



## **The Pulaski Pike Market: From Charity to Systemic Change, Part A**

Social entrepreneurship is a process by which citizens build or transform institutions to advance solutions to social problems, such as poverty, illness, illiteracy, environmental destruction, human rights abuses and corruption, in order to make life better for many. (Bornstein & Davis, 2010, p. 1)

The heart of social entrepreneurship is a willingness to try out ideas that are helpful to others. Social entrepreneurs are action researchers: they learn primarily through experimentation, not just by relying on theory. (Bornstein & Davis, 2010, p. 82)

### **Introduction**

In 2007, the Board of Directors of the Food Bank of North Alabama (FBNA) and its Executive Director, Dick Hiatt, reached a crossroads. The Food Bank, a 501(c) 3 nonprofit charity, was one of eight food banks located throughout Alabama<sup>1</sup> charged with the procurement and distribution of food to those in need. Despite the Food Bank's respectable impact—providing food to approximately 89,000 individuals through over 200 partner agencies across North Alabama (America's Second Harvest, 2006, pp. 6-7)—the agency's leaders wrestled with how, or even if, they could adopt a proactive strategy to mitigate, if not eliminate, the sources of poverty that created the need for charity in the first place.

Dick Hiatt and FBNA board members explored these questions with community leaders, including Tami Jordan, Director of a neighborhood association called the Terry Heights Hillandale Organization; Bill McDowell, Executive Director of a faith-based nonprofit called Second Mile Development; and staff members from the City of Huntsville's Community Development Department. A Steering Committee committed to community asset-building and social entrepreneurship emerged and developed a plan to alter the dynamic of poverty and achieve systemic change by creating new jobs locally vested in the Terry Heights Hillandale community, an economically distressed neighborhood of Huntsville, Alabama (see Exhibit 1 for demographic information). This team of social entrepreneurs worked to establish a worker cooperative grocery store located within the Terry Heights Hillandale community that would create jobs and offer residents, many of whom lacked reliable transportation, convenient access to healthier food

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<sup>1</sup> See <http://www.alfoodbanks.org/>, cited 24 October 2010.

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*This case was written by Professor John R. Whitman and Kathryn Strickland as a basis for class discussion rather than to illustrate either effective or ineffective handling of an administrative situation. Funding was provided by Equal Exchange and The Lewis Institute for Social Innovation at Babson College.*

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choices, including fresh produce grown by local farmers. To develop and implement this initiative—called the Pulaski Pike Market (PPM)—the partners recognized the unique advantages of a collaboration that married public sources of programmatic financial support and private sources of capital to launch an entrepreneurial enterprise committed to social change beyond charity.

This case study documents and evaluates the Pulaski Pike Market project. The case study was developed following Maxwell's guidelines for qualitative research (Maxwell, 2005). As indicated by the quotation that opens this case study, the partnership planned and undertook the Pulaski Pike Market project as an action research project. While there are various approaches to conducting qualitative research, *action research* is one that engages individuals who are trying to solve a particular problem in the research itself as a means by which to achieve their aims (Whyte, 1991). As described by Patton (2002, p. 221), who in turn draws on Whyte:

Action research aims at solving specific problems within a program, organization, or community. Action research explicitly and purposefully becomes part of the change process by engaging the people in the program or organization in studying their own problems in order to solve those problems (Whyte 1989).

Thus the reflective evaluation of the performance of the project and insights into its successes and limitations to date are drawn directly from the key participants in the project—the members of the public/private partnership established to develop the Pulaski Pike Market.

The case attempts to provide both theoretical and practical value to scholars and students of nonprofit organizations, cooperatives, and public policy, as well as to practicing executives of other organizations who may be interested in developing similar public/private partnerships to address social needs. Each such audience may read the case from a different perspective. Students in particular may wish to question what is the best organizational model for the venture: a cooperative, a traditional for-profit venture, or a nonprofit organization. Policymakers may question what can be learned from this example in a way that informs revised or improved policies to promote community economic development. Practitioners might ask how this narrative can encourage and guide innovative community development, and at the same time reveal potential pitfalls that could be avoided.

The case is presented in two parts—A and B. Part A is descriptive. It opens with a depiction and history of the Terry Heights Hillandale neighborhood. The initiative is then described in detail using material drawn from the project's report to the National Institute of Food and Agriculture, a source of programmatic funding. Part A closes with the challenges faced in solidifying a deal to finance the construction of the buildings necessary to house the cooperative grocery store and a distribution center for local farmers.

Part B is evaluative. The B case reviews the actual financial proposal used to secure construction financing and provides an evaluation of the PPM project by key members of the public/private partnership. The B case closes with the challenge of evaluating a bold social initiative that promises to move a community from charity to systemic social change.

The descriptive portion of this case was principally prepared by Kathryn Strickland in her capacity as Community Food Security Director of the Food Bank of North Alabama and lead facilitator of the Pulaski Pike Market project. The evaluative section of the case was largely prepared by John R. Whitman, Ph.D., Lecturer in Entrepreneurship at Babson College. Babson College and Equal Exchange, a fair trade cooperative, jointly funded this case.

## Pulaski Pike Market Project Description

### Trade Area: All the Hallmarks of an Urban Food Desert

Near a downtown intersection of Huntsville, Alabama, the site of the Pulaski Pike Market (PPM) was a 1.25 acre tract of vacant land on the southeast border of the Terry Heights Hillandale community (see Exhibit 2 for map and photos). Bordered by three public housing developments, the Terry Heights Hillandale neighborhood had all the hallmarks of an urban food desert:<sup>2</sup>

- Incomes well below half of Huntsville's median household income;
- Residents lacking reliable transportation;
- The absence of a full-service grocery store within the neighborhood's borders;
- A demographic illustrating the city's ethnic divide; and
- Rates of diet-related diseases well above national averages.

Home to NASA's Marshall Space Flight Center and Redstone Arsenal, Huntsville was considered the economic engine of North Alabama; however, despite the City's expanding national defense and aerospace industry, segments of the population were eclipsed by this rapid high tech growth, resulting in a dichotomy of prosperity and poverty.

In the Terry Heights Hillandale neighborhood, the 2007 median household income within .6 mile of the proposed PPM was \$13,558 per year (Suassuna, 2008). This statistic strongly contrasted with the \$63,800 median household income reported for the City of Huntsville during the same period.<sup>3</sup> During the 2006–2007 school year, the number of Terry Heights Elementary School students eligible for free or reduced price meals was 97%—more than double Huntsville's school system's average (Alabama State Department of Education, 2007).

