

August 14, 2017

From: VFC Board of Directors
To: Friends of the VFC
Re: Response to questions

Dear Friends of the VFC,

In response to the list of 16 questions detailed in your July 24th communication please see the following answers. Since KJ and Tom are the liaisons to the Friends of VFC, we request you share this with those who signed the original questions document.

We are all committed to our cooperative and cooperative principles of governance and management. With that being said, we also want to express that the general tone which came through was seemingly suspicious and distrustful – implying we don't do our due diligence with great deliberation among the board and management. We continually strive to ensure all members have a voice and opportunity to give input. Thank you for this opportunity to answer these vital questions.

1. When did the VFC Board first review the \$7.9 million expansion budget? Did the VFC Board vote on specific aspects of the expansion? If so, when (at which meetings)? And what was the specific wording and vote count of each expansion related vote?

The Board committed to the expansion project at the March 15, 2017 board meeting after a presentation to the board on March 14, 2017 on the proforma and NMTC program by Baker Tilly Accounting, Bank of Cashton, and Development Co-op and is recorded in the March minutes. The decision to move forward was contingent on a final budget and proforma to be completed and approved by the board. Over the course of the past 12 months there were many mile stones which had to be completed before a final budget could be approved. The decision to expand had numerous contingencies including our desire to remain in our current location, purchase the corner lot to consolidate the property on the east side of Center Street in the anticipation of its use as our future parking lot. In addition we had to gain permission from the city to close the street in order to build out from our current site in order to maximize the available square footage. We had numerous learning sessions and meetings to discuss the multiple aspects of the plan. We had in-person meetings with the Co-op Development Services (CDS) advisor, Leslie Watson from East Side Cooperative in Minneapolis during our annual planning sessions. Regular monthly teleconference check-ins with Leslie occurred and was attended by those board members who were available. Curt Brye generally attended all of the teleconferences. East Side Co-op was in the middle of completing their expansion and Leslie provided valuable advice and insights. There was not a need to vote on individual aspects of the planning; our discussions were to become informed, provide feedback, ask questions and challenge assumptions and give commentary to our management. Minutes to our board meetings are posted online at www.viroquafoodcoop.coop.

2. Why were the architectural and construction contracts no-bid? As contract bidding usually helps to keep costs down, how does the VFC Board justify this in terms of its fiduciary responsibility to the members?

Several board members have expertise in construction bidding and contracting. We do not believe that bidding a project will necessarily deliver the lowest possible price, nor be in keeping with building to the level of standards which the current VFC building was built. Bidding can result in poor quality materials,

shortcuts to save costs and labor practices, such as using temp hires to reduce costs which we do not condone. Weiser Bros. built our current building and also did the recent addition to expand out back room areas and is very familiar with our building. They are a local company employing people from the Crawford, Vernon and Monroe counties. Weiser have done a significant amount of the commercial construction in the Driftless region and are known for their quality, ability to deliver according to plan and timelines and their straightforward, honest business approach.

3. Did the coop hire an independent building professional outside of the Wieser group to review the building blueprints, and if not, why not? Will there be any independent building professionals inspecting the building during construction to confirm contract/specification requirements? Will there be an independent commissioning of the building at completion?

The Co-op hired the Development Co-op (DC) to assist with the entire project of expansion from beginning to end. They have considerable expertise from developing our market survey to designing the retail space and assisting with the business plan and proforma. The DC has reviewed all plans and will continue to monitor and assist with any aspects they would consult on pertaining to the construction until the completion. River Architects of La Crosse drafted the design and blueprints, and Paragon Associates of La Crosse did the engineering (as they both did for our current building). The VFC will be open for business during the expansion and expects only minor disruptions to our normal business hours in order to complete some key tasks during the course of the project. At every stage of the building project, State and City inspections are performed as required by law.

4. It has been stated that prices will be lower due to the expansion. However the VFC Business Expansion Plan states that cost of goods assumptions are based on current business. This indicates that pricing will remain the same. How will the lower prices come about?

Lower prices is a constant priority from the membership and we are proud to have delivered lower prices with our margin strategies over the course of the past two years. There is always a fine balance with lower prices in terms of insuring that our employees are well compensated and that we pay fair prices to our local suppliers and farmers. We are proud to have raised our employee compensation package over the past two years at a time of lower price strategies in order to compete in the greater market area. With the expansion we will be growing sales in our higher margin departments such as our deli and prepared foods. A common theme found in our membership surveys was the request for more and better offerings with our deli and prepared foods and more room for dining and a community space. In addition because we will have more assortment due to our added space we will be able to sell more “discretionary” products such as health and body care products with higher margins. The overall store margin may actually increase while allowing us to keep our grocery, produce, bulk, dairy and meat margins low and competitive. This hi-lo margin strategy is strategically employed by retailers such as the leading Cooperatives, Natural Grocers, Whole Foods and progressive grocery chains.

