



Buying a Business to Start a Co-op

A Case Study of Food Co-op Conversions

By Patricia Cumbie
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This study was commissioned by Food Co-op Initiative, an independent, non-profit organization, working with community groups across the country to help them organize new retail food cooperatives as efficiently and effectively as possible. For more information and access to our many resources, visit our website at www.foodcoopinitiative.coop.

Funding for this project was provided by the Blooming Prairie Foundation, through their generous support of Food Co-op Initiative.

Interviews were conducted by the author, spring 2013.

About the author:

Patricia Cumbie is a Minneapolis writer who has worked in the food co-op sector as a member services and marketing director, and for many years was the editor of The Mix: A Twin Cities Natural Food Co-op Publication. She is the co-author of the history book *Growing With Purpose: Forty Years of Seward Community Cooperative*.

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Introduction and Overview

Within food co-op development, infrastructure continues to grow and be strengthened to address the needs of startup groups. However, very little is known about another subset of startup organizing: independent businesses converting to cooperatives, and whether more conversions could be another viable path to growth within the food co-op sector. To date, food co-op conversions are rare occurrences.

Fortunately, two co-op conversions occurred virtually simultaneously in communities on the east and west coasts in 2012 providing the sector a valuable opportunity to compare and contrast their experiences and study their outcomes. The Food Co-op Initiative commissioned this case study of these two independent retail businesses in order to learn more about the process of the change-over, as well as the benefits and challenges of co-op conversions in order to get a better understanding of the value of this kind of organizing and its potential.

Summary Points

1. Support specifically designed to assist the conversion process is minimal.*
2. Conversions require buyers, sellers and financial institutions to have a strong understanding of the needs of cooperative financing.
3. Sellers have to be patient with groups that need time to organize their community, raise capital, and carry out the legal process of conversion.
4. Changing organizational structure and transitioning operations to reflect cooperative best practices, including a chart of accounts, membership records, and management accountability to a board, is an extensive undertaking.

*Three national organizations currently specialize in serving food co-op startups: Food Co-op Initiative, CDS Consulting Co-op and the National Cooperative Grocers Association's Development Co-op. Regional cooperative development centers such as the Cooperative Development Institute and the California Center for Cooperative Development support food co-ops in some parts of the country.



The writing on the wall!



The Research

The purpose of this activity was to find out more about conversion groups, track trends within their activities, and better understand their challenges. The study entailed conducting interviews with key stakeholders (independent proprietors/sellers, the co-ops' founding board members, and its current management) in February and March 2013.

The Case Study Participants

We are grateful for the time and expertise of the following case study participants:

Melisa Clark

Current general manager, Placerville Food Co-op

Alice Cozzolino

Former owner, The Old Creamery, Cummington, MA

Karen Doherty

Current general manager, Old Creamery Co-op

David Harde

Former owner, Noah's Ark, Placerville, CA

Mickey Kaiserman

Founding board member, Placerville Food Co-op

Ruthie Loeffelbein

Founding board member, Placerville Food Co-op

Kimberly Longey

Founding board member, Old Creamery Co-op

Tripp Mikich

Community organizer, Placerville, CA



Old Creamery Co-op

Cummington, MA

www.oldcreamery.coop

Old Creamery Co-op at a Glance

Year business was founded: 1886

Year incorporated as cooperative: 2010

Year doing business as cooperative: 2012

Number of members at opening: 525

Number of members in spring, 2013: 559

Member equity investment: \$150

Cost of total project: \$1.2 million

Member loans: \$215,000

New member equity: \$76,000

Financing: \$676,500

Donations: \$232,000

Number of staff: 26 (six are full time)

Retail square feet: from 1,300 to 1,570 post-renovation

First-year sales: \$1.4 million

Projected 2013 sales: \$1.6 million



Old Creamery Co-op is located in Cummington, Mass., in a small town (population 1,000) in the Berkshire Mountains. The Old Creamery, as it was known before the conversion, has a 100+-year history in the community. When it was founded in 1886, it was a dairy and cooperative creamery owned by local farmers. In the 1930's the cooperative closed, and independent owners purchased the co-op's building. Over the years seven individual proprietors of The Old Creamery continued to serve the community as retail grocers for over 70 years. The current product line at Old Creamery Co-op is both conventional and natural and organic foods. Because of the longevity of the business and its necessity to daily life, The Old Creamery was a critical part of the community, and this was a big factor in the reason for its conversion to a cooperative.

Alice Cozzolino and Amy Pulley were the last independent owners of The Old Creamery, and they had owned the business for 12 years prior to selling it to the cooperative in 2012. They had run the business very much like a community center—it had a café where people could gather



The Old Creamery, prior to the co-op's renovations.

and have food, they hosted live music, sponsored many community events, as well as selling groceries and sundries for the household. Their dedication was legendary, for example, spending the nights in the store during snowstorms so people could still get staples when local rural roads were impassable.

