

Approved February 14, 1991
Date

MINUTES OF THE Senate COMMITTEE ON Agriculture

The meeting was called to order by Senator Jim Allen at
Chairperson

10:10 a.m./~~10:10~~ on February 6, 1991 in room 423-S of the Capitol.

All members were present ~~except~~

Committee staff present: Raney Gilliland, Legislative Research Department
Lynne Holt, Legislative Research Department
Jill Wolters, Revisor of Statutes Department

Conferees appearing before the committee: Joe Lieber, Kansas Cooperative Council
John Butel, farmer, Overbrook

Senator Allen called the Committee to order and called on staff to review SB 73.

Staff reviewed SB 73 noting that the bill requests amendments for the Cooperative Marketing Act which has not been updated since 1921. Staff reviewed the changes in the sections of the bill and stated that the outline followed was one that had been made by the Coop Council included in (attachment 1) on pages 2 and 3. Staff stated that the outline had been studied; that it was prepared very well and thus used as a guide for reviewing the bill.

The Chairman called on the following to testify on SB 73.

Joe Lieber provided copies of his testimony to the Committee (attachment 1). Mr. Lieber explained that updating the Cooperative Marketing Act had been worked on for about a year, and that the changes had been discussed with agricultural organizations.

In answer to Committee discussion Mr. Lieber answered that the changes were requested to make the reading of the Cooperative Marketing Act up-to-date, and to make it compatible with corporation law.

John Butel gave the Committee copies of his testimony (attachment 2) and requested favorable action on SB 73 by the Committee.

Senator Allen announced that the hearing for SB 73 would continue on February 7 and then adjourned the Committee at 10:58 a.m.

GUEST LIST

COMMITTEE: Senate Agriculture

DATE: February 6, 1991

| NAME | ADDRESS | ORGANIZATION |
|---------------------|--|-----------------------|
| Mike Jensen | Manhattan | Ks Park Producers |
| Bruce GRAHAM | Topeka | KEPC |
| DEBBIE McCASKILL | TOPEKA | COMMERCE |
| John Schlageck | Manhattan | KFB |
| Jeff Burkhead | Manhattan | Farm Bureau |
| KEN STEWART | 1021 1st Nat. Bldg WICHITA, KS. 67202 | AMPI legal counsel |
| Ernie H. Fenner | City of Lamas, Mo 64759 | individual |
| Nancy F. Kantola | Topeka | CKFC |
| Diane Gruver | Topeka | Ks Co-op Council |
| Gino Bereman-Morill | Kansas City, Mo | Ferland |
| Elita Ann Nutwiler | Topeka | Interv. |
| Chris Wilson | Topeka | Ks Grain & Feed Ass'n |
| Tom Turner | " | " " |
| Ivan W. Wyatt | McPherson | Ks Farmers Union |
| Tom Dersel | Lamed | Ks Farmers Union |
| Emil P. Muehrst | McPherson | Ks. Farmers Union |
| Terry D. Berthoff | Natchinson | Ks Co-op Council |
| Howard M. Lee | " | KFAA |
| Joe Lieber | Topeka | Ks Co-op Council |
| Becky Watts | Emporia | Ks. Farmers Union |
| John Butel | Overbrook | Overbrook Corp |
| Bill Miller | Manhattan | Kansas Farm Bureau |
| Ralph W. Smith | Halvosta Kans | Kansas Farmers Union |

Testimony on SB 73
Senate Agriculture Committee
February 6, 1991
Prepared by Joe Lieber
Kansas Cooperative Council

Mr. Chairman and members of the Committee, for the record, I'm Joe Lieber, Executive Vice President of the Kansas Cooperative Council. The Council has a membership of nearly 200 cooperatives which have a combined membership of nearly 200,000 Kansas farmers and ranchers. I have Terry Bertholf with me, a cooperative attorney who wrote most of the proposed changes. Terry will help to answer any technical questions.

