

The Fuzzy Math of Cash Patronage Percentages

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Cooperative leaders have the responsibility of protecting the cooperative's financial security and providing members with information as to the firm's status and performance. One aspect of that transparency is to describe how the cooperative retained and distributed profits. In the early days of U.S. agricultural cooperatives, there was very little non-member business and all profits were allocated to members in a combination of stock and cash patronage. Under those conditions, the description of the cash patronage percentage told the members everything they needed to know about what the cooperative was doing with its earnings. The cash patronage percentage allowed the member to understand how much the cooperative was retaining and the cash flow and taxation that would be associated with their patronage.

Over time, some cooperative have developed more non-member based profits that are retained as unallocated retained earnings. Some cooperative boards have elected to retain a portion of member profits as unallocated retained earnings. Most cooperatives still describe their cash patronage percentage as the percentage of the patronage allocation distributed in cash. That leads to some fuzzy or confusing math. I heard a mid-western cooperative describe their profit distribution as 50%-50%-50%. They were referring to retaining 50% of profits as unallocated retained earnings and then distributed the allocated portion as 50% cash and 50% qualified stock. By my math that would 50% unallocated, 25% cash and 25% stock. Another cooperative allocated only 25% of their profits to the members but described a 100% cash patronage distribution in the manager's report to the members.

Cooperative members have access to the annual financial report and should be able to determine how profits are channeled. Still, I wonder if we could not improve our description of profit distribution. There is really two important pieces of information to communicate. First, what portion of member-based profits are allocated as patronage? Second, what is the breakdown in the allocated patronage between cash, qualified stock and non-qualified stock? For example: The board is recommending retaining 5% of member profits as unallocated retained earnings and allocating 95% as patronage. The allocated patronage will be distributed 50% cash and 50% nonqualified stock. Many cooperatives will also be passing on a portion of their Section 199A deduction. That creates another percentage to communicate.

The best way to prevent members from being fuzzy about these percentages is to be sure we are describing them as clearly as possible!