Yet the long hours and limited resources they had to pay for the physical plant problems that came with an old building left them exhausted and burned out. They wanted to sell, but to whom? To them, and the community, the business was so much more than an exchange of goods and commerce. It was a hub of entertainment and village initiatives, and they didn't want what they had devoted their lives to maintaining

to just end. They wanted to preserve something they knew was special to the area Hilltown communities and continue the value-driven approach they had nurtured in the business. Ultimately, they believed that Cummington needed businesses like the Creamery that Cozzolino said could "create more resiliency in our community." Cozzolino and Pulley had known about other cooperatives in the area, including the Berkshire Co-op and the startup River Valley Market. They had seen how well those co-ops built growth and community and decided to investigate cooperation as a way to make The Old Creamery a true communal asset. "As a cooperative, we knew people would be buying into preserving the place and give it the greatest chance to save what we'd created together. We felt we owed it to people," Cozzolino said.

The impetus to convert The Old Creamery into a co-op came from the independent owners themselves.

According to Cozzolino they had a "vague recollection" of an organization called the Cooperative Development Institute (CDI) in South Deerfield, Mass., the Northeast's center for cooperative business development. She called them one day in 2009 out of the blue and she said "they were so hopeful and supportive. Amy and I wept with relief and joy." Thus began their journey as both sellers and boosters for the co-op.

Cozzolino and Pulley organized the first community meeting in January 2010 to assess interest in potentially converting The Old Creamery into a co-op. They wondered; would people embrace

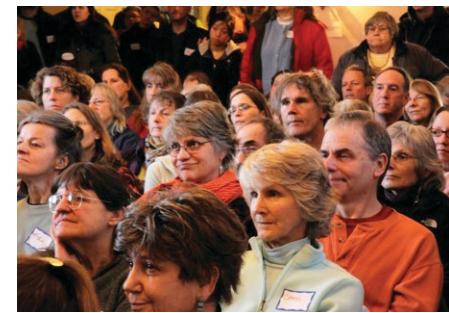


the idea of a co-op? They were truly humbled and astonished when 300 people showed up. “The community response was phenomenal,” said Cozzolino. After that meeting, Cozzolino and Pulley invited several other people from the community to help them form a committee to begin the organizing process. A steering committee of 9 people, including Michael Kalagher and Kimberly Longey, were very instrumental in beginning the process of converting The Old Creamery to a cooperative and engaging the community.

Kimberly Longey has a career in economic development activities in the Berkshire Hilltown area, and had a good idea about what it could take to build community support for the co-op as well as finance it. Her experience as an organizer and developer was invaluable to the co-op’s conversion process. She is currently the Old Creamery Co-op’s board president. “Amy and Alice were running the business with a lot of co-op-like values, so the community had all the benefits without the responsibility,” Longey said.

“As a cooperative, we knew people would be buying into preserving the place and give it the greatest chance to save what we’d created together. We felt we owed it to people.”

Once they got a steering committee organized, the group began in-depth feasibility analysis. This included a market study and a “brain dump” from Cozzolino and Pulley, wherein they collaborated with the group on sharing their business records. “We had a strong base of information,” said Longey, “It was our job to find out what we needed to do for the co-op.” They also contacted other food co-ops in the area and made site visits and met with their boards and management to learn more about governance and operating a values-based business. “We made strong alliances in that process,” Longey said, and she credits those established co-ops (Wild Oats Cooperative, Williamstown, Berkshire Co-op Market, Great Barrington, River Valley Market, Northampton, Green Fields Market, Greenfield, Leverett Village Co-op, Leverett, and the Putney Food Co-op in Putney, Vt.) with unwavering support then and to the present.



Community support was clear at the Old Creamery’s information meeting.



After the data-gathering phase, they concluded in July 2010 that the conversion process looked feasible. They incorporated the co-op, created articles and bylaws, and offered equity shares to the community. They organized themselves into more specialized committees focused on governance, community and business and finance. Their goal was to gain 300 members by the end of 2010. They actually met that goal in six weeks, and were able to “capture a lot of momentum” because of it, according to Longey.

Longey credits some of their success with this because they immediately assembled an email list from the initial meeting of 300 people, launched a website, and kept in constant contact with people. “We’ve trained our member-owners on electronic communication, and it’s been very helpful for keeping the community up to date on our activities,” Longey said.

The founding group also continued to gather relevant data. They did a survey of the current employees of The Old Creamery because they wanted to learn more about the strengths and weaknesses of the operations from the staff. The group also surveyed the members that had joined, as well as the store’s current customers, and did random sampling of survey participants from six neighboring towns. “It emerged that we’d be foolish to buy it and run it as it was. We learned there was a lot of unmet need in our community. The store was basically maxed out,” Longey said.



The co-op group understood that they needed to make their project bigger, and raised their initial fundraising budget of \$800,000 to \$1.25 million in 2011 in order to include renovations and a 200 square foot expansion into their plans. They began to work with an architect on what the co-op could look like.

Longey was very proactive regarding how the co-op planned to finance its expansion plans and the conversion. She met with bankers early on, not to ask for money right away, but to demonstrate the co-op’s plans and the community’s excitement for the project. “We had to educate the bank on the co-op model and help them understand it wasn’t a hippie collective, that we were a professional organization,” she said. It was a strategic move designed to gauge their interest, share information about cooperatives, and encourage them to think about the conversion in a positive light.

Old Creamery provides a community gathering place, served by its excellent kitchen.



