements and Restrictions

None at this time

Weight and Quality Requirements and Restrictions

None at this time

Nutrient Specifications for Grow/Finish Diets

The following nutrient specifications are expected to be followed by Members feeding cattle for this project.

Nutrient	100 kg	200 kg	300 kg	400 kg
C. protein, %	19.0	18.5	17.0	16.0
Lysine, %	1.1	1.0	0.85	0.80
Met. & cyst., %	0.66	0.62	0.53	0.51
Threonine, %	0.72	0.65	0.55	0.53
Tryptophan, %	0.21	0.19	0.15	0.14
Calcium, %	0.75	0.70	0.60	0.50
Phosphorus, %	0.68	0.60	0.50	0.40

Animal Health

It is not anticipated that cattle in care of the Member will require routine animal health treatments. Animals should be observed on a routine schedule and more frequently during inclement weather. Animals should be examined for signs of health problems, physical discomfort, or injury. Unexpected death or signs of illness should be reported promptly to the Co-operative. Sick or injured animals must be promptly treated. Animals suspected of having a contagious disease must be isolated. Sick animals should be observed thoroughly at least twice daily and assisted with feeding and drinking, if needed, and given veterinary care, as appropriate. It will be required to record all treatment events on documents provided by the Co-operative. Medications must be administered according to label directions. A local practising veterinarian can be called for emergency purposes, but it is required that the Co-operative personnel be notified before such action is taken.

Animals unable to walk or that are ill and will not recover must be humanely euthanized on the farm and not transported to the feedlot. Where the likelihood of recovery is low, despite the treatment, the animal should be euthanized. When the likelihood is high, the

animal should be removed to an area where competition for feed and water is lower and the animal can be monitored and treated regularly.

If death occurs, necropsies will be ordered only by representatives of the Co-operative. Dead animals must be removed from the pens immediately. Depending on the site and local ordinances, they may be buried, composted, incinerated, or disposed of by a commercial rendering service. For rendering pick-up, a screened pick-up site should be constructed away from the buildings. Rendering trucks will not be allowed to enter the Member's facilities.

Medical supplies and needles should be disposed of properly after use.

Transporting Animals

During hot weather, transporting cattle during midday should be avoided. During cold weather, trailers should be properly bedded.

APPENDIX "B"
Delivery Notice

Date: _____

Member: _____

Annual Quota: _____ Animals

No. of Animals to be delivered under this Notice: _____

Delivery Schedule

1. _____ Animals between _____ and _____
2. _____ Animals between _____ and _____
3. _____ Animals between _____ and _____

All deliveries are to be made to the Feedlot at the Member's expense. All provisions of the Member's Marketing Contract apply to this Delivery Notice, and all deliveries made by the Member under it.

Please acknowledge receipt of this Notice by signing, dating, and returning the attached copy within one week of receipt.

**GRASSY MEADOW CATTLE FINISHING AND
MARKETING CO-OPERATIVE LTD.**

Per: _____

I acknowledge receipt of this Notice: _____

Member's Signature

Date

Contact Information
for Questions Related to
New Generation Co-operatives

Centre for the Study of Co-operatives

University of Saskatchewan
101 Diefenbaker Place
Saskatoon SK S7N 5B8
Telephone: (306) 966-8509
Facsimile: (306) 966-8517
Web Site: <http://coop-studies.usask.ca>

Saskatchewan Economic and Co-operative Development
Regional Economic Development Services

1919 Saskatchewan Drive
Regina SK S4P 3V7
Telephone: (306) 787-5787
Facsimile: (306) 787-2198
Website: <http://www.gov.sk.ca/econdev>

Saskatchewan Agriculture and Food

Industry Development Branch
Room 329, 3085 Albert St.
Regina SK S4S 0B1
Telephone: (306) 787-8523
Facsimile: (306) 787-0271
Website: <http://www.agr.gov.sk.ca>

Participant List for the NGC Experts Workshop

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