This vast economic disparity also mirrored an ethnic divide. Terry Heights Hillandale was a predominately African American neighborhood. While Huntsville's overall population was 65% white (Chamber of Commerce Huntsville AL, 2000), within .6 mile of the proposed PPM, the white population dropped to 6% (Suassuna, 2008).

A study commissioned by the City of Huntsville's Community Development Department (CDD), and conducted in collaboration with Zogby International, highlighted the employment needs and health concerns of the Terry Heights Hillandale community. Before the 2008 national economic downturn, respondents to the study survey reported a 13% unemployment rate—more than double Huntsville's average. Twenty-one percent of participants reported that they or a member of their household had been diagnosed with diabetes—a rate almost three times the national average.<sup>4</sup> Forty-two percent reported that they or a household member had received a diagnosis for hypertension, diabetes, or high cholesterol. All

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<sup>2</sup> According to the Centers for Disease Control and Prevention, "Food deserts are areas that lack access to affordable fruits, vegetables, whole grains, low-fat milk, and other foods that make up the full range of a healthy diet." Source: <http://www.cdc.gov/features/fooddeserts/> (accessed 24 January 2011)

<sup>3</sup> Chamber of Commerce, Huntsville, AL. "Population and Income Growth, 1990–Current." Source: [http://www.huntsvillealabamausa.com/new\\_exp/community\\_data/demographics/growth.html](http://www.huntsvillealabamausa.com/new_exp/community_data/demographics/growth.html) (accessed April 2009).

<sup>4</sup> Department of Health and Human Services Centers for Disease Control and Prevention. Data and Trends: Age-Adjusted Percentage of Civilian, Noninstitutionalized Population with Diagnosed Diabetes, by Race and Sex, United States, 1980–2006. Source: [www.cdc.gov/diabetes/statistics/prev/national/figraceethsex.htm](http://www.cdc.gov/diabetes/statistics/prev/national/figraceethsex.htm) (accessed April 2009).

three diagnoses portended severe dietary concerns and underscored the need for access to healthy food choices including fresh fruits and vegetables.<sup>5</sup>

Neglected by conventional retail services including large grocery chains, Terry Heights Hillandale did not have access to nutritious food choices within the neighborhood's borders. Lacking reliable transportation and thus dependent upon public bus routes or taxi rides, many Terry Heights Hillandale community members found shopping, particularly grocery shopping, difficult and expensive. As a result, many residents purchased their groceries from small, conveniently located "quick stops" that typically have unhealthy food selections and high prices.

### Site History: "Urban Removal"

According to Dr. Darryl Gurley, a member of the PPM's Steering Committee and long-time resident of Terry Heights Hillandale, the neighborhood flourished prior to the late 1960s when the era of Urban Renewal took hold in Huntsville.<sup>6</sup> Dr. Darryl Gurley's grandfather, Sidney Gurley, subdivided his vegetable farm in 1951 and founded what would become a key southeast section of the Terry Heights neighborhood. Sidney Gurley was the first African American to annex property into the City of Huntsville and develop a planned community.<sup>7</sup>

Ms. Carla V. De Shields, a member of the PPM Steering Committee, the Vice President of the Terry Heights Hillandale Organization, and also long-time resident of the community, described how her family built their home in Terry Heights in 1957. Ms. De Shields' family was forced to move from their original home to Terry Heights after the City exercised eminent domain to construct a main thoroughfare. Ms. De Shields called this period of the 1950s, "The first 'urban removal' in Huntsville" (Carla De Shields, personal communication, 22 November 2010). According to De Shields, many African Americans moved to the Terry Heights community during this time because so few landowners would sell property to African Americans. As a result, she noted, Terry Heights Hillandale became home to many African American teachers, doctors, and other professionals. Eventually a thriving African American business sector operated along Pulaski Pike Avenue, the eastern boundary of the neighborhood.

As indicated by photographs archived by Ms. Linda Allen, the former Historic Planner of the City of Huntsville, at least three neighborhood grocery stores existed in the community – one directly across the street from the PPM's site. In the late 1960s, the City of Huntsville again exercised eminent domain. It acquired these tracts of land as part of a roadway improvement plan. Many of the businesses folded, and the City demolished the existing structures. The PPM site was purchased by the City during this second wave of "urban removal." The tract remained vacant ever since. In many respects the PPM project promised to be an effort to rebuild what once existed—locally owned, neighborhood businesses that were an integral part of community life.

<sup>5</sup> See Harvard School of Public Health, <http://www.hsph.harvard.edu/nutritionsource/what-should-you-eat/vegetables-full-story/index.html#cvd> or <http://www.hsph.harvard.edu/nutritionsource/what-should-you-eat/vegetables-and-fruits/index.html> (accessed 16 January 2011).

<sup>6</sup> For a history of housing policy in the United States, see David Erickson, *The Housing Policy Revolution: Networks and Neighborhoods* (Erickson, 2009).

<sup>7</sup> Dr. Daryl Gurley, Pulaski Pike Market Steering Committee meeting, Huntsville, AL July 15, 2009.

## Genesis: A Proactive Strategy of Social Entrepreneurship

In 2007 FBNA's Board of Directors scrutinized the agency's two-fold mission:

- The FBNA procures, warehouses, and distributes food products in support of North Alabama's needy, ill, and children.
- FBNA is a regionally based organization proactively committed to finding solutions to help end hunger and poverty.

Although the second goal of the FBNA's mission went beyond charity, the agency's operations solely focused on responding to the needs of people in crisis by providing emergency food assistance. The agency had not pursued a proactive initiative designed to eliminate the underpinnings of hunger and poverty since the 1990s after an initiative to launch a shiitake mushroom processing plant failed. In response to the 1996 Welfare Reform Act, Dick Hiatt, FBNA's Executive Director, joined a job creation committee convened by Alabama Arise, a nonprofit dedicated to improving the lives of low-income Alabamians. Alabama Arise recognized a need to create jobs accessible to all skill levels that paid fair wages—particularly in light of the new “welfare to work” legislation.<sup>8</sup> In order to implement this committee's research, Dick Hiatt and Ed Hart, an FBNA board member, collaborated with Stan Johnson, an experienced community organizer, to launch a shiitake mushroom processing plant in north Alabama. The plant would incorporate as a worker cooperative—meaning the plant's workers would own the enterprise, enabling them to generate long-term savings and wealth through equity in a viable business.