The co-op first set up a fiscal sponsoring arrangement with CDI (a registered 501c3 nonprofit) that allowed donors to get a tax deduction on their gifts. CDI in turn kept 5% to cover administration and dispensed the donated money to the co-op to pay for legal costs, site exploration, and communication expenses. “CDI’s sponsorship helped us tap into big community donors and attract gifts at the \$10,000 level,” Longey said. The final tally on the fiscal sponsorship gift campaign was \$160,000 specifically for co-op development, and \$72,000 in other no-obligation gifts. They also raised \$215,000 in member loans and were able to secure \$676,500 in bank financing from Florence Savings Bank in 2012, which was more than they had asked for. The co-op really wanted the Cooperative Fund of New England (CFNE) to be their lender, but they ended up getting better rates from Florence. “It was a disappointment to the CFNE, but the mutual bank had better terms,” she said.

“We had to educate the bank on the co-op model and help them understand it wasn’t a hippie collective, that we were a professional organization.”

It is important to note that the money raised by the co-op, especially the fiscally-sponsored gifts, is an unusual achievement. The Old Creamery Co-op’s success can be attributed to a number of factors. The people on the steering committee, including Longey, are experienced fundraisers. They knew who to ask for resources in their community, and what organizations might be willing to do challenge grants. Additionally, they hired a professional fundraiser, who helped them create a sophisticated fundraising strategy that included a range of ways for people of all financial means to contribute, and holding events with high profile individuals who used their celebrity to help the co-op attract funds. “Everyone can be a philanthropist if it’s important to them,” Longey said. “Giving them the opportunity to give in many different ways helps them do that.”

Nonetheless, Longey noted she felt they did make one financing mistake, and that was they launched a second membership campaign about halfway through their gift campaign, and it led to some confusion. She advised closing any ongoing fundraising campaigns before launching another. Although the financing process went as well as could be expected in the current economy, it still took two whole years to secure the money.



Two years wherein the business was still being run by Cozzolino and Pulley.

Both Longey and Cozzolino said that they were able to work well together during the conversion, but there were still pressures regarding the length and breadth of the process. Cozzolino and Pulley were on the co-op's board helping make decisions to convert their business while still having control over it. They were okay with making decisions about their business on behalf of the co-op, but what would happen if the co-op venture failed? It was an anxiety-provoking thought, but Cozzolino and Pulley just kept the faith that it would all work out. They placed enormous trust in the co-op group. "Having them in the process helped us," said Longey. "But it was also painful at times and a slow-going process."

Cozzolino concurred. They also had some legal and appraisal costs in the process. When the co-op realized it needed a Point of Sale (POS) cash register system to account for member purchases, the system was acquired through a lease agreement with the manufacturer. Cozzolino and Pulley shared the costs of installation, training, and lease and maintenance fees for the \$140,000 price tag, with some nervousness. "We were trying to be generous to the co-op, while limiting costs to Amy and I," said Cozzolino. "But there was rarely tension. We absolutely trusted each other's motivation. It was never chaotic, it was very organized and planned out," she said.

Yet the whole thing was a process of discovery for everyone involved.

Because of the transparency needs of the co-op, the independent owners felt like they were at times "stripped bare" by the process of sharing their financials and formerly private business decisions in order for the group to make critical decisions. "Some private owners would not allow any of that information to be public. But transparency created community buy-in on a deeper level. I wouldn't have done it differently," Cozzolino said. Above all, Longey and Cozzolino said it was important for everyone involved to be respectful and honest, and recognize the sacrifices everyone was making.



Old Creamery owners Alice Cozzolino (left) and Amy Pulley sign the documents and breathe a sigh of relief.

Still, people got tapped out by the process. The store's owners were stretched to the max by selling their business to launch another, and the co-op's founding board members had demanding careers that also required their energy. The capacity they needed as a group to see things through to the legal and financial conversion, much less the operational one, was a huge challenge to everyone involved. "None of us had ever engaged in something like this before. It was hard to get a broad scope of what needed to be accomplished," Cozzolino said.



Often they thought they were close, only to discover other arcane tasks that needed to be completed. For example, in order to transfer the store's liquor license, the board had to convince the state of Massachusetts they weren't up to any "funny business" (the state had insisted that they needed to do background checks on all the owners, not understanding there were 500 of them). Convincing the state to grant the license transfer took 4 months, (and according to Longey, was the equivalent of getting a law degree in state liquor regulations). The co-op's board persevered in order to set a precedent for any other potential co-op conversions in their state.

On November 7, 2012, the Old Creamery opened its doors officially as the Old Creamery Co-op. A month before, the co-op had hired Karen Doherty to be general manager. She had experience in running a cooperative as the general manager of the Blue Hill Community Market & Café in Blue Hill, Maine. She'd also worked with the startup MOON Co-op in Oxford, Ohio, and was familiar with both retailing and creating new systems from scratch. Her experience in food co-op retail has been invaluable to the transition, but it hasn't been a process without challenges. Merging a formerly independent business with standard cooperative retail practices is a big undertaking, even for someone with a lot of experience.

