Owner Bond Drives Support Growth at Willy Street

BY LYNN OLSON AND DAVID WAISMAN

Back in April 2010, Willy Street Co-op (Madison, Wis.) launched an owner bond drive to raise money to support the opening of a second retail store, Willy West. In just 37 days, the bond drive was complete and the maximum amount of $1,000,000 was raised. But the road to this successful drive was a very long one.

Past successes

Willy Street Cooperative is extremely fortunate to have been founded in the heart of Madison's eastside community, where a long and passionate history of activism in the areas of human rights and ecology still remains. Serving their needs for over 37 years, Willy Street Co-op has owners who have traditionally been eager to participate in their co-op, whether that meant working in the aisles or serving on board committees.

Issuing bonds to support the co-op's growth has a long history dating back to opening its first location in 1974. With an ever-expanding base of owners, the leaders of the co-op have responded by increasing its retail area on Williamson Street—or Willy Street, as it is affectionately called. Willy Street Co-op has offered bonds to co-op owners on four occasions, to support the first location and subsequent expansions.

During 1998–1999, a third bond sale financed the purchase, remodel, and relocation to the current site at 1221 Williamson St. With 4,500 owners and their strong support, the co-op successfully raised $443,000. That expansion was in response to owners' dissatisfaction over the lack of parking and lack of adequate space to provide a larger product selection.

By 2004, the site was already feeling the effects of rapid sales growth, including an increasing number of out-of-stocks, tight back stock, a heavily trafficked store and parking lot, and related labor stresses. General Manager Anya Firszt and the board of directors responded by creating an Opportunities Committee to research the co-op's expansion options. That committee determined that the best next steps for the co-op were the creation of an off-site commissary kitchen, a second retail location, and the eventual remodel of 1221 Williamson St. building.

In 2005, the co-op built its off-site commissary one mile from its retail site (reported in *CG* for May–June 2005). Immediately following, our sights were set on a second retail location to relieve the overcrowding.

Weathering a setback

In 2007, a site in the heart of Madison's downtown area and near the University of Wisconsin campus was chosen. The co-op planned to be the anchor tenant in a 160-unit condominium project known as Metropolitan Place II. After we had received positive endorsement from the developer's banker, had signed the lease, begun construction, and hired key managers, hard lessons were learned when the bank foreclosed on the property before the doors could open. After the storm of that difficult time, Willy Street Co-op was able to recoup a portion of the $750,000 that was lost—through a voluntary reduction in workforce, a tax refund, and repurposing of unused project materials.

Once the co-op stabilized operations and rebuilt its financial reserves, it took its lessons learned and focused on securing the long-sought second retail site. By fall of 2009, after a committee search, a preferred site was identified at 6825 University Ave. in Middleton, a stone's throw from Madison's western border. Lease negotiations and plan development began. The Middleton site, now called Willy West, is located eight miles from our first store and has 9,500 square feet of retail.

In 2009, despite the failed expansion two years earlier, with 20,000 owners (five times the number in 1999) and a proposed second store in a neighborhood that strongly welcomed the co-op, there was confidence that the bond program would be successful. But there were still barriers to be addressed. In preparation, management established three guiding principles for the bond drive:

Keep it super simple. Managers wanted to be sure that the terms of the bonds were easy to explain and promote and easy for owners without financial expertise to understand.

Allow broad owner support. The Willy Street Co-op board of directors encouraged management to set an accessible minimum bond amount. The desired outcome was to get as many owners as possible to participate in the offering.

Focus efforts and resources. In 1999, the bond drive had lasted a little over one year. With this in mind, it was decided that it would be in everyone's best interest to manage as short a bond drive as possible, due to the many other critical tasks in getting the second store opened successfully.

Simple and short

The result was the development of a bond program that had the goal of gathering $600,000

Bond Options and Definitions

- Co-op owners lend the co-op money. The co-op issues to each lender an IOU (or bond) which pays a stated rate of interest in addition to the original loan amount at maturity. Some co-ops call these member (or owner) loans.
- Each bond is zero compound, with interest paid at maturity.

Bond A	**Bond B**	**Bond C**
Maturity: 3 years	Maturity: 5 years	Maturity: 7 years
Interest rate: 4.004%	Interest rate: 4.564%	Interest rate: 5.190%
Minimum: $200	Minimum: $200	Minimum: $200

Optional feature: Bondholders purchasing more than $2,000 may choose to receive annual interest payments.

