Determining the Attributes of Successful Farmer Owned Value Chains

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Table of Contents

Acknowledgements…………………………………………………………..3

Executive Summary……………………..6

Introduction……………………………………………………………7

Research Methodology………………………………………………….8

Steering Committee……………………………………………………10

The Champion…………………………………………………………12

Capitalization……………………………………………………….....13

Site Selection………………………………………………………...15

Board Composition/Creation…………………………………………16

Hiring a Chief Executive Officer………………………………….....18

Strategic Plan………………………………………………………..21

Strategic Drift………………………………………………………...22

Confidentiality…………………………………………………….…….23

Points to Ponder

- Too Much Success Too Early…………………………………..24
- Micromanagement……………………………………………25
- Adopting New Technology……………………………………25
- Avoiding Self Interest…………………………………………26
- Is Court Time a Waste of Time?..26
- Knowing When to Quit………………………………………..27

Conclusion……………………………………………………………..28

References……………………………………………………………..29

Executive Summary

Western Canadian farmers have dabbled in value added opportunities since farming arrived over one hundred years ago. The reasons have varied but the most common one has been to try and capture additional value either up or down the value chain. Some companies have failed while others have gone on to do extremely well. The relative success or failure of these farmer owned ventures appears to have as much to do with the way farmers make decisions as the actual viability of the business idea itself.

The primary goal of this report is to determine the attributes of successful farmer owned value chains with an emphasis on governance and how it contributes to a company's success or failure. A group of 23 enterprises from England, Wales, Ireland, France, Ukraine, Northern United States and Western Canada were interviewed and researched. This report looks at nine different points of discussion that consistently show themselves to be problem areas for farmers during the formation and operation of a farmer owned business venture. The findings of this project will prove useful not only to aspiring farm entrepreneurs but also to any other stakeholders that may become involved in the proposed value added enterprise.

The main issues occur during the initial formation of the steering committee and revolve around a lack of formulated process, documentation and record keeping. There is a strong tendency for farmer owned boards to create a monoculture that perpetuates itself and does not allow for the need to diversify the board's skill sets. This creates a board that is hampered by inexperience and potentially distracted leadership that is focused on farming first. The need for a champion to lead, a diverse board to direct and an experienced CEO to organize are three of the most important qualities in a successful farmer owned enterprise. The dangers of undercapitalization, emotion based investment and site selection cannot be overlooked, while an emphasis on strategic planning, marketing and human resources needs to be strongly enforced if a farmer owned business wishes to succeed. These farmer centric habits should be taken into account by farmers themselves as well as government and financial institutions when guiding and financing any potential venture that has farmers as the main stakeholders.

Introduction

*"*When you come *to the fork in the road, take it"* Yogi Berra

The life of a company is full of decisions. There are a number of key decision points on the road to success that must be navigated in order to create the largest probability of business success. Farmers often find themselves taking a more difficult path to success full of unneccessary detours and dead ends.

While the purpose of this report is to determine the attributes of successful farmer owned value chains, the main focus will be on how governance, or the lack of it, influences the level of business success farmer groups have when they form a new venture. Please note that this report references and builds on a previously published document by the Agricultural Marketing Resource Center (AgMRC) in Iowa, USA.

Ever since European settlers moved on to the prairies of Western Canada in the mid 18oo's farmers have been interested in finding ways to add value to the products they produce. This entrepreneurial spirit has led to the formation of farmer owned enterprises that strive to capture additional value through vertical integration. The push to build farmer owned processing facilities gained traction in the late eighties and early nineties when commodity prices were under pressure. This report will attempt to show that the relative success or failure of these farmer owned ventures appears to have as much to do with the way farmers make decisions as the actual viability of the business idea itself. Particular problem areas seem to be tied to a series of decision making traits and tendencies that are repeatedly exhibited by farmers in, and outside, Western Canada. These farmer centric traits which stand a farmer in good stead during their agricultural career can become a major impediment in forming and steering a company through its inception. As there are plenty of books on governance and business strategy that farmers can access, this study will look at why it is that farmer owned companies consistently make conscious choices based on emotion and habit over tried and proven business techniques. This report will look at nine different points of discussion that consistently show themselves to be problem areas for farmers during the formation and operation of a farmer owned business venture. Included in this presentation are actual events from interviewed companies that serve to highlight the difficulties encountered and are followed by some solutions that may help change the outcomes described in the examples.

This report will show that farmer owned ventures have a far greater chance at sustainable success by recognizing the importance of a formalized process and making a greater effort to instill corporate governance, while avoiding emotion and habit-based decision making.