The first step in this undertaking was passing legislation making it possible to incorporate as a worker cooperative in the State of Alabama. After an initial failed attempt, Representative Laura Hall introduced the bill in a special session of the 1997 Alabama legislature. FBNA and other supporters deliberately maintained a low-profile, and the bill passed without a single question raised. However, when Hiatt and the other collaborators tried to secure funds for the processing plant they met resistance. State and municipal decision-makers viewed the social entrepreneurs “as a bunch of do-gooders” with little to no business acumen (Dick Hiatt, personal communication, 22 November 2010). After continued rejection, FBNA finally ended its efforts on the project in 1998.

In analyzing this failure, those involved in the project determined that they lacked the political capital necessary to launch such a social entrepreneurial venture. That year, 1998, the City of Huntsville was holding its municipal elections. After a series of informal meetings with board members of FBNA and other supporters, Hiatt announced his candidacy for District 2's City Council position. Hiatt and his backers aimed to raise the profile of their issues to the broader public through a political campaign. In an upset victory, Hiatt won the council seat and eventually chaired the City of Huntsville's finance committee (Dick Hiatt, personal communication, 22 November 2010).

During Hiatt's tenure on the city council, he and FBNA cultivated relationships with City staff members. Both parties learned about each other's operations—including the parallels in their financial management due to the fact that both the municipality and FBNA, as a nonprofit, are stewards of public dollars. During this period, Hiatt, trained in business, was able to recruit new FBNA board members including CPAs and other professionals. FBNA advanced its risk management practices to include multiple reserve accounts

<sup>8</sup> For a history of welfare in the United States leading up to ending “welfare as we know it,” see Michael Katz, *The Price of Citizenship: Redefining the American Welfare State* (Katz, 2008/2001).

including paying monthly into a depreciation reserve. By 2007, nine years after ending efforts on the shiitake processing plant initiative, FBNA had accumulated over \$650,000 in addition to its operating reserves, and FBNA's Board of Directors arrived at a juncture:

- Either invest FBNA funds in a proactive project aligned with the second half of its mission; or
- Enhance its existing operations and remove the second mandate from the agency's mission.

Ultimately, the board recognized that if *they* were unwilling to shoulder some of the risk of social entrepreneurship then who would? As Dick Hiatt explained, "The goal is a stronger community through the application of action research—to demonstrate and test solutions to poverty in the real world—out on the street."

FBNA convened organizers from the Terry Heights Hillandale community including Tami Jordan, Director of the Terry Heights Hillandale Organization (THHO), and City staff members to discuss the FBNA's renewed focus to further its mission. During Jordan's tenure at THHO the neighborhood association had a history of active collaboration. Jordan had successfully advocated for improvements to the neighborhood ranging from installing streetlights to the redevelopment of a neighborhood park. She had cultivated relationships not only with City council members but also with City staff as she routinely invited them to speak at ongoing neighborhood meetings. As a result of these discussions with the FBNA, Jordan, with support from

In the spring of 2009, when the City of Huntsville's allocation of stimulus package dollars (approximately \$346,000) for the PPM was proposed, leaders from a local NAACP chapter and residents from a predominately white section of the City expressed initial concerns and resistance. Jordan and representatives from all of PPM's urban partners organized one-on-one discussions with each Council member, attended a community meeting outside the neighborhood, and personally answered questions of constituents. Jordan's standing with and outreach to local politicians had a significant impact. When the vote before the Council ultimately came, it was in unanimous support of the allocation.

the City's Community Development Department, pooled a team of residents together who went door to door conducting 181 face-to-face surveys as part of a preliminary community needs assessment. The survey identified a number of needs, including home repair and crime prevention. In terms of retail services, however, the community's highest priority was a grocery store.

(A brief video with members of the Terry Heights Hillandale Organization describing how the PPM project began is available online at <http://cooperativecurriculum.wikispaces.com/Pulaski+Pike+Market+Video>).

After THHO approached the FBNA with the assessment's findings, the two agencies recruited members from diverse sectors of the community to serve on a Steering Committee to investigate the feasibility and potential impact of a grocery store in the Terry Heights Hillandale neighborhood. The Steering Committee identified the following needs within the Terry Heights Hillandale community:

- (1) Job opportunities with fair wages;
- (2) Options for low-income workers to accumulate assets and improve their standard of living;



- (3) Access to food items including fresh fruits and vegetables;
- (4) Health and nutrition education for consumers at risk for dietary-related diseases; and
- (5) Retail investment to anchor a neighborhood stabilization and redevelopment plan.

The Steering Committee also included representatives from the local farming community, which led to a partnership with the Clean Food Network, (CFN) a network of family farmers<sup>9</sup> who pooled their resources in order to keep their farms in production. In its initial years, CFN experienced modest growth by:

- Increasing the number of member farmers from 4 to 15;
- Increasing annual sales from approximately \$5,000 to \$16,000 in 2009; and
- Expanding its customer list from 25 to over 200 urban consumers.

The CFN, however, operated without a dedicated distribution center—moving from location to location—and was unable to accommodate necessary processing and packaging needs. Many CFN members were new farmers operating small farms.<sup>10</sup> Due to a combination of inexperience, mortgage obligations, and limited financial resources, the new farmers were only able to keep a small percentage of the total acreage available to them in production. Those who rented their parcels were unable to earn enough income to raise the capital necessary to purchase their own tracts of land. At the time, only four CFN members had survived entirely through farming; this fact mirrored statewide statistics in which only 40% of Alabama growers in 2007 farmed as their primary occupation—a 13% reduction since 2002.<sup>11</sup>

Through its discussions, the Steering Committee identified multiple objectives that would assist rural producers' ability to operate a viable business capable of generating livable incomes: (a) infrastructure for a centrally located distribution/packaging site; (b) marketing tools and resources; (c) accessibility to a larger market; (d) and consumer education about the benefits of sustainably grown, local farm products.

## Objectives

The Steering Committee's research and discussions informed a business model for the PPM designed to mutually benefit residents of a distressed urban center and farmers who were from rural areas, had limited resources, and/or were just starting out in their farming careers. In order to create jobs that addressed the underpinnings of poverty, the PPM would operate as a worker cooperative where workers earned fair wages with benefits, owned an equal share of the enterprise, and accumulated long-term savings through equity in a viable business. The rationale for selecting the worker cooperative business model is further described in the section entitled Model Basis.

The grocery store project would meet the infrastructure needs of CFN by housing its distribution center. To address the Network's outreach needs, the grocery's marketing strategy would promote not only the store but also the farmers who supplied it. The strategy combined traditional advertising with nutrition education including seasonal food cook-offs, in-store sampling, and community food celebrations. The store's marketing budget exponentially exceeded the farmers' past marketing efforts. For its part, the CFN

<sup>9</sup> The USDA defines a "family farm" as any farm organized as a sole proprietorship, partnership, or family corporation. Family farms exclude farms organized as nonfamily corporations or cooperatives, as well as farms with hired managers. Family farms are closely held (legally controlled) by their operator and the operator's household.