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Sources and Uses of Capital for Second Retail Location

SOURCES		USES	
Cash contribution	$850,000	Professional services	$147,570
Owner bonds	$600,000	Construction, equipment	$2,217,105
Landlord's improvement allowance	$200,000	Pre-opening expenses	$270,440
Vendor credit	$150,000	Inventory, other expenses	$515,760
Long-term debt	$1,650,562	Cost overrun allocation	$299,687
Total sources	$3,450,562	Total uses	$3,450,562

in 60 days. Although we were authorized to sell up to $1M in bonds, we chose a lower goal that would be attainable in the allotted period while meeting the minimum project financing needs (see the sidebars).

The owner bonds were set up as zero coupon bonds, which is a simplified bond structure that pays all the interest at maturity. For example, if an owner purchased a $200 bond, the co-op will pay back either $225 after three years, $250 after five years or $285 after seven years, depending on the chosen maturity. The minimum purchase price was set at $200 to encourage broad participation, and we also set a maximum purchase of $25,000.

Any bondholder purchasing a bond worth more than $2,000 could elect to receive annual interest payments. The interest rates were established with consideration given to certificate of deposit rates and the expected borrowing rate for other debt financing. Although able to issue bonds at a lower interest rate and achieve similar success, the co-op wanted rates that recognized the importance of owners in this process and that supported our goal to complete the bond drive within 60 days.

Once the lease was signed in spring 2010, a letter was sent to all owners announcing the new location, along with information about the owner bond drive. Although it was costly to send a letter to 20,000 owners, it was consistent with the plan to focus all resources in order to meet the financial goal as quickly as possible. In addition to this letter, owner bonds were promoted in the co-op's monthly newsletter, on its website, and in the store. The infamous Bond-o-Meter, which tracked results and motivated owners to action, was posted in the store.

Other key communication materials were the bondholder information packet and bond contract. The messaging was consistent in all materials, reinforcing the credibility, rationale for expansion, and risks of purchasing a bond. (For more specifics on staff preparation and owner communications, see below.)

Lessons learned

"Unanticipated" may be the best way to describe the immense response from owners and the general public once the bond drive was launched. We had created bondholder information packets designed as a prospectus for potential buyers, including instructions for purchasing a bond. Between collating packets, sending packets, and taking phone calls, it became an all-consuming task to keep up with the requests.

Hundreds of calls and emails were received, requesting information. After explaining to a considerable number of nonowners that the sale was only open to owners of the co-op, many of those immediately joined in order to participate. Had it been clear that this work would take so much time and resources, adequate staffing arrangements would have been made. However, once in the midst of it, there was little else to do but to keep running to make it all happen.

Financially, the bond drive was a resounding success, including revising our goal to the allowed maximum of $1 million. One down side was that only 200 owners participated; we had hoped that, by setting each bond price at $200, more owners would be able to participate. On the upside, there is renewed confidence that the next time bonds are issued, there will be strong demand amongst Willy Street Co-op owners. ■

Excerpts from the Letter to Willy Street Owners

It is critical to note that all owner bonds are absolutely unsecured, non-transferable, and subordinated to other creditors.

Your support can also be voiced in other ways like paying off the balance of your equity Fair Share, voting, writing customer comments, and shopping.

Am I guaranteed to get my money back?

No. Although we have invested over the last several years to build organizational capacity, to select a high-quality site, and to improve our financial position, there is no guarantee of success. These loans involve risk and should be made only by owners who have determined that it is in their interest to support the growth of the cooperative.

Are these bonds callable?

Yes. This feature enables the co-op to buy back the bonds prior to maturity. The board can call the bonds if the co-op is able to borrow funds for an interest rate at least 1% less than the bonds are paying.

Can I get out early?

Yes. Bondholders may request early redemption by giving the co-op 60 days' written notice and paying a penalty equal to one year's interest deducted from the amount otherwise payable. All early redemptions must be approved by the board prior to payout.

Excerpts from Staff Support Materials

Bond Drive Customer Service Talking Points

Top Things to EMPHASIZE

Buying a bond is a way for owners to support the co-op's growth

You must be a paid-in-full Fair Share equity owner to purchase a bond.

You must be a Wisconsin resident to purchase a bond.

All bonds are unsecured, thus not guaranteed. There is risk involved.

All bonds are not transferable under any circumstance.

Paying off your Fair Share is another means of supporting the co-op.

Top Things to AVOID

Do not call it an investment. It is a way to support the co-op.

Avoid any deception, even if it is unintentional. Do not speculate or try to answer questions you are unsure of. Refer them to the appropriate person.

Accuracy is key. We do not want to get someone to buy a bond based upon false or speculative information.

Avoid getting yourself into an uncomfortable position. If someone pushes you for answers or information that you're not sure about, be sure to refer them to the appropriate person.