Research Methodology

The primary goal of this report is to determine the attributes of successful farmer owned value chains with an emphasis on how board structure and governance influence success. Although this has been written with a Western Canadian audience in mind, portions of the report - especially the governance issues - have been found to apply to virtually all farmer run businesses regardless of the country of origin.

To determine these attributes, a group of 23 enterprises from England, Wales, Ireland, France, Ukraine, Northern United States and Western Canada were interviewed and researched. While some of these enterprises have been around for a number of years, the bulk of the businesses have come into existence within the last 20 years and range from recent start ups through to well established ventures as well as a number of failed enterprises. Research consisted of one-on-one interviews with a wide range of participants who were key players in the formation of their business and are still actively involved. This includes shareholders, current or former board members, key members of the current management team and owners.

While this report mainly concentrates on small to medium sized farmer owned ventures, visiting additional single proprietor value-added enterprises and co-operative ventures has added significant depth to the discussion of governance. Further research consisted of follow-up interviews and substantial research on governance and corporate values for comparison purposes. It is important to note that the observations included have shown themselves to be reoccurring trends, not just individual opinions. Even though the outcomes of this report are based on the comments that have repeatedly come to the forefront, it must be stressed that they are the opinions of only one or two individuals in any operation and, no matter how valid, may not represent the views of the company as a whole. By understanding the decision making process this report hopes to clarify the challenges and avoid the pitfalls of previous farmer lead companies.

This report seeks to build on work done by the Agricultural Marketing Resource Center (AgMRC) at Iowa State University located in Ames, Iowa. Although this particular study is focused on interviews with seven large producer owned commodity processor businesses, it is an accurate template and a good jumping off point for further discussion on how farmer attitudes and expectations influence governance and the choices farmers make when starting a farmer owned business (Senechal, Lesitritz, and Hodur).

Farmer owned processing facility, Regina, Saskatchewan, Canada

Steering Committee

*"*50% of all new businesses fail or close within the first six years of opening.*" (Head 21)*

When looking at the background of the founding members of a new farmer owned value-added venture in Western Canada, it was noted that the key players in any drive to form a farmer owned venture had been exposed to at least some market opportunities outside their own farm operations. This may have been through involvement in a local marketing club, grower group and/or commodity organization. The opportunity to get outside primary agriculture and be exposed to industry players up and down the value chain is an important catalyst for the start of many farmer owned businesses.

Many new companies start as a conversation and it is difficult for most to pinpoint when the idea moved from a conversation to the beginnings of a company. Farmers are no different. Something that starts as a coffee shop discussion between two farmers then evolves into a group discussion and an agreement to form a steering committee has often been the genesis of farmer owned companies. The step from conversation to action can sometimes be an abrupt and spontaneous one. However, once it happens and the founding members have agreed to take on the mantel of responsibilty, they are obligated to do the best they can. The informal way that a large number of farmer owned ventures start is also the very reason that there is rarely, if ever, a feasability study done.

To understand the role of the steering committee we must first look at what experienced entrepreneurs do to ensure success. In large formalized public share offerings a great deal of preparation occurs long before the public ever sees the prospectus.

Experienced steering committees will have invested in a feasability study and put together a comprehensive business plan to support their prospectus. They have learned to eliminate as much uncertainty as possible in order to maximize their chance for success. By fully explaining the risks and rewards, and by outlining the path to market, these committees are assured of attracting investors of like mind who support the new venture with full knowledge of the potential outcomes of buying shares.

Unfortunately, when looking at the small and medium sized farmer owned businesses that had their genesis in a farmer led steering committee, we see a much different story. More often than not the informal decision making process used by most farmers spills over into the actions of the steering committee. Without some outside business expertise the farmer led steering committees were victims of the same repeated errors resulting in the same failed outcome time after time.

One of the most consistent failures noted was a lack of documentation and record keeping in the early stages of the ventures formation, as well as an incomplete understanding of the steps necessary to formalize a multi owner venture and immunize it against potential legal challenges in the event of its failure. There cannot be a farm reader out there who has not finished a farmer led meeting only to hear a voice at the end of the meeting ask the proverbial question, "Did someone take notes?" It cannot be stressed enough the importance of some type of formal documentation during preliminary committee meetings. While this absence of documentation tends to diminish as the company becomes more formalized, the initial effect of not having a recording secretary to keep track of motions and discussion will inevitably lead to friction at the board table as everyone brings their own recollections and interpretations to subsequent meetings. Many companies fail or disband before they ever get off the ground and even those that become a going concern run the risk of legal action at some point during their lifetime.

"That might be what you heard but that's not what I said*"* (Unknown)

As an example, one of the companies researched decided to enter litigation in order to settle a dispute over services rendered. The dispute in question occurred during a very early stage in the company's formation when there was no recording secretary. Because there was little or no documentation, most of the company's assertions were based on recollections and personal interpretations of the events in dispute. Without significant documentation or signed contracts the chances of the company reaching a satisfactory conclusion are highly unlikely. The ongoing legal expenses coupled with the added cost of a distracted board for the duration of the court case will make this an expensive exercise.