We appreciate the Committee's willingness to introduce SB 73 that updates the Kansas Cooperative Marketing Act.

As most of the Committee knows by now, the "Act" was enacted in 1921 and has had only modest changes since that time, the last being in the 1940s.

The "Act" is 70 years old. Think of all the changes that have taken place in cooperatives, farming, agriculture and in our state economy in the last 70 years.

Another way of looking at it is to imagine what farming and agriculture will look like in the year 2061, 70 years from now.

These changes are why the Kansas Cooperative Council supports the

*Senate agriculture Committee
2-6-91
attachment 1*

updating of the Kansas Cooperative Marketing Act. If farmer/owned cooperatives are going to continue to provide service for their members, they must be able to diversify and become more flexible.

What does the proposed changes in SB 73 do to help the farmer owned cooperatives to prepare for the '90s and beyond?

1. It makes technical changes such as modern spelling, new terms and definition.
2. It allows five persons to form a cooperative instead of ten.
3. It allows cooperatives to form cooperative subsidiaries or invest in other corporations.
4. It allows cooperatives to engage in business with non members as long as the majority of their business comes from members.
5. It amends the language to increase control of the association by stockholders who attend and vote at meetings.
6. It leaves the decision on payment for a member's stock to the discretion of the board of directors.
7. It allows cooperatives to pay higher annual dividends on common or preferred stock.
8. It designates a special time that the directors must call a special meeting and the notice of that meeting must be mailed.
9. It allows cooperatives to have up to 20% of their board made up of non members if they want to.
10. It allows cooperatives to call their board presidents, chairmen, and the manager, president of the cooperative if

they want to.

11. It allows voting to be based on patronage if the members want it, but no member will have over 5% unless it is another cooperative.
12. It requires that if the cooperative's bylaws provide for election of directors by district, then a petition to remove a director must be signed by 20% of members residing in that district.
13. It provides that any increase in Capital be first approved by two-thirds of the directors.
14. It removes the section that makes it a crime to spread false reports about the cooperative.
15. The last part of SB 73 sets forth the procedure for mergers and consolidations of cooperatives.

As stated earlier, most of these changes were written by our hired attorney, Terry Bertholf. He specializes in cooperative Law and has been involved with most cooperative issues and cases over the last several years in the state.

Copies of these proposed changes have been sent to all of our members including regional cooperatives. Some of the language was written by attorneys from Farmland Industries and the National Cooperative Refinery Association in McPherson, KS. Both are organized under the Kansas Cooperative Marketing Act. The Revisor's Office also made changes.

Since the cooperatives are owned by the producers and ranchers of Kansas, we felt it was important that we receive their input and support.

Last August, we sent copies of the proposed changes with our explanation of those changes to the following Ag organizations.

| | |
|----------------------------------|------------------------------|
| Associated Milk Producers | Kansas Livestock Association |
| American White Wheat Prod. Assn. | Kansas Pork Producers |
| Farmers Union | Kansas Soybean Association |
| Kansas Board of Agriculture | Kansas State Grange |
| Kansas Corn Growers | Kansas Wheat Growers Assn. |
| Kansas Electric Cooperatives | Mid-America Dairy |
| Kansas Farm Bureau | |

I made personal presentations to the board of directors of the Farmers Union, the Kansas State Board of Agriculture and the Kansas Wheat Growers Association.

I spoke to the leadership of the Farm Bureau and made presentations to the members of the Kansas State Grange at their annual meeting and spoke to several district meetings of the Kansas Wheat Growers Association. I am happy to report we have received favorable support from the Grange, Farm Bureau, Wheat Growers and the Pork Producers, as well as the Committee of Kansas Farm Organization.

The only negative response has been from the Farmers Union. We're disappointed by that because we feel that the philosophy expressed in these changes in the Kansas Marketing Act coincide with the philosophy of the Farmers Union.

I would also like to respond to some other negative comments that I've heard.

