Collective reasoning

Going it alone isn't the best route for all business owners.

Cooperative corporations offer an alternative to franchising, with members working together to decide how their company should operate. With lower startup costs than most franchise systems and greater opportunity for owner input, the co-op model is gaining steam.

BY JASON DAILY
To many, the word co-op brings to mind Depression-era dirt farmers and hippies running organic grocery stores. Liz Bailey, interim president and CEO of the Washington, D.C.-based National Cooperative Business Association (NCBA), admits that those stereotypes have been difficult to overcome, but says people are slowly beginning to realize the power of cooperatives and their potential as a viable business model. In addition to groceries and agriculture, there are co-ops for other types of retail, as well as banking and housing.

"By our best estimate there are 29,000 cooperatives generating 2 million jobs in the U.S.," Bailey says. "They hold $3 trillion in assets and add $650 billion [annually] to the economy. The recession has really driven interest in co-ops. They are affordable, and people are looking for deals. Lots of people have been moving into credit unions, which are a type of co-op, and that has had a big impact on perception."

In many ways, franchises and cooperatives are mirror images of one another. In franchising, a corporate entity with a strong concept and sense of purpose creates a system that can be replicated by franchisees. In a cooperative, independent business owners band together to reduce costs and in the process create a corporate entity to do their bidding, deciding together the details of their concept and what values they will pursue as a group. That type of cooperation can be hard to manage, and cooperatives often have a more difficult time expanding than centrally run franchises. At the same time, co-ops appeal to a different type of person, one who wants to own a business but doesn't want the rigidity of a franchise system.

"Cooperative members have a lot of free will. What you agree on and what you want to do is what the cooperative is then about. It's not like a franchise."
—Liz Bailey, National Cooperative Business Association

Meanwhile, some franchises actually have a cooperative element to them. Supreme Court rulings in the 1980s opened the door for franchisees to form purchasing cooperatives in order to buy supplies from sources other than their franchisors, often at great savings. While many corporate offices resisted the cooperatives at first, the practice has become widespread—Subway and Burger King
"It's the lack of understanding that has been the big barrier, not a lack of success in the cooperative world." — Howard Brodsky, CCA Global Partners

sell water, ice or pizza, too, that’s their choice. They still benefit from a powerful national brand and purchasing power.

"We have stores from Minneapolis to Miami right now. Our quality is the same as you’d find at a franchise. Our coffee is brewed to spec. Our cups, bags, boxes and donuts are all uniform. It’s a very attractive model for someone who wants to get into business without paying a 10 or 20 percent royalty."

Still, it’s not a free-for-all. Members can’t tamper with the brand, stock discount donuts or run dirty stores. "We do maintain tight control over the core brand, and we still take them and take legal action if we have to, though that’s something we haven’t had to do yet," Merrill says. "Our members have a lot of freedom in how they want to do things because they know their market better than anyone else."

Merrill at Kaleidoscopes agrees that the most appealing aspects of co-ops are the freedom and low overhead costs. There is no upfront franchising fee, nor are there royalties to pay (though there is a charge of about $6,000 in licensing and training fees, and a nominal membership fee). "Our cost of getting into business is now under $100,000," Merrill says. "Yogurt and ice cream franchises usually run $250,000 to $500,000. We cost about 30 percent of what it costs to get into those businesses."

Kaleidoscopes offers members assistance in finding locations, signage, access to proprietary flavors and many other services similar to those that a good franchiser would provide. What’s more, co-op members receive patronage divvies, since the corporate side of the coopera- tive does not hoard its surplus profits but redistributes them to members.

But cooperatives do have shortcomings. Many like Kaleidoscopes don’t have the resources to engage in national advertising. And whether they have often been a bare-bones staff, new members don’t get the same level of hands-holding new franchisees usually receive. Morton at Donut Connection says that he helps members as much as possible but admits that as the only person running the ‘corporate’ side of the business, he has difficulty addressing all the questions and problems that crop up.

Howard Brodsky has thrived with the co-op model. When he co-founded carpet retailer CCA Global Partners 27 years ago, he selected his locations to run as cooperatives, not franchises. His goal was to even the playing field for independent business owners, not to manage and control a chain of stores.

Now his empire encompasses 12 co-ops—

including Carpet One Floor & Home, Lighting One, The Bike Cooperative and RV Cooperatives America—which are more than $10 billion in sales per year. CCA says it has returned more than 8 billion in divi-
dend to its members, and that the extra boost helps them grow and reinvest in their businesses. While 25 percent of independent flooring shops hit the dust because of the recent recession, CCA flooring cooperatives had a failure rate between 1 and 2 percent, Brodsky says.

Successes like his are one reason talk about cooperatives seems to be in the air right now. "There’s been a tremendous interest in co-ops in the last two or three years. There’s an enormous awakening of what’s being done in this sector," Brodsky says. "Most co-ops started in the Great Depression, when people were frustrated and felt they didn’t have any control over their lives. People have that same attitude today. They don’t want to be part of a larger company that can control them, but they often don’t have the scale to make their business profitable. That’s where co-ops fit in."

The NBCLA Bailey thinks businesses owners and investors should start looking more seriously at co-ops. "Cooperative development is a form of entreprene-

urism," she says. "Entrepreneurs take risks, and a cooperative development does, too—it’s just a collective form of risk. Co-ops are a tool for entrepreneurs who really want to own their own businesses, but who also want access to products and economies of scale that will make them better business."

Brodsky agrees. "It is a hidden gem of a model," he says. "When someone understands what a cooperative is, they love it. It’s the lack of understanding that has been the big barrier, not a lack of success in the cooperative world. I think the future of co-ops is a tremendous horizon, not just in the world as its playing field."®

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