The final comment on steering committees is in regards to expenses. One trend seemed constant in all of the ventures the author has been a party to. Early in a company's creation the tendency is for every farmer to pay out of pocket for expenses incurred. This "pay your own way" encourages every expenditure to be looked on as an expense and, being farmers, expenses are to be avoided. This initial lack of funds is often the reason legal and financial advice are in such short supply early on, as they are considered an unneccessary expense. As a result, a good portion of farmer owned ventures lack the necessary diligence and documentation that may be required for future reference.

It is imperative that legal, financial and professional advice be retained and consulted from the start. These services should never be seen as an expense but instead looked upon as an investment. If there is ever a dispute, legal or otherwise, these investments will pay heavy dividends.

The Champion

"*It's amazing what you can accomplish when you're not w*orried about who gets the credit" (Harry S Truman)

Every business has challenges great and small during the course of its existence. These companies generally succeed because they have a "champion" who is committed to the success of the company no matter what. For companies that grew out of one person's dream or idea, the champion is easily definable. The most notable ones that come to mind are John Deere of Deere and Co. and tech giants like Bill Gates of Microsoft, Steve Jobs of Apple or Mark Zuckerburg of Facebook. In each of these cases the person who drove the success of the company is readily apparent. For the bulk of today's farmer owned companies the CEO acts as a form of hired champion in that they are responsible for the day-to-day success of the company and for rallying and inspiring the troops in times of a crisis.

But what about steering committees and companies that consist solely of a farmer led board? When difficulties arise, there is no one readily available to assist management or to reassert control as the board may be too distracted by their own enterprises to deal with issues effectively. Without a champion, the board may be reluctant to fire or restructure. In these cases the champion acts as a caretaker during a management crises. During the start-up phase the champion acts as the company cheerleader. At the end of the day the champion is the person who steps forward when everyone else steps back. They are readily apparent in the companies that succeed and often conspicuously absent in the companies that fail.

Capitalization

"*Risk is commensurate with the amount of money you don't have*" (Jim McCarthy)

The topic of capitalization prompted a wide variety of opinions. Only two of the interviewees stated that overcapitalization was a potential problem. One manager felt that overcapitalization could make you complacent while another admitted that the lack of debt adversely affected how they operated at the board table. On the other side of the coin was a CEO who stated that "undercapitalization can make you hungry" which was taken to mean that it acted as an incentive to move towards profitability as quickly as possible. While this theory may have merit in a well run and experienced company, the vast majority of respondents pointed to a lack of initial capital as their greatest impediment to success.

"While the necessity of sufficiently capitalizing the business would seem obvious, its importance cannot be overstated. The business must be sufficiently capitalized to withstand cash flow risks during the first few years of operation. Further, plant start-ups often require some fine tuning before reaching planned capacity. Also, markets take time to develop. Without sufficient working capital, a glitch in production, marketing or an industry-wide disruption could prove fatal" (Senechal, Lesitritz, and Hodur).

While Senechal, Lesitritz , and Hodur clearly talk about the risks associated with starting a company with limited cash reserves, there was more than one steering committee interviewed that took the situation one step further by ignoring the obvious. It was disheartening to see the number of struggling or failed companies who admitted to putting themselves in a negative cash position simply by choosing to ignore the business plan and move forward with the build even though they had not raised the targeted funds required. Not only does this cash shortfall affect every aspect of the build but it imperils the very thing that every company so desperately needs -

a leader. It will be very difficult to get a CEO to entertain employment with a company that is already cash starved. Without sufficient cash reserves the situation is no longer about hiring to your potential, it is about reduced expectations and settling for whatever you can get. One individual reported that the steering committee rationalized going forward by calculating that if they cut expenditures to get the plant up and running, they could then rebuild the cash reserves from the impending profits. In other words, being broke was just temporary.

"Raise capital externally or you will be forced to raise it internally" (Unknown)

One of the last and most poorly thought out parts of any business interviewed was the need to recapitalize. If you watch public companies trading in today's stock market you will see that they are very aware of the need to have large cash reserves and will act to raise additional share capital when they have a positive outlook that could be used to drive additional investment. Every farmer led company that struggled or failed in this report did just the opposite. Struggling companies consistently waited until their cash reserves were depleted and their lenders were knocking at the door before approaching their shareholders for additional capital. By this time the board is usually in turmoil and the short window with which to raise capital to avoid a default results in a demand for cash versus a well-reasoned plan on how this new cash will be utilized to turn the company's fortunes around. As can be expected, there is little appetite for threats and the demands for further investment failed to raise the cash required to save the businesses. Only one company interviewed chose to approach their shareholders with a plan to restructure. By explaining what needed to be done to turn things around and creating a compelling picture for success, the required funds were raised and the company was able to reinvent itself and continue in business. The other important contributing factor in this turnaround was that the board made it clear that they supported the new business plan by investing heavily themselves. This clear indication of support, along with a well-reasoned argument for recapitalization, gave the rest of the shareholders the confidence to invest.