First of all, I heard, "These changes will allow Farmland Industries to circumvent the Kansas Corporate Farming laws and take the power away from the country."

Farmland is owned by the country. Without the country, there is no Farmland. Farmland is a member of the Kansas Cooperative Council, but so are nearly 170 local cooperatives, and without them, there is no Council. Terry Bertholf does not work for Farmland. His clients are the local cooperatives. In all the discussion in the Council's Legislative Action Committee, the special Ad Hoc Committee and the board of directors meeting, the subject of corporate farming never came up.

Farmland would benefit from some of these changes, but every change they benefit from will help the locals, too. Farmland is in support of SB 73 and would like to see it passed. There is no hidden agenda. If there was, you can rest assured I'd be back next

year making new changes.

Another negative comment I would like to respond to is, "Would this give cooperatives competitive advantages?" The answer is NO. What it would do is create a level playing field in which cooperative corporations can compete.

Cooperatives need to be able to be as flexible as other corporations. Since September 1980, 59 Kansas Cooperatives have ceased to be independent operations. Seven of them have gone out of business. Nine have been bought by independents and the rest have either merged, consolidated or been bought out by other cooperatives.

In a lot of communities, the cooperative is the largest tax payer and largest employer. The proposed changes in SB 73 will not save all of them but it will give them an opportunity to adjust and to merge if necessary.

We would like to thank the Committee for your time this morning and for introducing SB 73. We would also like to thank the Revisors Office and Legislative Research for the work they have done.

Again, thanks. Terry or I will be willing to answer any questions.

COOPERATIVES PAY TAXES

(1) Farmer cooperatives are taxed like any other corporate entity with one exception. With respect to earnings which may qualify for distribution to the cooperative's farmer members, such earnings may also be deductible to the cooperative. Even so, such earnings remain taxable to the cooperative's farmer members as part of their overall taxable income.

(2) Earnings by farmer cooperatives thus are not exempt from taxation. Such earnings are taxed either at the cooperative level or as taxable income to its farmer members. And, in some cases, such earnings or income may be subject to taxation at both levels.

(3) According to USDA data, the 100 largest cooperatives paid over \$164 million in income taxes in 1989.

(4) Surveys conducted by the Kansas Cooperative Council for 1988, 1989 and 1990 show:

In 1988 local cooperatives paid, on the average, \$41,182.91 in property taxes.

In 1989 the average was \$44,739.72.

In 1990 the average was \$51,566.78.

(5) The annual payroll average was:

1988 - \$428,801.84
1989 - 439,069.75

(6) The average paid for licenses and fees annually:

1988 - \$4,136.31
1989 - 6,396.58

This would more closely mirror the ability of non-cooperative corporations to form wholly-owned subsidiaries.

The changes in subsection (c) are merely spelling changes.

- 4. Section 17-1604. The amendment to Section 17-1604 is intended to expand the purposes and powers of an association formed under the Act. Its purpose is to allow an association to engage in any activity, so long as a majority of its business is done with or for its members. The current language, by delineating certain types of activities as appropriate to engage in with non-members, might be interpreted to imply that other activities are not permitted. In order to survive in the current business environment, it is often necessary for a business to diversify its operations, thereby protecting itself from the vulnerability that a one-product business has to fluctuating market conditions. A cooperative should similarly be permitted to diversify and to expand into more non-member related businesses. It is not uncommon for the non-member business to provide the steady income that allows the cooperative to continue to service its members in an industry which is affected by as uncontrollable factors as the weather. The amendment clarifies that these current practices are permissible. The amendment makes it clear, however, that the majority of the business of the cooperative must still be done with or for its members.
- 5. Section 17-1605. The amendments to section 17-1605 are somewhat parallel to those made in 17-1604. Subsection (f), as amended, simply would allow a cooperative to invest in other corporations, regardless of the business in which they are engaged. Cooperatives are currently investing in other corporations and the amendment would clarify that such activity is permitted. Again, this allows the cooperative to diversify its investments.