5. In the past 2 years significant changes in the natural foods industry have taken place and more are expected to come. As examples CSA memberships are down, OV sales are reduced, nationwide coop sales are down and online purchases of groceries are increasing. The market study does not address these current trends. Have any market studies included competing sales markets in La Crosse, Madison and online vendors such as Amazon? Have the forecast numbers been rerun in the last year based on eroding market shares of co-ops around the country and increased competition from conventional retailers? Has there been or should there be consideration of downscaling the project based on this information?

The Market Study absolutely addressed national and regional trends and the updated study showed changes in our projections accordingly. The marketplace is constantly changing and the VFC has to as well. We believe that expanding our services and offerings to our membership is how we will survive and thrive in the future. We do not feel that downscaling this project will offer any benefits and is contrary to building out to the full extent that we can on our site so we can remain downtown for decades to come. Overall the expansion and total retail space is very modest in terms of total square footage and the expansion is in the departments which our members have been asking for more goods and services. We are not sure where the comments about CSA membership and OV sales being down come from. Nationally CSA's and farmers markets are growing each year. OV is growing, oversupply of milk, is OV's challenge today.

Many retailers are threatened with stagnant growth and certainly the ability to order almost any product online today will continually challenge the retail community. Some of us on the board believe we should also be aggressive with online ourselves, we can envision doing home delivery in our area, which could be coupled with CSA deliveries too. It's much more efficient to have one truck deliver to fifty households than fifty households drive to the store. We could envision the ability for a member to order online and pick up at the store much in the way in which "InstaCart" and Amazon are pioneering today. We are encouraged by the National Co-op Grocers plans with a new Co-op to Co-op program, (the development of direct sourcing from Co-ops), the growth of the value priced "Field Day" day products, and the continued success in negotiating lower costs from several distributors and great deals from our suppliers. NCG recognizes the need to resource and develop programs to address ecommerce and add value for the membership and insure our viability in the constantly dynamic marketplace.

6. Was a more conservative, practical expansion approach, say 2 or 3 million, considered? If so, why was it ruled out?

Initially we believed the project would be smaller, perhaps around \$5MM, but never in the \$2-3MM range as it would not achieve our goals determined by the market study and membership survey to add services and more assortment. Let alone the needed space for our shoppers to readily negotiate the store during peak shopping hours, and to offer our deli workers more space to work efficiently and safely. As the project developed and we insured our ability to stay in our current location, it was evident that if one is going to tear open walls and pour foundations that maximizing the building footprint on our site would not add considerable expense and would carry us forward for many years to come. We also committed to building values of energy efficiency, sustainable materials, LED lighting, cooler doors rather than open cases, all which added costs. Once we were confident that the VFC did qualify for the New Market Tax Credit (NMTC) it gave the board the confidence to move forward with a financing package, which was financially sound and allowed us to achieve most of our expansion goals. We did back off in some areas including opening a full service meat and seafood department, or a full service Juice bar, because we felt it could add costs and financial risks at the onset. We will be able expand in that direction in the future as we achieve our budgeted goals, and if the membership desires those services.

7. What are the terms of the construction contract regarding modification of plans such that the scope of the project could possibly be reduced?

We don't see the need to curtail or reduce the project as planned. The expansion will give us 9,250 sq. ft. of retail space, which compared to our local independent grocery store at 28,000 sq. ft. of retail is modest. In the NCG retail community we will be ranked as a midsized store.

8. Why did the VFC Board vote for a project of this magnitude, risking member capital, incurring a net \$6 million debt, without consulting the membership? When was it decided that an expansion of this magnitude did not warrant being taken to the ownership for a vote? Who made that decision?

The board has followed the same process as when we expanded from our original building. There was never a plan to vote on the expansion, but to receive membership feedback over the course of three+ years with opportunities for input with surveys and at our annual meetings, summer events, coffee and beer with the board. The board's fiduciary responsibility is to make these decisions, and take this responsibility seriously. The entire board is investing in the project as a sign of our confidence and commitment to the VFC.

9. If sales do not meet projections what are your specific concrete strategies for dealing with the shortfall?

The VFC has a history of sound management, with strong leadership. The co-op with its "open book" management with our staff is focused on achieving budgeted goals and reviewing those numbers weekly. The board too will be monitoring the financial results each month, quarterly with a deep dive, and annually with our financial reviews/audits, and budgeting process. It is difficult to forecast how our results will be until the store is complete to know where/if we may fall short. We can anticipate the need to market our assets widely through social media, our website, local advertising and positive word of mouth. One of the most important things we can all do as members is to keep the positive energy flowing, with our words and actions. Shop co-op!

10. Can the VFC Board assure members that the NCG strategy of bringing in more and more conventional foods into coops with expansion shortfalls will not be utilized by VFC as has occurred in other coops?

The NCG does not have a policy or strategy of "bringing in more conventional food", nor does the VFC. We have always sold conventional food, such as locally grown produce, dairy and egg products which are not organic. We do have many members who cannot afford organic food so we are mindful of their needs by choosing good quality products. We have organic Field Day products from UNFI and other products in the basics program, the co-op deals and owner deals programs offering savings on natural and organic foods. We cannot compete in that space with WalMart and nor do our members want us to. Coca Cola and Tide will not be on our shelves....