<sup>10</sup> The Small Business Administration (SBA) generally classifies farms as small if they have sales less than \$500,000.

<sup>11</sup> United States Department of Agriculture, Economic Research Service. *Data Sets: State Fact Sheets: Alabama*. [www.ers.usda.gov/statefacts/al.htm](http://www.ers.usda.gov/statefacts/al.htm) (accessed April 2009).

would augment the grocery's conventional merchandise plan by supplying it with fresh, sustainably grown fruits, vegetables, and other local foods.

The Pulaski Pike Market was projected to create at least 15 jobs representing a cumulative three-year total of nearly \$1.4 million dollars in wages, benefits, and donations back to the community. With this business model, the PPM aimed to accomplish the following objectives:

- Offer residents of the Terry Heights Hillandale community and beyond convenient access to conventional groceries and fresh, locally grown produce;
- Address the alarming rates of diet-related disease through nutrition education and community food events;
- Create jobs with ownership opportunities for low-income workers with entrepreneurial aspirations;
- Leverage marketing dollars and create infrastructure for local, rural producers;
- Stimulate economic development in a distressed urban neighborhood by incubating an anchor retail enterprise;
- Demonstrate a viable niche market for small-format, urban groceries within low-wealth communities; and
- Contribute to a locally sustainable food system by linking rural, local farmers to the collective buying power of low-income, urban consumers.

### Due Diligence

The Steering Committee was given a mandate to determine if the Terry Heights Hillandale neighborhood, despite its concentration of poverty, could sustain an independent, cooperative grocery that would benefit both low-income, urban residents and small, rural farmers. Research had shown that the potential buying power in such neighborhoods could be great (Porter, Watson, & Kwan, 2002, p. 6):

In a study completed in 1998, the Initiative for a Competitive Inner City (ICIC) and The Boston Consulting Group (BCG) conservatively estimated that America's inner cities possess over \$85 billion in annual retail spending power, equal to the total purchasing power of Mexico. More importantly, the study found that \$21 billion of this demand went unmet within the inner city, representing a tremendous urban retailing gap. The study also found that inner city sales volume is a function of income density, not average household income. With a highly concentrated consumer base of shoppers, inner-city markets offer enormous buying power per square mile—two to six times as much as surrounding metro areas – despite lower household incomes.

For over two years, the Committee carried out extensive research on the grocery industry and cooperative management. Steering Committee members attended national conferences on worker cooperatives, food cooperative management, and community food security. The Committee traveled to sites and held interviews with staff at Calhoun Foods, an independent chain of groceries in south Alabama that primarily serves African American communities and Three Rivers Market, a food cooperative in Knoxville, TN.

Members participated in the intensive cooperative development training conducted by *Cooperation Works!*, a national association of cooperative development centers. The Committee supplemented this education with a series of food cooperative development webinars and a worker cooperative finance



workshop led by Tim Huet, of Arizmendi Association of Cooperatives, and Melissa Hoover, the Executive Director of the U.S. Federation of Worker Cooperatives. The Steering Committee diligently followed the cooperative development model created by Gerald Ely and emphasized in *Cooperation Works!* Trainings, as well as a comparable model promoted by the Food Coop Initiative (formerly Food Coop 500). This step-by-step development model encompassed key activities ranging from a characterization and analysis of the potential market to drafting legal documents.

As part of this development process, the Steering Committee carried out a site analysis and sales forecast conducted by G2G Research and a feasibility study informed by a team of consultants from CDS Consulting Co-op (CDS), a consulting firm specializing in food cooperative development throughout the United States.

An initial market/site analysis, completed in March 2008 by G2G Research, defined a trade area encompassing 15,600 consumers and forecasted \$3 million in sales for PPM's first year of operation in 2010. It projected \$5.4 million in annual sales when the store achieved maturity in 2014. This forecast was based on a 6,000 square foot facility with 4,000 square feet of space dedicated to retail sales (Suassuna, 2008). A subsequent market analysis conducted by G2G Research for a similar grocery in an impoverished area of Newport News, VA forecasted a sales volume of \$5.2 million at maturity. (See the accompanying worksheet for detailed financial pro forma statements.)

These results indicated a viable, untapped niche market in low-income communities for the retail grocery business, corroborated by reports in grocery trade journals describing TESCO, Safeway, and Wal-Mart's efforts to target inner-city markets with smaller-format food stores (The Food Institute, 2007). A study published by the Initiative for a Competitive Inner City also found that limited competition "inner-city supermarkets have the potential for high sales per square foot and sales per employee" over regional competitors because "despite lower household incomes, inner-city areas concentrate more buying power into a square mile than many affluent suburbs" and that "inner city sales volume is a function of income density, not average household income" (Porter, et al., 2002, pp. 6-7). After a review, Stuart Reid, Executive Director of the Food Coop Initiative, described the Steering Committee's feasibility study/business plan as "one of the best documented feasibility assessments that I have seen."<sup>12</sup>

### Model Basis

The Steering Committee deliberated on which of three cooperative models to implement:

- Consumer Cooperative Model, which dominated the food cooperative sector, where consumers (also called members) owned and governed the enterprise;
- Worker Cooperative Model, where the workers owned and operated the business; and
- Hybrid Cooperative Model, where both the workers and consumers owned the enterprise and exercised voting rights over the business operations.

Stuart Reid, Executive Director of the Food Coop Initiative, estimated that 98% of food coops in the United States operated as consumer cooperatives.<sup>13</sup> The decision to structure the PPM as a worker cooperative rather than a consumer cooperative departed from the prevalent business model; however, it was based on the Terry Heights Hillandale neighborhood association's deliberations. The THHO board members clearly expressed that they simply wanted a grocery store—not necessarily the responsibilities associated with a consumer cooperative. They also believed a member equity drive or membership share

<sup>12</sup> Personal communication, December 4, 2008.

<sup>13</sup> Personal communication, July 21, 2010.

requirement associated with a “community-owned store” would be met with suspicion from Terry Heights Hillandale residents.

While there are examples of successful hybrid cooperatives like Weaver Street Market in North Carolina with two locations in Chapel Hill and Hillsborough and over \$25 million in annual sales (Weaver Street Market, 2009), the Steering Committee viewed the two classes of membership (consumers and workers) as adding unnecessary complexity to the project and potentially fueling internal tension between the two constituencies. Ultimately, they elected to pursue the worker cooperative model due to its comparatively simple structure, success in communities experiencing inequities, and historical commitment to job creation and retention (Huet, 2001; The Economist, 2009).