In subsection (i), cooperative associations are granted the powers "necessary or incidental to the purpose for which the association is organized . . ." The proposed changes remove some of the limiting language. The economy in which cooperatives operate is much more complex than the economy of 1921 when the Act was enacted. Many cooperatives now desire to engage in activities intended ultimately to benefit the cooperative and its members that may not be characterized as "incidental" to any business being carried out by the cooperative with or for its members, such as lawn and garden operations, convenience stores and auto parts supply business. Again, diversification of the cooperative's business may be necessary for survival of the cooperative.

The proposed amendments to sections 17-1604 and 17-1605, taken together, would eliminate any arguments about whether a cooperative's activities were "incidental." It would authorize a cooperative formed under the Act to engage in any activity so long as the cooperative was engaged primarily in the conduct of business with or for its members and the business done with or for members was greater than that done with nonmembers.

- 6. Section 17-1606. The changes in language in this section are merely done to reflect that terminology commonly used by Kansas Cooperatives. The amendments also specifically provide for the manner in which a trust would participate (*i.e.*, through the actions of a trustee) and make a spelling change.
- 7. Section 17-1607. The amendments in this section generally make it more similar to the statutes applicable to regular business corporations. For example, the regular business corporation statutes do not require that the principle place of business of the corporation be included in the articles of incorporation. Subsection (c) was therefore deleted to remove that requirement. Similarly, general business corporations may have perpetual existence unless the articles of incorporation otherwise provide. The current Cooperative Marketing Act limits the duration of a cooperative to 50 years. This limitation is deleted in the proposed amendment. The change to the current subsection (5) merely removes unnecessary redundant language.
- 8. Section 17-1608. This section is amended to include the term voting stockholders (as the voting members of many cooperatives are often called). It also amends the language so that a determination on the necessary votes is based on the number of voting members or voting stockholders *voting at* a meeting, instead of merely the number of stockholders *attending* the meeting. This would eliminate any possible problem with members registering as attending a meeting and then either leaving the meeting or not participating in the vote.
- 9. Section 17-1609. Subsection (b) is amended to address the issue of a quorum when voting is determined by voting power.

Subsection (i) is amended to eliminate the requirement that a cooperative appraise the stock of a member who withdraws or is expelled and pay the member for that stock within one year. The decision on payment for a member's stock would, instead, be made at the discretion of the Board of Directors. If a cooperative member has the right to withdraw from the cooperative and require payment for his stock, this could put an unreasonable burden on the cooperative. Cooperatives have not traditionally had large amounts of available cash and, therefore, for a cooperative to pay for the stock of one departing member, might require the cooperative to liquidate the assets that are of benefit to all of the remaining members. Although not specifically addressing this section of the Act, the courts have recognized that, in general, decisions on redemption of cooperative stock should be in the sole discretion of the Board of Directors.

The amendment to subsection (j) would allow an increase in the rate of dividends payable on common or preferred stock from 8% to an amount not exceeding the contract rate of interest set forth in the Kansas statutes at the time of issuance of the stock. This rate is currently 15% per annum. The principal purpose of this amendment is to allow a

cooperative to issue a class of preferred stock bearing a dividend rate that might be attractive to an investor.