Site Selection

"*If the dress doesn't fit, it's not a deal at any price*." (Unknown)

Western Canada is a very large, sparsely populated area and the site selection for a new business must take into account distance to market as well as distance to an adequate population and service base. Many of the farmer owned companies that were interviewed were created as a result of not only farmer investors, but local community investment as well. It must be appreciated that not all the participants viewed site selection through the same lens and more than one felt that their business location had a detrimental effect on the viability of their business venture. How the business is ultimately located is an opportunity to look at investor mentality and the rationale for investing.

There are many reasons for local investment to occur outside of the obvious financial ones. Communities usually invest to create local jobs and economic growth. Producer shareholders tend to invest with the expectation of benefiting from an enhanced price for their produce, as well as reduced transportation costs. Pride of ownership is an emotion driven reason for locals to invest in a new venture. The ability to be able to see it out their window is often a more compelling reason to invest than the actual business plan itself. An excellent example of emotional conflict overriding business sense occurred when a local company chose to build their secondary processing facility in a nearby community. This caused a great deal of dissension at the board table as the local community felt that the reason that they had invested was to support the local economy and not the neighboring community. It is important for new ventures to understand what motivates their potential shareholders and make sure that there is alignment between themselves and their stakeholders.

One of the other important aspects of site selection is to not let the short term benefits affect the long term potential of a properly sited facility. There are a multitude of business related reasons to consider a site in a rural or low density area. These reasons are generally tied to taxes, lower land and labour costs and room for expansion. However, it is important to realize that over time the growth of the business can drastically change the variable costs and what was a minor cost difference in the short term could become a fatal competitive disadvantage in the long term. An example of this is a now defunct company that located in a small community for many of the above reasons. In the beginning the penalty for distance to market was reflected in transportation costs but this was more than offset by the initial fixed and variable cost savings of their location. Over time their sales grew and as a consequence the small loss incurred on every additional truckload sold also grew, until eventually the total transportation costs far outweighed any savings from their original decision. The company was slowly strangled by its success and eventually forced to close. A good business plan would have provided clear indications that this would be the case, but for any number of the above reasons, the board chose differently.

"Site selection can become an emotionally charged issue. Business leaders and economic development professionals often appear to be more interested in local development benefits of the business than its profit potential. Grower-members may insist that the facility is sited in their home community even though an alternate site is shown to be economically advantageous. This can make the site selection process very difficult. Regardless, site selection must be based on sound business judgment" (Senechal, Leistritz, and Hodur).

Board Composition/Creation

Next to the CEO, the most important decision the steering committee will make is defining who will sit at the board table and provide guidance and direction to management. In most of the companies studied, the steering committee usually consisted, for the most part, of farmer owners and there was a natural assumption that they should sit on the board as they needed to monitor their investment. The unfortunate side effect of this decision is that there is often little consideration given towards identifying the skill sets needed to create a diverse board. Farmer owned companies, and co-ops in particular, tend to be the most prone to creating monoculture[1] boards consisting solely of farmer directors. The first thing that farmer based boards and organizations try to do is put a box around membership and board participation. This has the effect of not only limiting who can sit on the board, but also committing the board to choose

[1]Monoculture is a culture dominated by a single element**:** a prevailing culture marked by homogeneity (Meriam Webster)

from an ever-shrinking pool of candidates who may or may not have the skill sets needed to create a dynamic decision making team. The end result is a board prone to group think.[2]

A strong board will seek to circumvent this by advertising for and employing outside directors with a broad range of industry experience that compliment the goals of their company. The two areas where farmer directors would benefit from outside experience are in marketing and human resources. The addition of non-farmer directors changes the board dynamics and adds a level of professionalism that also acts as a form of director education. Some of the interviewed companies hired experienced directors/consultants on a per diem basis. This allowed the board to minimize expenses while getting the expertise they needed. As an example, one of the newer boards consisted entirely of farmers that had been struggling to move their company forward during tough times. A decision was made to look for outside directors with the appropriate skills. This addition led to a major shift in how the board responded to their challenges and highlighted the innovative solutions that outside directors brought to the table. This change in board composition was probably one of the defining moments in the eventual success of the venture.