11. What means did you use to gather employee input regarding the expansion details? How is that documented?

Staff input began when a special team took the VFC Board's interpretation of the Community Conversation event and applied it to operations. (Check out this link to see our Vision Statement that guides staff in the daily operations of the Co-op. <http://www.viroquafood.coop/viroqua-food-coop-blog/bid/208081/The-VFC-Experience-Viroqua-Food-Co-op-prepares-for-the-next-chapter> Input on specific floor plans and design happens at weekly staff meetings, one on one staff to manager check-ins, and department managers meetings with department consultants.

12. What was the scope of work and how much has been paid to each consultant for expansion related services and for other consulting services since 2012? In what line item were the payments for consultants reported in the annual report each year?

These expenses are a part of the total cost of the expansion project. Costs incurred before the start of expansion (but expansion related) are recorded in the professional services line which is a part of the Administrative and /or Operations line in the annual report depending on the services performed. Many of these can be recovered through a 'reimbursement system' when project financing is completed.

13. Has the VFC Board considered and discussed how this expansion will affect Village Market? What were the considerations and the outcome of your discussion?

The VFC Board has not discussed nor considered how our expansion may affect the Village Market. We represent the member's interests of the VFC, not other retailers. The Village Market which predominantly sells conventional food, primarily competes with WalMart. Village Market regularly updates their store and has never discussed their plans with VFC and vice versa. We wish them well and know how important their store is to our community.

14. What was the board's basis for excluding renewable energy, deemed important by many coop members, from the original expansion plan. Now, after the fact, will the board consider conducting an analysis utilizing existing member expertise to include solar electric and hot water?

We know energy efficiency is important to our members. That is why VFC incorporated many sustainable energy ideals into the expansion from the beginning. The heat exchangers from our compressors to supply hot water for the store is the most significant area of energy savings, beyond our super insulation and HVAC planning. In a grocery setting, the most important energy use is efficient coolers and freezers, and is also the greatest expense. The planning process was not far enough along to apply for the grant concerning solar voltaic last fall, and we felt our chances would be better this fall. We have been developing a plan with Ethos to apply for a grant for the installation of a solar voltaic system. If the Article V change is approved at the annual meeting, giving us more shares to sell, we plan to offer a special class of investment for our members who want to designate their investment into the passive solar system. We've also worked with Ethos on our Electric Vehicle Charging Station for the parking lot. Check the FAQs for other questions and answers on energy saving choices already made.

15. This expansion seems to be going in the opposite direction of sustainability: increased single-serving packaging, less bulk foods, increased prepared packaged food, increased energy consumption for heat, cooling and refrigeration, the environmental impacts of new construction materials, etc. Why is there no significant sustainability analysis or plan for the VFC?

In terms of the statements about increased packaged foods and less bulk, those are not part of our strategy. While the store will have more assortment which will represent more packaged foods, we will be able to accommodate more space for locally produced foods, health and beauty care products, produce, dairy, meats and eggs. While bulk food sales are declining nationally, primarily because Millennials are not purchasing as much in bulk, we are expanding our bulk foods offerings, as we believe it is part of our mission to provide the lowest possible cost and sustainable choices. In terms of our deli offering more prepared foods, this will come in two forms, packaged and offered fresh for consumption on site. We will have more packaged foods from our deli, and from a Life Cycle Analysis (LCA) perspective is much more sustainable even when sold in the package, because we are producing the food in-store without the need for the multiple points of warehousing and logistics with traditional distribution. Prepared foods from our deli can utilize more directly sourced farm products and ugly vegetables which don't make the grade for produce sales but are perfectly good to cook. This will add value for our direct source farm suppliers.

Since 2014, VFC has participated in *Co+efficient*, NCG's co-op sustainability program, which works to

measurably improve co-ops' social, environmental and local economic impacts. We do this continually through three main steps:

- Measure baseline performance with Co+efficient Metrics and Co+efficient surveys.
- Analyze our metrics for a deeper understanding of our co-op's strengths and opportunities.
- Improve using Co+efficient Tools and Resources and the knowledge shared by others in the co-op community.

16. Viroqua and Vernon County need more employment opportunities. Did the VFC Board consider requiring any percentage of the project to be local hire? If not, why not?

Providing more employment in our community is a key outcome of this project. The NMTC requires that new jobs are created, and naturally as our store grows we are providing more quality employment, more opportunities for local farmers, and more business for our local manufacturers and suppliers on many fronts. VFC jobs are currently paying \$10/hr and up, include benefits like comprehensive health care, short term disability, family leave and bereavement, 401k, paid holidays, time and a half holidays, Paid Time Off, FSA with match, food discounts and more (these are current benefits, pre-union contract). Due to the Co-op's internal growth trends in previous years and the needs for additional staff from the increased production capabilities at the expanded store, it's estimated that 35 direct full time equivalent positions will be created by 2020. In terms of short term jobs during the constructions phase, Weiser Bros is a local company and will be utilizing other contractors all within a 40 mile radius of VFC several right here in Viroqua. Using economic modeling software and other local data, it is estimated that the construction hard costs for this project will support approximately 87 full time construction jobs. The construction activities will support 8 full time equivalent indirect jobs.