- 10. Section 17-1610. This section is amended to provide more protection and rights to the members of the cooperative. It is amended to specifically require that, upon request of the stockholders for a meeting, the directors must hold a meeting within 60 days. The current Act does not set a deadline within which the meeting must be held. In addition, a change has been made on the method for notice about meetings to be given to members. The current Act allows for notice of meetings to be mailed to the members and stockholders or to be published in a newspaper where the cooperative has its principle place of business. The provision for notice by publication was removed because such notice would be inadequate notice in today's environment.
- 11. Section 17-1611. The amendment to this section would specifically allow the members or voting stockholders to elect some directors who were not members of the cooperation association, so long as eighty percent of the directors were members. This reflects the modern trend of corporations to have outside directors so that the corporation can draw on the expertise of persons outside of the organization. It would also allow a cooperative to elect its general manager as a director, where the general manager was not a member of the association. It would not require that a cooperative permit the election of non-member directors. Each cooperative would have to separately address that issue in its Articles of Incorporation and/or Bylaws.
- 12. Section 17-1612. This section is amended to provide that the president and/or the chairman, as well as the vice-president and/or the vice chairman shall be directors. The change would permit the Board of Directors to elect as president and/or vice presidents individuals who were not directors. For example, the manager, who might not be a director, could be elected as president.
- 13. Section 17-1613. This section is amended to change the limit on the percentage of a cooperative's stock that any one member may own. The current statute provides that no one member can hold more than one-twentieth of the voting stock. The amendment would increase that amount to 20% of the voting stock. This change is consistent with the change in section 17-1603, decreasing to five the number of members necessary members to form a cooperative.

This section is also amended to specifically permit a cooperative to enact a voting system based on patronage and/or patronage equity. This allows the cooperative to set up a structure that gives more vote to those members who use the cooperative and/or have more equity in the cooperative, rather than requiring that all members have equal vote.

This section is amended to change the language on restrictions of common stock transfers. The current language prohibits transfers "to persons not engaged in the production of agricultural products handled by the association." The proposed language

would prohibit transfers "to persons not eligible to be a member of the association." The current language seems to apply only to marketing cooperatives and not to ag supply cooperatives or those whose members are not producers but are associations of producers. The change in the language merely reflects the character of many cooperatives.

Finally, the amendments to this section would remove the restriction on redemption of stock. The current Act prohibits a cooperative from redeeming stock when the debts of the cooperative exceed 50% and require the cooperative to pay for redeemed stock within one year. No similar restriction applies under the general corporation act. Those restrictions are therefore removed and, as amended, the Act would leave redemption of stock solely to the discretion of the board of directors. This change benefits members who are seeking redemption of stock because it permits the Board of Directors to redeem stock when the debts exceed the 50% benchmark.

- 14. Section 17-1614. The term "voting stockholder" is again added to reflect the terminology used by many cooperatives. In addition, the procedures for removal of a director or officer are enlarged to address the voting system of some cooperative which vote by stock and not by one member one vote.
- 15. Section 17-1615. The changes in this section mirror those in section 17-1610 and specifically require the board of directors to hold a stockholders meeting within 60 days after demand by one-third of the directors. The current Act does not set a deadline for holding the membership/stockholders meeting.
- 16. Section 17-1616. Section 17-1616 is amended to conform to the increased rate of dividends that would be permissible on common or preferred stock under the amendment to Section 17-1609(j).
- 17. Section 17-1617a. The amendments to this section, similar to those in section 17-1605 remove the limitation on the types of corporations in which a cooperative may have an ownership interest.
- 18. Section 17-1620. Spelling changes only.
- 19. Section 17-1621. These changes mirror the changes in section 17-1608 and make voting decisions based on the number *voting at* a meeting.
- 20. Section 17-1622. This section is deleted in its entirety. It makes it a crime to spread false reports about the finances or management of a corporation under the Act and sets a civil limitation on damages for such conduct at \$500. This provision is not contained in the general corporate statutes and appears unnecessary. The deletion of the provision would not prevent a cooperative from pursuing normal civil actions claiming libel or slander for such false statements. Furthermore, the \$500 limitation on damages may

have been a great deal of money in 1929, but today would act as an unreasonable restriction on the right of a cooperative to seek compensation for the damages caused by libel and slander.