The co-op is currently in the midst of expanding walls for a produce and bulk department expansion, going from 1,300 to 1,500 retail square feet, and doing a renovation and reset of the entire retail environment. The co-op felt it was necessary to reorient the shelving and the cash registers in order to create better flow and generate more sales and traffic in the store. In addition to these major physical plant changes, other big changes have to happen simultaneously. The co-op installed the new POS system, which staff had to be trained to use. Getting the Electronic Benefits Transfer (EBT) machine switched over to the co-op to accept food stamp payments took 3 months of state red tape. Besides the day-to-day operational systems customers interface with, the general manager has to shift the staff's culture to one of greater empowerment and accountability. Previously, the two owners were in charge of all departments and kept track of profitability using general accounting. Now Doherty needs to establish department heads and a management team where none existed before. Additionally, she needs to introduce margin pricing and the tracking of purchases/ingredients in all departments, as well as set up a new co-op chart of accounts. In



Old Creamery Co-op's General Manager
Karen Doherty

the long term, the co-op also wants to adapt the product line to focus on more local and natural products in keeping with the co-op's goals of health and sustainability. "We are engaging the store in all ways co-ops engage," said Doherty.

“ Aligning an existing business with co-op practices is a bigger task than starting from scratch. Even just asking shoppers ‘are you a member of the co-op?’ is a big change for the staff and customers. ”

One of the benefits of the Creamery conversion is that the community is incredibly supportive, and that its success is more predictable based on its past. Doherty said that the other startup she worked at struggled to capture its customer base after it opened. "But aligning an existing business with co-op practices is a bigger task than starting from scratch," Doherty said. "Even just asking shoppers 'are you a member of the co-op?' is a big change for the staff and customers. That change has been difficult for some."

She also acknowledged that it was a "tricky dance" working with the previous owners together in the store. The previous owners stayed on for about a month to help with the transition and in retrospect it was challenging for both parties. The staff's primary relationship was with the former owners because of their long working relationship, but they were no longer "in charge." At times it was awkward.

Doherty's feedback for anyone considering a co-op conversion is to give the operations plenty of time to transition its vendors, credit card processing, and membership database, in order to have the basics functional on day one. "I think the biggest challenge I face is I have so much on my plate. I wish I had a few more hands," Doherty said.



Volunteers played a big role in organizing the new co-op that took over Old Creamery. (Left to right: Sylvia Snape, Shirley Todd, Susi Westwood, Helen Larkin, and GM Karen Doherty.)



However, she and everyone else interviewed on behalf of Old Creamery Co-op believes that the co-op's future looks promising, despite the inherent challenges of overhauling an existing enterprise to conform to co-op business practices. They are working diligently to become a fully participating member of the food co-op sector, with the goal of reaching \$2 million in annual sales and joining the National Cooperative Grocers Association. However, they feel like they could really use the NCGA membership now while they are trying to get established. The board is getting training for transitioning from a working board to a governance board. "I think the community made the right decision in deciding to take over the business. This is a co-op with a bright future. It has all the elements, a strong staff and board and a supportive community," Doherty said.

Longey noted that if the sector is going to put resources into conversions, cooperators need to understand that "they can't be replicated." Each one has a unique set of circumstances. There are things that she also thinks the sector could consider, including a loan fund that could lend money or hold assets. "People take time," Longey said, and she thinks a dedicated fund would help shorten the time it takes to get financing. She also thinks that if the sector wants to support conversions, it could put more resources into assisting operational transitions, rather than always relying on the goodwill of nearby established co-ops for help.

"It would have been easier to start from scratch," admits Longey. "But what's better? To fix up an old house or build a new one? When you consider that kind of analogy it depends on what you want. Momentum would have been lost if we closed The Old Creamery, and our ability to attract capital would have been harder." Not only that, she said, "This is our way to preserve our history."



Some of the people that made the Old Creamery Co-op transition a reality. (Left to right: Kimberley Longey, Patty Kimura, Michael Kalagher, and Hattie Plehn.)



Old Creamery Co-op Summary Points:

Consulting Services Used

- CDI provided fiscal sponsorship, consulted on initial community meeting, and carried out preliminary and casual mentoring.
- FCI provided toolboxes, websites and webinar resources, answers to questions, and assistance with a \$10,000 grant.
- Professional consulting services from within their community including fundraising and business planning.
- Other food cooperatives in region provided advice, tours and operational assistance.

Circumstances Favorable to Old Creamery Co-op Conversion

- Enthusiastic sellers fully supported co-op idea.
- Engaged a supportive community through skilled community organizing.
- Tapped into resources from CDI, FCI, peer-to-peer sharing, free toolboxes.
- Followed due diligence in feasibility of conversion.
- Capitalized on 100+-year old business tradition.
- Created strong business plan.
- Secured adequate financing for plans.
- Attracted qualified general manager.
- Got ongoing support from existing food co-ops in the area.

Challenges to the Old Creamery Co-op Conversion:

- Cooperative way of business is very different from private ownership in structure, transparency, and accountability to the community it serves.
- Not enough guidance or education for what to expect during conversion process.
- Financial institutions don't understand co-op business model.
- State of Massachusetts bureaucracy slowed legal modifications to cooperative.
- Lack of extensive planning for operational transitions.
- Not yet eligible for NCGA membership which would provide access to lower cost of goods and operational support.