It is also a distinct advantage to have both genders on the board. Having female board members improves corporate governance (Brown, Brown, and Anastasopolous). Studies done by Adler and supported by Brown, Brown, and Anastasopolous suggest that boards containing women consistently rank higher in revenues than their peers. Another reason for encouraging female participation is that women constitute a growing segment of the consumer population but their preferences are consistently overlooked. Women also tend to listen more and see problems and solutions differently from their male colleagues.

When attracting potential new directors the board needs to consider what constitutes fair compensation. It is not unusual for a new venture to expect the directors to operate on a gratis basis as a way to reduce costs, with board service often seen as a responsibility or duty.

[2]Group think is a psychological phenomenon that occurs within a group of people, in which the desire for harmony or conformity in the group results in an incorrect or deviant decision-making outcome. Group members try to minimize conflict and reach a consensus decision without critical evaluation of alternative ideas or viewpoints, and by isolating themselves from outside influences. Loyalty to the group requires individuals to avoid raising controversial issues or alternative solutions, and there is loss of individual creativity, uniqueness and independent (Wikipedia).

This attitude may inhibit the board's ability to attract the kind of directors that will benefit the board. In order to attract and retain quality board members, reasonable forms of compensation should be offered in exchange for the expectation of committed participation. Small companies can sometimes attract retired CEO's or business people who will sit on the board in return for the experience or challenge provided by a dynamic board. Other professionals will participate or provide direction and view it as a way to give back to their business community.

Once the board has been formed it is important to practice good corporate governance. An unfocused and poorly run board can be a major turn off for a potential board member that sees their time as valuable and expects their participation to be focused in a professional manner. A long, drawn out board meeting is the bane of good governance and can be streamlined with a few suggestions.

1. Start on time. It is a major inconvenience to directors who show up on time to wait for delinquent board members.
2. Set an agenda. Get all of the necessary information out to board members so that they have time to reflect on the proposed agenda items and will not have to make a decision in the heat of the moment.
3. Stay focused on the agenda to avoid discussion drifting to non-agenda items. Off topic discussions can be a considerable waste of time and should be discouraged until after the meeting has been adjourned.
4. Avoid side bar conversations. Carrying on a discussion with a neighboring board member while a colleague is speaking can be very distracting to everyone else and prevents you from participating in a meaningful way.

Hiring a Chief Executive Officer

"*It's impossible to unsign a contract so do all your thinking before signing*." (Warren Buffet)

The most successful farmer owned companies researched to date have made one great strategic decision and that is to hire the right CEO. They have chosen that rare commodity that operates the company with demonstrated integrity and foresight. This person develops and leads strategy while garnering respect from the board for their honesty and transparency. These companies are well positioned for success. However, the reality for the vast majority of small companies is that this is very often not the case. Most companies, regardless of their ownership structure, will have to begin corporate life on a much smaller scale with both a CEO and a board that will have to work together to succeed.

Anyone who has worked for a farmer board would generally agree that farmers can be a very independent minded group to work for. It takes a special CEO to recognize the farm culture and choose to lead from behind while working with farmers to move their company forward. Finding and interviewing that special CEO could require a great deal of effort and experience that not all farmers possess. So what are some of the things that will make this process less painful for all involved?

1. Seek professional help. During start up and especially when capital is tight, the tendency is to see the professional fees associated with hiring as a cost and not an investment. Most farmers have no relatable experience in attracting, negotiating and retaining a professional CEO. The hiring process is often no more sophisticated than posting a small ad in the local paper or having a steering committee member state that they "know a guy". All potential candidates should be included in a formal interview process where their suitability can be assessed by the board. One of the major reasons companies struggle or fail is due to a lack of professional diligence in hiring management.
2. A CEO should be hired based on the board's currently perceived needs for the company. They can be chosen based on many criteria but it usually comes down to a tradeoff between what you need and what you can afford. Pick the candidate that best reflects the current board's goals so as to avoid the dead-on-arrival CEO that is doomed to failure because their management style does not align with the board's. Undercapitalization is one reason we tend to downsize our choices, as the best candidate is often the one we need the most but feel we can least afford.
3. Make sure the CEO's contract has set terms. A good CEO is going to expect and demand a formalized contract that outlines the terms of employment, including severance and length of employment. Farmer led boards may find the hiring process a daunting or

onerous task and therefore prefer to hire for life. It is important to understand that most companies will have different CEO needs during their corporate life and the terms of employment need to reflect this fact. Based on interviews and experience, the two items that are most often overlooked by an inexperienced board are the contract length and the terms of dismissal. A set term for the contract allows an opportunity for the board to assess the progress of the company and the performance of their CEO and reward or rehire accordingly. The other critically important consideration is to clarify the terms of dismissal so as to minimize legal issues down the road. While it is always assumed that the relationship will be a rewarding one for both parties, not all business relationships end cordially. Setting the terms of compensation and dismissal from the outset are two areas where professional recruitment firms will more than pay for themselves in value and peace of mind for both parties.