- 21. Section 17-1627. Spelling changes only.
- 22. Section 17-1629. This section is amended to specifically provide that any increase in capital be first approved by two-thirds of the directors (rather than unanimous approval). The existing requirement of a unanimous approval would allow one board member to prevent the increase in capital. By requiring the two-thirds approval, the act still provides protection to the members of the cooperative. The amendment section also changes the terminology to reflect that currently used by cooperatives. Also, like sections 17-1621 and 17-1608, it adds the "voting at" language to the voting mechanism.
- 23. Section 17-1631. Spelling changes only.
- 24. Section 17-1636. These changes merely make the provisions regarding disposal of property consistent with the other sections, including the "and voting at" language for counting votes, the modification of the terms member and stockholder and the provision for associations organized on the one person, one vote plan.
- 25. New Sections 17-1637, 17-1638, 17-1639, 17-1640, 17-1641, 17-1642. These sections would set forth the procedure for mergers and consolidations of cooperative associations. The current Act does not specifically address mergers and consolidations. The current Act does state that the General Corporation Code applies, except where its provision are in conflict with or inconsistent with the express provisions of the Cooperative Marketing Act. It is not clear whether the legislature intended to incorporate the General Corporation Code provisions on mergers and consolidations or whether mergers or consolidations of cooperatives was contemplated at all at the time that the Cooperative Marketing Act was enacted. Because not all of the merger and consolidation provisions of the General Corporation Code apply well to cooperative associations, new language specifically addressing mergers and consolidations was developed for inclusion in the Cooperative Marketing Act. Many of the provisions of this proposal are identical to the parallel provisions in the Kansas' General Corporation Code (Sections 17-6701, 17-6702, 17-6709, 17-6710, 17-6711, and 17-6712).

Basically, the sections set forth the procedures for mergers of two or more cooperatives to merge under certain procedures. The required procedures include detailed agreement by the Boards of Directors of both cooperatives, vote by the members or stockholders of both cooperatives, and the filing of certain documents with the government (New Section 31). The amendment provides for an exception to the voting requirement for the surviving cooperative's stockholders under certain circumstances (New section 31) similar to the exceptions in the general corporation act (section 17-6701(f)).

The exception applies if the articles of incorporation of the surviving cooperative are not amended and the book value of the equity securities issued in the merger is less than 25% of the aggregate book value of all equity securities of the surviving cooperative immediately following the merger (the General Corporation Act uses 15%).

In New Section 32 the amendment provides for similar procedures for the merging or consolidation of a domestic cooperative with a foreign cooperative.

New Section 33 requires certain taxes and fees to be paid prior to the merger or consolidation being effective; New Section 34 allows the issuance of stocks, bonds, securities and similar obligations by the new cooperative after the merger or consolidation; and New Section 35 discusses the effect of the merger on pending actions.

New Section 36 sets forth the procedure for handling dissenters rights, i.e. the right of stockholders to object to the merger and receive instead the appraised value of their stock. However, the section provides that dissenters rights are not applicable where the merger does not effect the membership rights of the members of the surviving cooperative or where the active members of the non-surviving cooperative are eligible to become members of the surviving cooperative.

2/6-91

Senate Bill 73
Senate Agriculture Committee
February 6, 1991
by John Butel

Mr. Chairman and members of the Committee. I'm John Butel and I farm near Overbrook, in Osage County. I'm also a member of the board of directors of Overbrook Farmers Union Co-op Association.

It is my understanding that Senate bill 73 would enable cooperatives to diversify their operations and by doing so become more competitive.

As a farmer stockman and a director of our cooperative, I feel it very important that our cooperative be able to compete in the marketplace in the future.

As you already know, margins are narrow in the elevator and farm supply business. If we are to continue to be able to service our members we will have to diversify. The Overbrook Cooperative has recently gone into the lawn care business. This is an effort to recoup some of our losses in the grain business.

Most of the income from the lawn care business comes from non-members. Other cooperatives have opened convenience stores and other businesses with non-members to help their financial position.

These incomes from non-members are very important to all cooperatives if they are going to survive in the very competitive grain and farm supply business.

For the good of all cooperatives I would like to have the changes made in the Kansas Cooperative Marketing Act.

Thank You.

Senate Agriculture Committee
2-6-91
Attachment 2