The Committee was inspired by the worker cooperative model designed by the original founder of the Mondragón Cooperative Complex headquartered in the Basque region of Spain.<sup>14</sup> Since 1956, Mondragón had grown from a five-member cooperative to a multinational cooperative providing over 92,773 people worldwide with jobs.<sup>15</sup> While the PPM would be one of the first worker cooperatives in the state of Alabama, over 200 already operated in the United States.<sup>16</sup> For example, the Arizmendi Association of Cooperatives had successfully incubated four (soon to be five) worker cooperative bakeries in Oakland, CA.<sup>17</sup> With backing from the Cleveland Foundation and ShoreBank Enterprise Cleveland, Evergreen Cooperatives was incubating a network of worker cooperatives based on the Mondragón model within several underserved neighborhoods of Cleveland including Evergreen Cooperative Laundry, Ohio Solar Cooperative, and Green City Growers Cooperative (ShoreBank Enterprise Cleveland, 2008).

The PPM’s merchandise plan also deviated from the U.S. food cooperative sector’s propensity to specialize in natural and organic offerings. Debbie Suassuna and Peter Davis, the consultants hired to perform the PPM’s market study, confirmed that food (consumer) cooperatives in the United States tended to specialize in natural/organic foods and predominately served a middle to upper class, white, college-educated consumer base—a very different demographic from the community to be served by the PPM.

Based on the market study’s results, site visits, and feedback from Mel Braverman, a cooperative grocery operations specialist, the Steering Committee committed to a “cross-over” product mix of 80% conventional food items and 20% natural, organic, and local foods. PPM would accept EBT (food stamp) cards and stock Women, Infants, and Children (WIC) products. As the PPM’s nutrition education would likely impact demand, PPM’s merchandise plan would expand its locally grown, natural, and organic offerings.

PPM’s modification to existing business models was on the forefront of a burgeoning trend noted by Stuart Reid, Executive Director of Food Coop Initiative:<sup>18</sup>

In the newest wave of co-op development, there are many more considering mixed product lines or even primarily conventional inventories. I think this arises

<sup>14</sup>For a history and description of the Mondragón Cooperatives, see Whyte and Whyte *Making Mondragón: The growth and dynamics of the worker co-operative complex* (Whyte & Whyte, 1991/1988). For critiques, see George Cheney *Values at Work* (Cheney, 1999) and Sharryn Kasmir *The Myth of Mondragón* (Kasmir, 1996).

<sup>15</sup>Mondragón Corporation. *Frequently Asked Questions*. [www.mondragon-corporation.com/language/en-US/ENG/Frequently-asked-questions/Corporation.aspx](http://www.mondragon-corporation.com/language/en-US/ENG/Frequently-asked-questions/Corporation.aspx) (accessed July 20, 2010).

<sup>16</sup>National Cooperative Business Association. *Coop Types*. [www.ncba.coop/ncba/about-co-ops/co-op-types](http://www.ncba.coop/ncba/about-co-ops/co-op-types) (accessed July 20, 2010). See also the map of worker cooperatives in the United States, <http://www.american.coop/node/39> (accessed 13 January 2011).

<sup>17</sup>Arizmendi Association of Cooperatives. *Home*. [www.arizmendi.coop/node/286](http://www.arizmendi.coop/node/286) (accessed July 20, 2010).

<sup>18</sup>Personal communication, July 21, 2010.

from the need for ANY meaningful access to food in both urban and rural food deserts and the lower-income communities that would be served.

## Risk Analysis

The Steering Committee performed a thorough risk analysis using three analysis models. The Porter's Five Forces analysis focused on five external forces (Supplier Power, Buyer Power, Competitive Rivalry, Threat of Substitution, and Threat of New Entry). The PEST (political, economic, social, technological) analysis focused on the business environment and specifically on the political, economic, sociocultural, and technological aspects of the business. Finally, the committee undertook a SWOT (strengths, weaknesses, opportunities, threats) analysis to focus attention on PPM's strengths, weaknesses, opportunities, and threats. Strengths and weaknesses focused on internal matters, while opportunities and threats focused on external matters.

As cited in Katherine J. Henning's article, "Grocery/Convenience Store Start-Up Profile," the Committee also considered the following reasons why businesses fail (Henning, 1998):

Inefficient control over costs and quality of product; bad stock control; underpricing of goods sold; bad customer relations; failure to promote and maintain favorable public image; bad relations with suppliers; inability of management to reach decisions and act on them; failure to keep pace with management system; illness of key personnel; reluctance to seek professional help; failure to minimize taxation through tax planning; inadequate insurance; loss of sales momentum; bad personnel relations; loss of key personnel; lack of staff training; lack of knowledge of merchandise; inability to cope adequately with competition; competition disregarded due to complacency; failure to anticipate market trends; loose control of liquid assets; insufficient working capital or incorrect gearing of capital borrowings; growth without adequate capitalization; bad budgeting; ignoring data on the company's financial position; inadequate financial records; extending too much credit; bad credit control; over borrowing or using too much credit; bad control over receivables; and loss of control through creditor's demands.

## Risk Mitigation

After extensive analysis, the Steering Committee made recommendations to mitigate what it perceived as the PPM's greatest risks: under-capitalization at start-up and mismanagement.

### Addressing the Risk of Under-capitalization at Start-up

The capitalization of the overall project consisted of two components: the business itself and the facilities. As part of its oversight responsibilities, FBNA was charged with fully capitalizing the cooperative business by raising \$1.2 million for start-up and operational expenses including equipment. The role of Neighborhood Concepts, Inc., the partnership's nonprofit real estate developer, was to secure another \$1.2 million in financing for the Market's building facilities, to oversee construction, and to manage the property.

PPM's public/private partnership would utilize the strengths of each partner agency to ensure the venture was fully capitalized. Nonprofits in the partnership, for example, had the ability to access grants or offer

patient loans<sup>19</sup> to reduce the start-up's debt service. The project's new facilities and equipment would not only establish the tone desired by the community but also reduce the start-up's initial maintenance and equipment repair/replacement costs. To ensure PPM would meet its sales projections, the Finance Committee invested in a marketing plan taking advantage of traditional advertising methods as well as drawing upon the strengths of the Terry Heights Hillandale Organization's grassroots outreach abilities.