4. Consult a lawyer before you need one. Lawyers need to be viewed as a cost of doing business especially when negotiating the terms of hiring a CEO. Retain one and consult them on any matters of importance. If there is a legal issue, this truly is where an ounce of prevention is worth a pound of cure.
5. It is up to the board of directors to make sure that they always have the right CEO. This means that there needs to be an ongoing process of agreed performance criteria and formal reviews to help board and management identify and improve CEO performance. It is very important that performance reviews be a constructive and rewarding experience for both parties as they are a crucial part of maintaining alignment between the stakeholders and management.
6. Many companies struggle to reach their potential or fail all together because the board becomes dissatisfied with the current CEO but are reluctant to intervene as the replacement process is seen to be too uncomfortable, too onerous and too expensive. The author interviewed board members that actually allowed their company to financially bleed to death because no one wanted to be the bad guy. Once again, a clear employment contract will alleviate much of this angst.

Strategic Plan[1]

"A vision without a plan is a halucination" (Will Rogers)

"Early in the development of a farmer owned enterprise, the board and management need to work together to define business goals, objectives and standards. Typically, management with its industry knowledge and expertise would prepare a strategic plan and present it to the board for approval" (Senechal, Leistritz, and Hodur)

The earlier management comes on board, the earlier the process of formalizing and leading the strategic plan can begin. When looking at companies that failed it would appear that without strong management leadership to articulate the visioning process, farmer owned enterprises may forgo the process entirely and concentrate on just getting the plant up and running. Even with good leadership it can be difficult for farmers in general to see value in vision and mission statements.

It could be argued that because farmers tend to be strongly results driven, process is not viewed to be as important as results. The problem with ignoring strategic planning is that if there is no vision and worse, no plan to achieve that vision, once the focus of completing the build is done, the farmer board runs into the wall of reality which is sales and marketing. While farmers are familiar with production and sales, they very seldom have experience in marketing and promotion. Without a strategic plan to define the path to market, the company will become a price taker the same as the farmer. The company will be producing an undefined product and pushing it into an undefined market for an undefined customer at an undefined quality and price. Companies that could not define their market struggled and were eventually sold or went out of business. They could not create enough margin to operate their facility while continuing to pay competitive prices to their suppliers.

[1] Strategic Plan is the systemic process of envisioning a desired future, and translating this vision into broadly defined goals or objectives and a sequence of steps to achieve them. In contrast to long-term planning (which begins with the current status and lays down a path to meet estimated future needs), strategic planning begins with the desired end and works backward to the current status (ww.businessdictionary.com).

Strategic Drift[2]

"Manage evolution or expect revolution" (Unknown)

"In revolutions, *the prize does not normally go to the slow and steady gradualist"* (John S. McCallum)

Any companies that have been in existence for even a short period of time realize the pitfalls of ignoring their strategic plan. Company failure can often be traced back to a strategic plan that is ignored in the short term or one that has failed to recognize the need to be responsive enough to environmental change. This is where strategic drift comes into play.

[2]Strategic Drift is the tendency for an industry to base their development on historical and cultural influences and on their past foundations (Bendetta).

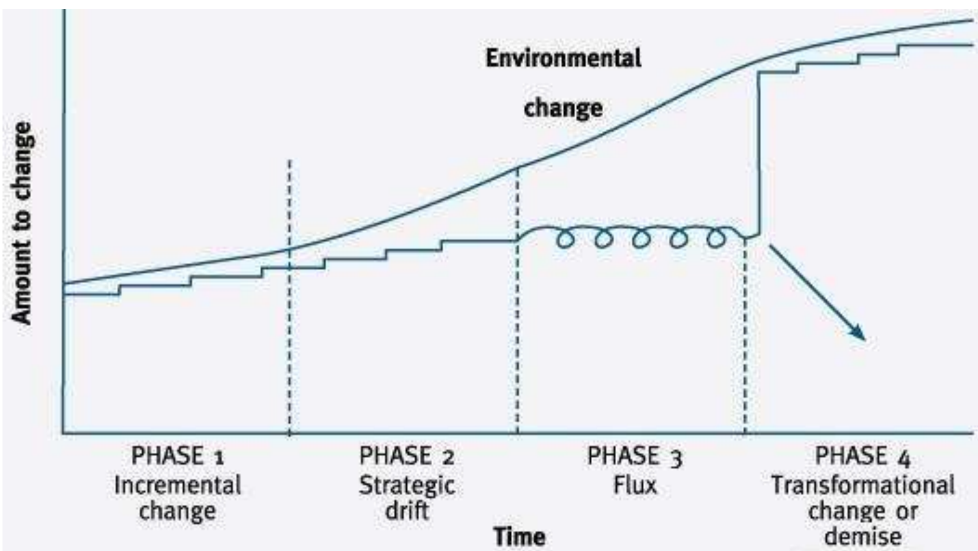

Image courtesy of:

http://kfknowledgebank.kaplan.co.uk/KFKB/Wiki%20Pages/Emergent%20strategies.aspx

A group that is often susceptible to strategic drift is the farmer owned co-operative with a monoculture board of farmers that are prone to group think and unable to support or challenge management.

In Phase 1 of the above graph, the co-op is making incremental changes to strategy but not fast enough to keep pace with market changes.

In Phase 2, the incremental changes continue but market change is accelerating while the co-op is still relying on tried and true market and decision-making practices. There is not enough independent thought to act as a catalyst for change.

In Phase 3, the co-op reaches a state of flux where members of the board and management are confused and struggle to define the new path to market.

In Phase 4, the co-op reaches the final stage where the co-op will undergo transformational change and redefine itself or it will cease to function.

Reverse strategic drift is also possible. This happens when the strategic plan is valid but the board and management are the ones drifting as they start chasing non-core strategies that cause the business to veer away from its original purpose. One of the fundamental purposes of the strategic plan is to remind board and management exactly what their business priorities are and discourage them from diverting time and capital to perceived opportunities outside of their core business.

Confidentiality

Lack of confidentiality is one of the most insidious ways that a board can harm the company. At the board table there is a definite distinction as to how privacy is viewed. During interviews, a colleague pointed out that as a private sector professional, he was constantly amazed at how much information flowed outside the board room of farmer boards. There are many reasons why this occurs but the easiest conclusion may be that the culture of farming can be very collaborative and the informal nature of information transfer does not easily lend itself to an expectation of privacy. It is, therefore, a very steep learning curve for any new board member when it comes time for discrimination at the board table. In the private sector there is a strong expectation that what is discussed at the board table remains confidential. A lack of confidentiality and a willingness to talk openly without board approval can lead to shareholders and the public receiving mixed messages. This can be very damaging to relationships between the board and management as well as customers and suppliers. This is even more relevant during times of company distress. More than one farmer board member has walked out of a board meeting and aired their personal views or grievances about policy, board members or staff in the public arena. They appear to do this with little regard for how it will be perceived by stakeholders and the potential negative affects it can have on staff morale or investor relations. Board education is critical to establish and maintain respect inside the boardroom and a united message outside the board room.

As a case in point, a company that was interviewed spoke of struggling to remain financially viable while having difficulty agreeing at the board table on a way forward. One or more of the farmer board members chose to air their version of board events at the local coffee shop and were very vocal about their dissatisfaction with the direction management was proposing. The CEO felt that they had a solid plan for restarting the venture, but when management approached local investors to gauge interest in a share offering they found that the unsanctioned comments had effectively poisoned the investment waters because the board and management were viewed as dysfunctional. The company was shut down and sold shortly thereafter.

Points to Ponder

Too Much Success Too Early

"*When on a long journey, don't get your successes too early*." (John Palmer)

One of the most surprising items encountered during interviews and research was the unexpected affect of success. On multiple occasions, discussion revolved around early success and the need to watch for arrogance creep and an attitude that the board can do no wrong. Early and easy success led one farmer group to expand aggressively and stretch their resources ever thinner. A lack of oversight and professional business experience combined with a loose board structure ultimately led to the demise of the company. This company had every reason to succeed, but with ample cash and a board comprised entirely of farmers who can be absentee managers much of the year, they allowed management to become ever more aggressive and misinterpreted this aggressive expansion as a sign of success. With neither the early warning system of good oversight, nor the sober circumspection of experience, the board was left with a mirage made of ego.

Micromanagement

While not an exclusive preserve of the farming community, there is a strong tendency toward micromanagement at the farmer board level. Whether this is because farmers are used to being involved in every aspect of their business or the reticence to delegate, micromanagement can become a big issue at the board table and can pull the board down into the minutiae of operations and away from the big picture of formulating company direction. A good chairman, along with management, will work to minimize this but during a crisis situation human nature causes us to go to what we know. For most farmers that is down at the operations level where they feel most comfortable and not up at the strategic level where they can be most effective.

Adopting New Technology

*"The early bird may get the worm but the second mouse gets the cheese." (U*nknown)

"The use of proven technology is critical to a new enterprise. A new enterprise should use the best available technology but also stick to proven technologies. An embryonic organization should not attempt to pioneer new technologies. There are simply too many unidentifiable risks for a new venture to attempt to overcome" (Senechal, Leistritz, and Hodur).