Placerville Natural Foods Co-op

Placerville, CA

www.placervillecoop.org

Placerville at a Glance

Year business was founded: 1993

Year incorporated as cooperative: 2010

Year doing business as a cooperative: 2011

Number of members at opening: 256

Number of members in spring, 2013: 716

Member equity investment: \$300

Cost of total project: \$515,000

Member loans: \$77,000

New member equity: \$33,000

Financing: \$100,000

Number of staff: 22

Retail square feet: 5,700

First-year sales: \$1.4 million

Projected 2013 sales: \$1.6 million



Placerville Food Co-op is located in Placerville, Calif. (population 10,000) which is in northern California within a 30 minute drive to Sacramento. The town of Placerville was established during the Gold Rush in the 1840's, and named for its placer gold deposits. For many years the town functioned as a hub for mining, and an interesting historical footnote is that it used to be called Hangtown, because it was also a focal point of frontier justice and frequent hangings. Today Placerville is known as a very livable historic city with agreeable weather, and this has made it a magnet for people seeking to escape expensive urban areas, like San Francisco, in search of a better lifestyle. It is also now known for its wine production and has many notable wineries in the region that are thriving in the foothills of the Sierra Nevada Mountains.

The co-op is situated on Placerville Drive, one of the main shopping streets in town close to the only Home Depot in El Dorado County. Before the co-op conversion in 2012, the business was known as Noah's Ark, a natural food store owned by David Harde and Toby Landis. Harde was a local organic farmer who was instrumental in founding the Placerville Farmers Market



in 1983 and a co-founder of Sierra Gold, a chapter of the California Certified Organic Farmers organization for the Sierra foothills region. Harde opened Noah's Ark in 1993 in order to offer the community year-round access to fresh and natural food, and provide a retail outlet for the produce he grew on his farm. In 2006, he had expanded the store and modernized the exterior. In 2008, Harde decided to sell the store and focus his energies on growing wine grapes on his farm. He is still peripherally involved in the Placerville Natural Foods Co-op as a member and a shopper at the store.

A local yoga practitioner, Bill Scrivani, and Noah's Ark's store manager, Melisa Clark, expressed interest in the business in 2008 and potentially converting it to a co-op. But the \$2.9 million offer for sale was too expensive and they dropped the idea. Two years later, Harde had reduced the price in response to the declining economy, and was willing to negotiate, so Scrivani and Clark began to look into forming a cooperative in order to pool community resources to purchase it.

In March 2010, Scrivani and Clark called a public meeting to assess the potential of forming a co-op. The meeting attracted a crowd of 200 people who were very interested in supporting Noah's Ark's conversion into a cooperative. Chris Maher, general manager of BriarPatch Co-op in Grass Valley, also spoke at the meeting. After that meeting, the group formed a steering committee that attracted the talents of Mickey Kaiserman, a financial and managerial consultant, and Ruthie Loeffelbein, active in land use planning and social justice issues. The steering committee created a mailing list, a brochure, and did a survey to gauge community interest. The committee also began taking steps to incorporate as a co-op because it wanted to buy the business right away.

"People in town wanted a place for local, sustainable products," said Kaiserman, who is currently on the co-op's board and chief financial officer. Otherwise people wanting access to natural foods would have to drive to Folsom or Sacramento. "The store is a big benefit to people who want to buy local and organic natural foods in Placerville," he said.

Even with the price reduced by half at \$1.4 million, the group knew it was a very big undertaking for a barely established group. "The building was two floors, had an elevator and covered parking," said Kaiserman. The store was overbuilt and a look at the seller's finances showed that the store



The Noah's Ark storefront before Placerville Co-op took it over.



had been losing money. They quickly learned financing would be an issue. “We found we couldn’t secure a loan from a local or national commercial bank for the store’s financial requirements. The banks just didn’t want to loan to a cooperative retail food store without personal guarantees and at least two years of operating results. The banks were not familiar with co-op ownership structure,” he said.

Harde reached a decision to do a lease agreement with the co-op (which dropped the price to around half a million) if it purchased the business and its inventory. Harde had a lot of debt and a mortgage on the building, so whatever deal he worked out with the co-op had to assure that he would come out ok financially. “He was supportive of the co-op, but he had his own financial needs,” said Ruthie Loeffelbein, the co-op’s current board vice president. The co-op put together a letter of intent to buy the business and lease the building, but negotiations for purchasing the business dragged on for a year. Loeffelbein attributes this in part to the real estate agent both sides worked with who could be difficult in negotiations. “I’d recommend co-op groups work with a co-op supporter or someone who knows co-op real estate,” she said.

Meanwhile, the steering committee went on to incorporate and establish articles and bylaws, and by October 2010 they were completed. The group contacted the California Center for Co-op Development (CCCD) to get contacts for legal advice during the process, and also apply for a \$12,000 USDA rural development grant, which they got. The FCI also awarded them \$10,000 grant money for the market study and funds to attend a CCCD conference. They also talked to cooperators at Davis Food Co-op, BriarPatch and Sacramento Natural Foods to learn more about co-op operations.

After getting the results from the market study, they believed the information they received was enough to go ahead with the project. “We never really seriously considered doing a startup,” Loeffelbein said, because they believed most of the elements they needed for their co-op were in place with an already existing business. Why recreate something that had already been started? The challenges it came with—being overbuilt, for example—would be something they trusted they could tackle if they could get the deal done.