And finally, in adherence to its development model, the Steering Committee would not implement the project until the venture had the necessary working capital and adequate cash flow during the ramp-up period before PPM attained maturity.

### Addressing the Risk of Mismanagement

To address the possibility of mismanagement, the Steering Committee planned the following safeguards described below.

#### Initial Oversight

FBNA would provide oversight of PPM's initial and most vulnerable years of operation. FBNA, a nonprofit, would initially own PPM's assets and contract with the worker cooperative to staff the market. During this incubation period, FBNA's Community Food Security Program Director and FBNA's Executive Director would work with the cooperative in an advisory/training capacity. When the PPM demonstrated its sustainability by consistently meeting predetermined operational and financial benchmarks, assets would be transferred to the worker owners, making PPM an independently owned worker-cooperative. Due to this contract model, FBNA had the ability to retain ownership if the store encountered problems and terminate a manager for whom this project was ill-suited. Additionally, after the transfer of any assets, FBNA would retain additional safeguards via loan documents for the life of its patient loan.

The predetermined benchmarks would be established on an annual basis (within an annual business plan) during the incubation period in consultation with Cooperative Development Services consultants. The financial benchmarks pertained to both overall store performance as well as targeted outcomes for individual profit centers (meat, grocery, produce, etc.) within the store. In addition to measuring the cooperative's performance against this annual business plan, FBNA had a three-year contract with an independent evaluator to measure the project's performance on multiple fronts, including effect of staff training, staff financial literacy, community impact, and store financial performance.

#### Rigorous Screening

The Steering Committee consulted with Arizmendi Association of Cooperatives and the Ohio Employee Ownership Center of Kent State University to inform its worker-owner recruitment plan. It also devised a rigorous screening process for the General Manager position based on the latest research in behavioral interviewing techniques and input from human resource specialists from local businesses including Redstone Federal Credit Union.

#### Long-term Commitment to Training

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<sup>19</sup> "Patient loans" are those with lenient payback terms offered by lenders with the patience to accommodate such terms.

The Steering Committee planned a long-term training program for the initial management team and staff. Key components included:

- A two-year contract with Mel Braverman, a cooperative grocery operations specialist, to facilitate individual skill development plans for PPM's management team and staff. The training plan encompassed operational, capital, and cash flow budgets; understanding critical ratios and industry reports; margin management; merchandising (product selection/discontinuation, product placement, category placement, pricing, signage); and inventory management, among other skill sets.
- A six-session worker cooperative training required of all recruits before assuming the responsibilities of worker-ownership.
- Ongoing board development and leadership training provided by Dr. Jennie Robison, formerly of the United Way of Madison County.
- Ongoing local food and health education provided by North Alabama Dietician Association, CFN, and Alabama Sustainable Agriculture Network.

In light of this strategy to mitigate the risks, the Steering Committee unanimously agreed that the PPM project was feasible.

### **Public/Private Partnership**

In the spring of 2009, the Pulaski Pike Market's public/private partnership included six agencies working in concert with the City of Huntsville. The partnership included the:

- Food Bank of North Alabama,
- Terry Heights Hillandale Organization,
- Neighborhood Concepts, Inc.,
- Clean Food Network,
- Second Mile Development, and
- Alabama Sustainable Agriculture Network.

A brief description of each partner and their role in the project, as well as the project's consultants, can be found in Exhibit 3.

### **Almost There**

By December 2009, the partnership had much to celebrate. FBNA had secured approximately \$1.2 million dollars for the Pulaski Pike Market's start-up costs including initial salaries, inventory, working capital, and store equipment. Neighborhood Concepts, Inc. (NCI) had secured a \$125,000 commitment for subordinate debt from a revolving loan fund, in-kind contributions including a 1.25 acre tract of land made available by the City of Huntsville through a long-term ground lease at nominal rates, and pro bono site preparation work with an estimated value of \$50,000 made possible through a city/county collaboration.

The challenge now facing NCI was how to put together a deal for the remaining \$1.1 million dollars in first mortgage financing for the construction of the facilities to house the cooperative grocery store and

farmer distribution center. The Building Financial Sources and Uses Statement presented to funding sources as part of an extensive loan package is outlined in Exhibit 4. Financial information is provided in Exhibit 5. Members of the Steering Committee appear in Exhibit 6.

## **Discussion Questions**

1. What is the business model for the Pulaski Pike Market? Do you think the Steering Committee has chosen the optimal organizational model for the venture?
2. Why do you think conditions called “food deserts” arise? Are you in favor of the role that business interests take in both creating and benefiting from such conditions?
3. The opening quotations by Bornstein and Davis seem to qualify “social” entrepreneurs as perhaps different from conventional entrepreneurs. Drawing on the material in this case or elsewhere, is such a differentiation justified?
4. Put yourself in the shoes of Neighborhood Concepts, Inc. and prepare a financial proposal to a funding institution to secure the needed \$1.1 million in funding necessary to build the grocery and distribution facility. Be sure to study the financial pro formas in the accompanying worksheet.

## **Acknowledgements**

Linda Allen, Jim Anderson, Jackie Arthur, Mayor Tommy Battle, Margaret Bau, Jim Blair, Terry Boyd, Jake Brabston, Mel Braverman, Lucia Cape, Leslie Charm, Sylvia Crum, Councilman Will Culver, Pete Davis, Carla De Shields, Elizabeth Fleming Dotts, Equal Exchange, Janice Frazier, Bill Gessner, Michelle Gilliam-Jordan, Dr. Darryl Gurley, Commissioner Bob Harrison, Amy Hartley, Dana Harvey, Dick Hiatt, PJ Hoffman, Tim Huet, Jaques Kaswan, Enorris Johnson, Commissioner Roger Jones, Tami Jordan, Mary Ellen Judah, Gregory Kamback, Councilman Bill Kling, Dr. Ritalinda Lee, Kaye Leslie, Kay Lowry, Margaret Lund, Audrey Malan, Lee McBride, Bill McDowell, Ken Meter, Councilwoman Sandra Moon, National Institute of Food and Agriculture of the United States Department of Agriculture, Joyce Orr, Marcie Porter, Stuart Reid, Scott Rogers, Councilman Mark Russell, John Russo, Councilman Dr. Richard Showers, Dove Stackhouse, Joe Still, Debbie Suassuna, Randy Taylor, Elizabeth Tuckermanty, Karol Waddell, Monty Williams, Karen Wynne, Andrew Zacharakis, and a team of volunteers and supporters who understand what cooperation means.