It is an already difficult learning curve when you are involved in a new venture and have limited experience. The increased risk that is tied to any unproven technology creates an added burden that no new venture should have to endure. One particular processing company that is currently successful started life by being the only plant of its kind using the technology that was installed at start up. The unproven technology proved too unreliable and this created an inconsistent supply of poor quality product that upset and frustrated all parties concerned. The company was eventually bought out and the new owners realized that the only way to re-enter the market was to install a traditional technology that was proven and reliable. It required three additional share offerings and two years of retooling to get the plant to the point of profitability that it should have reached five years earlier. While the current shareholders are thinking about expansion, the original stakeholders who had a great idea but poor execution are left wondering what might have been.

Avoiding Self Interest

Most farmer board members will have some form of vested interest in the company they serve. This may be through direct ownership of shares or as an interest in a company or farm that will be directly affected by the board's decisions. It is imperative for board members in this situation to recognize when they need to switch hats and make decisions that best represent the interests of the board they serve and not the business they own. Too many people join a board solely to promote and protect their own interests with little regard to their fiduciary duties to represent the stakeholders who elected them. Beware of the potential director who comes to the board with an axe to grind. They usually come to the table with an agenda and that agenda only has one item on it. Their interest in being a board member will almost always disappear once their agenda item has been concluded to their satisfaction. Board members need to be honest about their intentions and declare any conflicts of interest as early as possible. They should also be prepared to step away from the discussion until it is resolved.

Is Court Time a Waste of Time?

"If a technology problem or a production delay emerges that hinders start-up or causes a shut down in production, starting legal action against the technology provider or builder should not be postponed. A substantial lag can occur between the time of initiating legal action and financial remedy" (Senechal, Lesitritz, and Hodur).

One of the ways to minimize the need to pursue legal action is to consider attaching a performance guarantee rider to the contracts on any installed machinery that ties payment to a successful installation and start up. It is also sometimes prudent to pay extra and bring the manufacturer's staff in to install and train your employees. This will assure that there is complete knowledge transfer and minimize the time it takes to commission the plant. Since most contract guarantees will rarely cover any legal damages beyond the price of the machine itself, your best insurance is to have a sole contractor that designs and builds the entire facility. That way they cannot afford to ignore you as they are on the hook for the entire project.

There may come a time when a business is forced to consider legal action. Legal counsel will help you determine the relevance of your lawsuit, but you must enter into this knowing that it will be slow, it will be expensive and the outcome is not guaranteed. Even if you win, you will have diverted precious resources away from growing your business, including the board and management's time. Meanwhile, at the board table, you will find yourselves constantly rehashing the old and the negative and this can put incredible mental strain on all stakeholders involved and even derail the ability to attract new shareholders, board members and staff. Always remember that time in court is time away from your business.

The best example of a company who chose to walk away from litigation comes from a company that was poorly represented by a legal firm and was considering legal action. Their legal counsel advised that it would be an expensive and time consuming court case with the outcome uncertain. After much debate about economics versus justice, the board and management chose to walk away from what they knew to be a considerable loss and put their efforts to better use by concentrating on making the company profitable again. After two years of improvements, the once considerable loss was now the equivalent of only two weeks profit. By ignoring the emotional argument, the board demonstrated good judgment and best represented the interests of their shareholders.

Knowing When to Quit

"Some businesses have a finite lifespan; others just aren't likely to ever thrive. Persistence is good, but you must also know when to stop pouring good money into bad operations. As legendary Ottawa entrepreneur John Kelly, says, "When the horse is dead, dismount" (Spence).

Conclusion

"Insanity is repeating the same mistakes and expecting different results"   (Narcotics Anonymous, 1982)

The repeated struggles and failures of farmer owned companies can often be traced back to a simple series of events that occur in the very early stages of a start up venture. A combination of inexperience and farmer-centric traits contribute to the difficulties that many farmer owned operations experience during and after their formation. The realization and acceptance of these farmer habits combined with further training in governance and a more formalized approach to business would go a long way towards inoculating these companies against failure in the future.

While most farmer owned business woes are self inflicted, two other groups should be singled out as areas of concern. The financial services industry would serve their stakeholders far better if they were prepared to consider the many unique traits that influence the success or failure of a farmer owned business. With the knowledge gained from this report and a few well placed questions, it would soon become apparent whether the new venture in question has the appropriate governance tools and formalized processes to position the business for success. As well, government agencies sometimes become an enabler for banks and farmers by providing programs and support that fail to fully understand and address the unique issues involved in sustainable farmer owned value chains.

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