While the co-op development groups “were no end of help” according to Loeffelbein, the Placerville group was hamstrung by their inability to secure



Members of the Placerville organizing board met with Food Co-op Initiative advisors. (Front row: Jake Schlacter (FCI), Laura Owens; second row: Betty Albert, Pam Roberts, Mickey Kaiserman ; third row: Ruthie Loeffelbein, Bill Scrivani; back row: Stuart Reid (FCI), Melisa Clark (GM).)



financing, from both banks and their community. The co-op set their equity stock at \$300, the maximum allowed under California law. Initially they had 200 members join, but not all were fully vested, opting to pay their \$300 stock purchase through \$25 payment plans over 3 years, resulting in lower member equity totals (they closed their deal with \$33,000 in member equity). They did donation drives, tabling in front of the store, and hosted locavore dinners to generate excitement for the co-op. Their member loan goal was originally \$448,000 and the co-op group raised only \$77,000 in member loans. Commercial bank lenders continued to reject them.

“We never really seriously considered doing a startup. We believed most of the elements we needed for our co-op were in place with an already existing business.”

David Harde remained active in the management of his store while the Placerville Natural Food Co-op got organized and sought financing. He was glad that “all the things we established and cultivated as owners,” would be perpetuated in a co-op store, but he found the process “ambiguous and difficult.” What Harde wanted most of all was a reliable buyer for his business, it didn’t matter if it was a co-op, but selling to the co-op appeared to be his best and maybe only option. Like Cozzolino and Pulley from The Old Creamery, he too feared that the co-op organizing effort might fail, and that the repercussions would be grave.

“For well over a year my existing customers kept asking me, ‘What is a co-op? What will change?’ and at times the energy of the people working for me went toward working to form a co-op,” Harde said. “I wanted to support them, but I also worried they were scaring away other buyers.” He was concerned about the co-op’s ability to get funding and that the group seemed loosely structured—the deal could fall apart at any time. Harde was also anxious that the co-op would decide not to pursue the purchase after all and set up shop as a competitor instead. He felt like the whole process required a “measure of patience and faith” and that he had to be a participant in it, whether he wanted to be or not. Ultimately, he decided to do what he could to be supportive of the co-op in order to sell the business to them.

The conversion group had their own set of fears that Harde would cut his losses and close Noah’s Ark, and that they would lose the momentum gained by acquiring a going concern.



Harde and the co-op ended up agreeing to a rather complicated final transaction of leasing the building on a triple net basis for 5 years with options to extend, and a right of first offer to buy. With only \$68,000 down and no line of credit, they took over Noah's Ark on October 29, 2011.

The whole process for establishing a co-op concurrent with purchasing a business was a huge educational experience for the founding group. They wanted to see the co-op through, but outside of Kaiserman, had little relevant business experience. This took its toll.

Kaiserman is up front about the challenges the group took on by opening an undercapitalized co-op venture, but they felt like they were running out of time and options, so they went ahead and took the calculated risk. Loeffelbein said, "We went into it undercapitalized, not idiotically, but we really wanted to get into the store." They've been working diligently since the conversion to solve some of the big issues that threatened the co op's solvency.

“ Managing a store for an independent owner is way different than for a co-op. The co-op has all these constituencies, not only the staff, but the board, volunteers, the members, the customers, the general public. Running a co-op is like conducting an orchestra. ”

Without adequate working capital, the inventory levels were too low, and the store, which is too big for the level of sales it generates, is under-stocked. Building sales and attracting new customers has been slow going, because the Placerville community's perception of the co-op is still evolving. Internal and external membership systems are weak. The co-op's board is still learning its governance role, and current management is inexperienced regarding food co-op retail practices. "All the altruistic things we want to see happen are contingent upon the business doing well. It's been a difficult task," Kaiserman said.



Ruthie Loeffelbein stops traffic for the Placerville Co-op's opening.



Luis Sierra from the California Center for Cooperative Development congratulates GM Melisa Clark.

Melisa Clark is the store's current general manager, and she said the learning curve to put into practice co-op retailing has been steep. "You think you are getting handed a baby, but what you're really getting is a multi-armed octopus," she said. Clark used to manage Noah's Ark, and was asked to step in as the general manager when the person who was initially hired for the job was asked to leave. "Managing a store for an independent owner is way different than for a co-op. The co-op has all these constituencies, not only the staff, but the board, volunteers, the members, the customers, the general public. Running a co-op is like conducting an orchestra," she said. Her former responsibilities at Noah's Ark didn't include preparing financials or working for a board. Clark said she is not sure she's the best fit for managing the co-op, but she does have insight into the business and its history to help it through the conversion.

“Because we were independent we don’t have the co-op culture. We know we need to grow our community, but we don’t know how. Educating people about the co-op and how that benefits the community is something we struggle with.”

As Clark works on transitioning operations, she is learning as she goes about the unique features of cooperation, including the co-op's business relationship to its members. "Because we were independent we don't have the co-op culture," she said. "We know we need to grow our community, but we don't know how. Educating people about the co-op and how that benefits the community is something we struggle with."

Since the conversion, both the board and management have taken advantage of training opportunities offered through CDS Consulting Co-op and their CBLD (Cooperative Board Leadership Development) Program to gain more knowledge about cooperatives. "We've managed to do okay, but with more professional training I know we can be more successful," Clark said. She



noted that one of the operational challenges of a conversion is that you get a fully functioning store and all the pressures that go with running it while you learn how to transition it to a co-op.