## Exhibit 1: Demographics

The following demographic summary was prepared by Debbie Suassuna (2008)

### Trade Area Demographic Summary Pulaski Pike Market SEC Pulaski Pike/Hickman Avenue Huntsville, AL

| Census Tract              | Place      | Drive Dist | Trade Area Demographics |                 |                |                  |             |                  |                |                    |                       |                    |
|---------------------------|------------|------------|-------------------------|-----------------|----------------|------------------|-------------|------------------|----------------|--------------------|-----------------------|--------------------|
|                           |            |            | 2007 Pop                | 2007 Group Qtrs | 2007 Pop in HH | % Ann Pop Growth | % White Pop | % Aged 35-54 Yrs | % College Grad | % White Collar Emp | % HH Income \$50-150K | 2007 Median HH Inc |
| 12.00                     | Huntsville | 0.6        | 3,336                   | 1               | 3,335          | 0.4%             | 6%          | 20%              | 7%             | 33%                | 11%                   | \$13,558           |
| 7.02                      | Huntsville | 1.5        | 2,748                   | 154             | 2,594          | 1.7%             | 34%         | 24%              | 22%            | 50%                | 28%                   | \$27,698           |
| 15.00                     | Huntsville | 2.3        | 4,792                   | 845             | 3,947          | -0.3%            | 49%         | 23%              | 25%            | 63%                | 24%                   | \$31,621           |
| 13.00                     | Huntsville | 2.5        | 5,733                   | 0               | 5,733          | 0.7%             | 27%         | 26%              | 24%            | 58%                | 24%                   | \$28,655           |
| <b>Trade Area Totals:</b> |            |            | 16,609                  | 1,000           | 15,609         | 0.5%             | 30%         | 24%              | 20%            | 53%                | 22%                   | \$26,516           |





Figure 2:  
Within and bordering the Terry Heights Hillandale community,  
there are 11 fringe food establishments, elements of a typical food desert.

### Exhibit 3: Public/Private Partners in PPM

**Food Bank of North Alabama** is a nonprofit, tax-exempt charity affiliated with Feeding America since 1985. FBNA distributes over 5 million pounds of food annually to over 200 charitable feeding programs throughout 11 counties in North Alabama. FBNA's staff has contributed to community organizing efforts in low-income communities including the establishment of a commercial grade, community-canning facility located in rural Northeast Alabama and partnerships with low-income residents in both private and public housing developments throughout Huntsville. As a result of FBNA's participation in the Pulaski Pike Market's project, FBNA's board of directors launched a new programmatic division called Community Food Security in 2009. This program's purpose is to proactively address the causes of hunger and poverty through the creation of jobs that contribute to a locally sustainable food network. The program's satellite office is located in the Terry Heights Hillandale neighborhood and shares office/meeting space with THHO. FBNA's management team includes Executive Director, Dick Hiatt, who is trained in cooperative business development and has 25 years of experience in hunger relief work, and Kathryn Strickland, Director of Community Food Security, who has 8 years of experience in nonprofit administration and grant management. As the project's lead agency, FBNA is responsible for the following: (a) Project management and coordination of all collaborative partners; (b) Facilitation of the Steering Committee and all sub-committees including Design, Finance, Organizational Capacity, and Recruitment/Training; (c) Investment of over \$550,000 in the form of a low-cost loan to the PPM for start-up operations (this commitment increased to \$629,500 plus a set aside of a \$60,000 debt service reserve by the end of the project) and the commitment of two staff members' time; (d) Development of the legal structure of the PPM; (e) Recruitment and screening of potential PPM worker-owners; (f) Design and coordination of worker-owner training encompassing the following areas: cooperative business, board member responsibilities, grocery industry operation, and nutrition/local foods; (g) Facilitation of the PPM's initial relationship with suppliers; (h) Liaison for PPM's consultant team; and (i) Oversight of the PPM's initial operation until the cooperative met pre-established benchmarks.

**Terry Heights Hillandale Organization** is a nonprofit, tax-exempt, grassroots neighborhood organization founded in 1998 and dedicated to improving the living conditions of the residents of Terry Heights Hillandale. THHO has a history of active collaboration with other agencies including Huntsville's Community Development Department, Second Mile Development, FBNA, Huntsville Housing Authority, Huntsville Police Department, and several local churches and universities. THHO has successfully advocated for improvements to the neighborhood ranging from streetlights to the redevelopment of a neighborhood park. Their efforts have significantly contributed to the neighborhood's reduced crime rates. THHO operates with a part-time staff person and volunteer board of directors, almost all of whom live in the community. THHO's findings on its 2007 community needs assessment served as the catalyst for the Pulaski Pike Market project. Ms. Tami Jordan, the Director of THHO, worked with FBNA's Community Food Security Director on PPM's development. From the outset, Ms. Jordan served on the Steering Committee and all sub-committees. She also acted as a community liaison, facilitating dialogues regarding the PPM at quarterly neighborhood community meetings. In this capacity, Ms. Jordan also serves as the President of the Resident Advisory Board of the Huntsville Housing Authority. THHO's responsibilities in the project included: (a) Liaison to the community; (b) Public outreach and presentations; (c) Participation on all committees and sub-committees; (d) Recruitment of worker-owners; (e) Organization of community food events at the PPM such as "Meet Your Farmer Day," cook-offs, and health fairs; (f) Recruitment and coordination of Local Food (LF) Ambassadors who will run in-store



public service promotions, including food samples from local farmers, recipes, and nutrition education in the form of fun food facts.

**Neighborhood Concepts** (NCI), a tax-exempt, nonprofit developer founded in 1988, develops multi- and single family affordable housing and commercial space for other nonprofit organizations that provide services to low-income families. NCI routinely partners with the City of Huntsville Community Development Department on neighborhood stabilization initiatives and previously collaborated with FBNA on the construction of the Food Bank's current base of operations. NCI assumed the following PPM project responsibilities: (a) Oversee the LEED-certified building design for PPM's 6,000 square foot facility and 1,200 square foot food distribution center; (b) Secure permanent financing and supervise the construction process; (c) Asset manage PPM's building; and (d) Enter into favorable lease terms with PPM to foster the cooperative's ability to attain profitability. In April 2009, NCI and FBNA entered into a Memorandum of Understanding outlining these responsibilities.

**Clean Food Network** (CFN) is a local network of 15 small, family farmers who have pooled their resources in order to market their sustainably grown products to urban consumers. Its long-term goal is for member farmers to earn a living wage entirely from farming. As a member of the Steering Committee, CFN committed to the following: (a) Supply the cooperative with sustainably grown local foods; (b) Participate in joint marketing campaigns with PPM; and (c) Participate in community food events organized by THHO such as "Meet Your Farmer Day," cook-offs, health fairs, and in-store promotions.