The board has also had its challenges. “It’s probably a character of our own group,” but Loeffelbein said that their development has been chaotic, too. “We’re not as organized as we should be. We’re still working on it. We’re in transition between being a steering committee and policy governance board.”

Despite the steep challenges at Placerville Natural Food Co-op, positive things are happening. The co-op got a \$100,000 loan in early 2013 from the Northern California Community Loan Fund (NCCLF), which gives the co-op more resources to work with as they continue to improve their systems. (Getting the loan required Harde, who had unsecured loans, to go into second position to the NCCLF loan, something he felt like he had to do to demonstrate support for the co-op.) Sales are inching up every month since September 2012, and the co-op is ever-closer to breaking even. The co-op is also working on recruiting more members and getting current members fully vested. For a town of 10,000 with a newly established food co-op, their current membership of 716 demonstrates growing competence in recruitment. They’ve also brought in more local vendors in an effort to attract customers and to nurture the local economy (46 vendors now vs. 10 before), something Noah’s Ark didn’t cultivate because Harde’s farm was the business’ main local vendor. “When you consider all the things we don’t have, and yet we’ve managed to stay in business, that’s a financial triumph,” Clark said.

The Placerville Natural Food Co-op group found that the professionals involved in supporting co-ops, including FCI, CDS CC and CCCD provided resources they’ve used that have been very helpful. But like the Old Creamery Co-op, they too said they have a need for a co-op fund that would help finance the conversion so things could happen faster, or at the very least offer a line of credit. Loeffelbein noted that there was no peer or person they could talk to for advice who had been through a co-op conversion.

Placerville Natural Food Co-op also has a goal of joining the NCGA, but feel stymied by the requirements to become a member during a time when they believe membership would provide a lot of benefit.



Some of Placerville Food Co-op's first customers head to the checkout lanes.



Despite all they still need to accomplish, has the conversion been worth it? Apart from the former owner of Noah's Ark, everyone interviewed connected to the Placerville Food Co-op gave an unqualified yes. The people involved in the co-op believe that things are changing for the town of Placerville, where people are actively interested in creating the kind of community they want to live in—one that's more inclusive and supports healthy living. The co-op is on the cutting edge of that trend. "It's been mostly rewarding," Loeffelbein said. "We're moving slowly in the right

direction. What we did is working, but not without difficulty." She said conversions and whether they can be considered worth it or not, really depend on the specific situation. The Placerville Natural Food Co-op group believes they made the right choice.



Placerville Co-op's produce department features the local bounty.



Placerville Natural Food Co-op Summary Points:

Consulting Services Used

- CCCD consulted on initial community meeting, offered board and staff training, and provided a \$12,000 USDA grant to fund a market study.
- FCI provided toolboxes, websites and webinar resources, answers to questions, and assistance with two \$5,000 grants.
- CDS CC conducted the market study, and consulted with them on co-op operations.
- Other food cooperatives in the region provided advice, tours and operational assistance.

Circumstances Favorable to Placerville Food Co-op Conversion

- Seller willing to work with group developing co-op idea.
- Tapped into resources from FCI, CCCD, and CDS Consulting Co-op.
- Followed due diligence in feasibility of conversion.
- Seller provided financing through lease arrangement.

Challenges to Placerville Food Co-op Conversion:

- Cooperative way of business is very different from private ownership in structure, transparency, and accountability to the community it serves.
- Not enough guidance or education for what to expect during conversion process.
- Financial institutions don't understand co-op business model.
- Steering committee challenged by lack of business experience.
- Financial investment by co-op member-owners was weak.
- Proceeded with conversion despite being undercapitalized.
- Co-op management inexperienced in food co-op retail operations.
- Lack of planning for operational transitions.
- Not yet eligible for NCGA membership which would provide access to lower cost of goods and operational support.

Conclusion

Evaluation of Conversions

The development stories of the Old Creamery Co-op and the Placerville Natural Food Co-op share many similarities, in terms of the length of time it took their founding groups to organize a conversion (two years), the reasons for doing it (to preserve an existing grocery store for the community), and the subsequent operational difficulties they've encountered. But they are also different enough regarding community support and financing, management experience, and cooperative familiarity, that they provide instructive contrasts that assist with an in-depth analysis of co-op conversions. Based on the experiences of these two co-ops, we readily understand the following are the overall current challenges to the conversion process in the food co-op sector:

- Organizing community support and adequate capital takes time; often more than the seller wishes to allow. Rushing the process leads to future problems.
- All the food co-op development resources, while generally very useful, are geared toward startups, not conversions. There's no model or template for conversion groups to utilize.
- When you acquire an existing business, you acquire many of the problems it may have had. (Less than ideal site, old equipment, employee morale, insufficient customer support, etc.)

Organizing Community and Raising Capital for Co-op Conversions

- Community organizing and ownership buy-in is critical.
- Don't underestimate the value of a skilled steering committee.

One circumstance that was very favorable to the Old Creamery Co-op's conversion project is that the community support for it was very strong, from the former independent owners, to the co-op's founding board, the local lenders and the town at large. The co-op was able to capitalize on the 100-year history of the business and the goodwill that had been generated by Cozzolino and Pulley during their years as owners. Their commitment was a big part of the success of the conversion. They carried out a vision for the business while they owned it that demonstrated co-op-like values. In addition, the steering committee members had an unusual talent pool regarding fundraising and community organizing ability.