**City of Huntsville Community Development Department** (CDD) has targeted the Terry Heights Hillandale neighborhood for redevelopment and neighborhood stabilization. CDD staff served on the Steering Committee in the project's initial months and supplemented THHO's needs assessment with a study conducted by Zogby International. CDD's significant contributions to the public/private partnership include: (a) a 50-year ground lease (with two 15-year renewals) at the nominal rate of \$10 per year for PPM's site location for a 1.25 acre tract of land in Terry Heights Hillandale with an estimated value of \$217,000; (b) \$346,000 of CDBG Recovery funds for the PPM's equipment purchases; (c) \$50,000 worth of in-kind site preparation in collaboration with the Madison County Commission.

**Second Mile Development** (SMD) is a local, tax-exempt nonprofit that has supported the empowerment of children and their parents in the Terry Heights Hillandale neighborhood for over 20 years. They operate a preschool, parent initiative, and a neighborhood store for gently used items. From the outset, SMD's Parent Coordinator has served on the Steering Committee and is playing a key role on the Recruitment/Training Subcommittee. SMD is also providing office/meeting space in the Terry Heights Hillandale neighborhood for the THHO and FBNA's PPM development team.

**Alabama Sustainable Agriculture Network** (ASAN) is a network of farmers, consumers, and agriculture-related organizations that promotes sustainable agriculture and supports the advancement of farmers and consumers alike. Their programming includes farmer mentoring and consumer education. ASAN assumed the following role in the project: (a) Facilitate PPM's relationship with suppliers of locally grown food products; (b) Educate PPM employees about local, sustainably grown foods and their importance; (c) Coordinate ASAN members' participation in community food events at PPM; and (d) Lead the Steering Committee's strategy for long-term solutions to a locally sustainable food network.

**Consultants:** The Steering Committee has also engaged consultants from Cooperative Development Services to provide technical assistance with the multiple facets of the PPM's development: Mel Braverman, cooperative grocery management and operations specialist; P.J. Hoffman, store design specialist; Debbie Suassuna and Peter Davis, market/site analysis specialist; Bill Gessner, cooperative financial development specialist.

## Exhibit 4: Building Financial Sources and Uses Statement

Neighborhood Concepts, Inc. (NCI) was the nonprofit developer partnering on the Pulaski Pike Market project (see Exhibit 1). NCI prepared the following Sources and Uses statement as part of a complete loan package presentation to bankers. It pertains only to PPM's construction (consisting of two buildings—the grocery store and a food distribution building) and not the start-up costs for the grocery, which had been raised in full by FBNA. FBNA agreed to secure funding for the store's equipment as part of the \$1.2 million start-up costs. The equipment is included in total development costs in the Sources and Uses because it was part of the real estate's furniture, fixtures, and equipment and could be considered additional security for a loan.

The developer fee was 6%, significantly lower than the traditional 10–15% fee typically charged. NCI also agreed that any overruns exceeding the contingency would be drawn from their fee. The construction budget aligns with the original LEED design. The LEED design could have been adjusted if negotiations called for reduced expenses; however, that level of negotiations was never reached. The hard construction cost for the grocery building—consisting of 6,000 square feet—was approximately \$150 per square foot; the hard construction cost for the distribution building (referred to as the CFN Bldg. on the following statement)—consisting of 1,200 square feet—was about \$58 per square foot.



**PULASKI PIKE MARKET**  
Development Source and Use Statement  
Operating Pro Forma  
Equipment Funded w/CDBG-R

| Sources              |                 | Uses                          |                 |
|----------------------|-----------------|-------------------------------|-----------------|
| Donated Land         | \$ 217,800.00   | Acquisition                   | \$ 217,800.00   |
| 1st Mortgage         | \$ 1,160,000.00 | Construction (Hard)           | \$ 900,450.00   |
| CDBG-R Grant         | \$ 345,000.00   | Construction (CFN Bldg)       | \$ 70,000.00    |
| TARCOG               | \$ 125,000.00   | Construction Contingency      | \$ 45,000.00    |
|                      |                 | Architect                     | \$ 80,000.00    |
|                      |                 | Environmental                 | \$ 6,500.00     |
|                      |                 | Design Consultant             | \$ 9,000.00     |
|                      |                 | LEED Certification Agent      | \$ 5,000.00     |
|                      |                 | Survey                        | \$ 8,500.00     |
|                      |                 | Equipment                     | \$ 345,000.00   |
|                      |                 | Appraisal                     | \$ 5,000.00     |
|                      |                 | Legal                         | \$ 2,500.00     |
|                      |                 | Signage                       | \$ 10,000.00    |
|                      |                 | Title (Owner & Lender)        | \$ 5,600.00     |
|                      |                 | Insurance                     | \$ 5,000.00     |
|                      |                 | Loan Origination Fee          | \$ 11,600.00    |
|                      |                 | Loan Origination Fee - Tarcog | \$ 2,700.00     |
|                      |                 | Construction Interest         | \$ 20,650.00    |
|                      |                 | Soft Cost Contingency         | \$ 13,000.00    |
|                      |                 | Developer Fee                 | \$ 84,500.00    |
| Total Sources        | \$ 1,847,800.00 | Total Uses                    | \$ 1,847,800.00 |
| Est. Appraised Value | \$ 1,485,000.00 |                               |                 |
| 1st Mtge LTV         | 78%             |                               |                 |

**Annual Operating Proforma**

|                             |  |
|-----------------------------|--|
| <b>Income</b>               |  |
| Pulaski Pike Market Rent    | \$118,680  |
| <b>Net Operating Income</b> | \$118,680  |
| <b>Debt Service</b>         |  |
| 1st Mortgage                | \$97,813     \$1,160,000, 7%, 25 year amortization |
| 2nd Mtge (TARCOG)           | \$14,800     \$125,000, 3.5%, 10 years             |
| <b>Total Debt Service</b>   | \$112,613  |
| <b>Cash Flow</b>            | \$6,067  |
| 1st Mtge DCR                | 1.21   |

## Exhibit 5: Financial Information

For pro forma financial statements, please see the Excel worksheet accompanying this case.

## Exhibit 6: Steering Committee Members

From left to right, Lee McBride, Dove Stackhouse, Mary Ellen Judah (rear), Carla De Shields, Dick Hiatt, Karol Waddell (rear), Kay Lowry, Jim Blair (rear), Dr. Darryl Gurley, Tami Jordan, Greg Kamback, Karen Wynne, Kathryn Strickland.



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