The co-op conversion in Placerville didn't enjoy the same level of commitment from its community, lenders, or the previous owner, and this led to a conversion that was equally complex but a bigger struggle to carry out. While they were not at cross-purposes with any individual or group, every step of the way met challenges. It took them months to incorporate, a year to negotiate their lease, and their capitalization efforts were weak because they didn't know how to sell the concept of a co-op to potential stakeholders. The people on the steering committee worked very long and hard, but their inexperience with business financing and fundraising hamstrung their efforts. They opened despite being undercapitalized.

Financing Package Comparison

Financing	Placerville	Old Creamery
Gifts and Grants	\$ 10,000 FCI \$ 12,000 CCCD & USDA	\$ 25,000 FCI & USDA \$160,000 CDI Fiscal Sponsor \$ 72,000 Donations
Member Equity	\$ 33,000	\$ 76,000
Member Loans	\$ 77,000	\$215,000
Secured Debt	\$100,000 NCCLF (obtained one year after opening)	\$536,500 Florence Savings
Seller Financing	\$119,000 Equipment lease \$38,000 Note for business \$57,000 Note for inventory (Co-op also assumed \$60,000 trade payables)	\$140,000 (offset by equipment lease)

The takeaway is that community organizing and financing ability really go hand-in-hand, whether a co-op is established, a new startup or conversion. If the community support isn't there, it's going to be nearly impossible to demonstrate potential success and convince conventional lenders to take the risk. Both conversion groups suggested that the food co-op sector could do more to help financially assist their efforts in either community fundraising or with lending.

The Old Creamery Co-op group was unusually fortunate in this regard, and Placerville's experience may be more typical. By ensuring a community is able to support the co-op, it portends fewer problems for the co-op as an organization. This is something we already understand about startups, but because a conversion comes with an established customer base, organizers may be lulled into believing that financial backing and patronage is already in place when it may not be.



Development Assistance for Conversions

- The food co-op sector needs to organize better support/strategy if they deem these projects worthy.
- Conversions require a lot of patience and willingness to be transparent, especially on the part of the seller.

Everyone interviewed for the case study was quite clear that while they found the resources available useful, they also felt a profound lack in terms of working with people familiar with the challenges of co-op conversions. Converting an existing grocery co-op comes with some of the same challenges as new startups, but remaking an independent business affects everything from governance, management, operations, to community relations. Both Old Creamery and Placerville Natural Food Co-op groups relied a lot on their instincts as well as adapting various resources to carry them through.

A lot of questions about the process that they needed help to address included: How do you organize a startup group legally to purchase an existing business and convert it? What do you tell current customers, employees and the community about the conversion while the owner is still in place? How do you educate organizers and community about the co-op difference without alienating the owner? How do you transition management and operations once the deal is final? For an independent owner, like David Harde in Placerville, who just wanted to sell out and turn over the keys, the process of waiting for a group to build a cooperative infrastructure while holding on to his business in order to sell it to them required a lot of patience and uncomfortable transparency. There is an emotional component to these conversions that cannot be overlooked. The owners have poured their own lifeblood into the operations over the years, and they want to be respected in a process that acknowledges their sacrifice and hard work. Harde said that he could have used some advice from co-op professionals on how to manage that process and what to reasonably expect.

Acquiring an Existing Business as a Startup Group

- Conversion groups are challenged or bolstered by whoever is selling the business.
- Planning for the operational change-over needs to be planned much more systematically.
- There needs to be an early recognition in conversion groups that just because you have an existing store in your sights does not mean you have a co-op.



One of the potential benefits of a co-op conversion—an already existing operation—actually turns out to be one of its biggest challenges. Taking over an existing business, one that may or may not have been run well, and converting it to a co-op is a massive undertaking. As Karen Doherty, manager of Old Creamery Co-op said, it is actually harder to convert to co-op operations than start new. Establishing a co-op chart of accounts, working with a board, ensuring accountability, educating staff and community, and transitioning all of these components is a process of ripping everything apart and putting it back together. For someone like Melisa Clark, whose prior management of Noah's Ark didn't involve any of those things, the learning curve is steep. The years that it might take both operations to achieve operational stability may give an indication of the value of conversion—and this may be something we understand better in a few years.

Overall, converting operations to a cooperative points to the ever-present need in the food co-op sector for comprehensive management training, and the stark differences between the co-op business model (inclusiveness, transparency) and the standards of private business ownership.

Final Considerations

The purpose of this case study is to highlight important issues in co-op development and what we have learned from co-op conversions through our research. After reviewing the conversion process of Old Creamery Co-op and Placerville Natural Food Co-op, the issue for food co-ops and individuals and groups that serve them is to address the value of co-op conversions. Co-op conversions are still relatively rare, but with strategic initiatives, mentoring and guided support could conversions be a viable avenue for growth? Or would the sector be better served by existing food co-ops acquiring targeted independent operations and converting them, thereby utilizing the benefits of established operations, knowledgeable management, and an existing co-op culture?

Our next steps may include finding ways to engage the broader sector about these considerations and identifying areas of further study. The intention for distributing this report is to share what we have learned and to take a leadership role in exploring collaborative approaches to addressing the ongoing issues of startup co-op development within our sector.



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