

2016 HOSPITALITY LAW CONFERENCE

FEBRUARY 22-24, 2016

RESTAURANT REALITY 2016 Trends, Finance & Expansion

Presented by:

Jordan R. Bernstein, Esq.

&

Chris Tripoli, FCSI



PRESENTERS



Jordan Bernstein

Partner, Michelman & Robinson, LLP

- ❖ Jordan counsels established and emerging chefs, restaurateurs and food & beverage executives from concept through multi-year growth and expansion.
- ❖ He advises on entity structure, financing, strategic partnerships, operational matters, corporate formation and governance, as well as sales and acquisitions.
- ❖ He also works with his clients on branding, licensing, management, consulting, vendor and other contract and transactional drafting.



Chris Tripoli

President, A' la Carte Foodservice Consulting Group

- ❖ Chris Tripoli has over 35 years of service in the Hospitality Industry as a designer, developer, owner and operator. He founded and is the President of A' La Carte Foodservice Consulting Group.
- ❖ Chris regularly contributes to *Restaurant Startup & Growth Magazine*, *My Table Magazine*, *The Consultant* and *RestaurantOwner.com*.
- ❖ Chris remains active in the Foodservice Consultant Society International and National Restaurant Association. He serves on the advisory board of The University of Houston Small Business Development Center.



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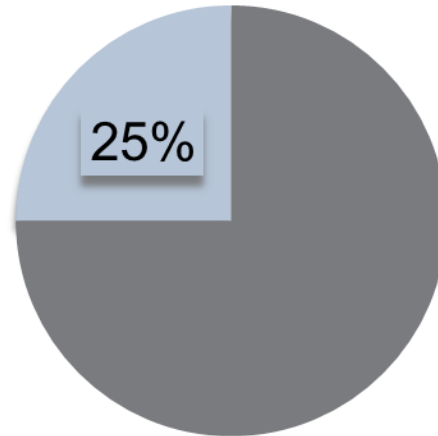
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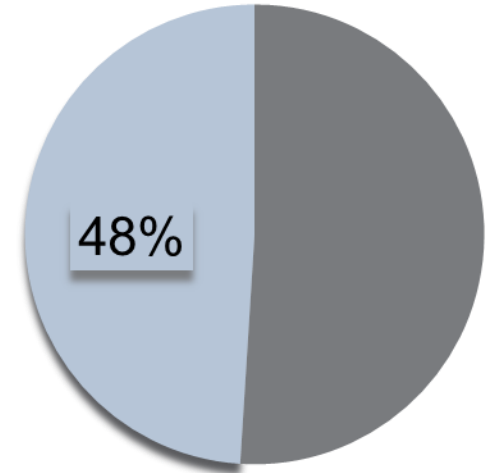


OVERVIEW

- Currently over **1.1 million** restaurants
- Share of food dollar = 48%



1955



2015



CUSTOMER EXPECTATIONS

Value



Fresh & Healthy



Variety



Convenience



Service

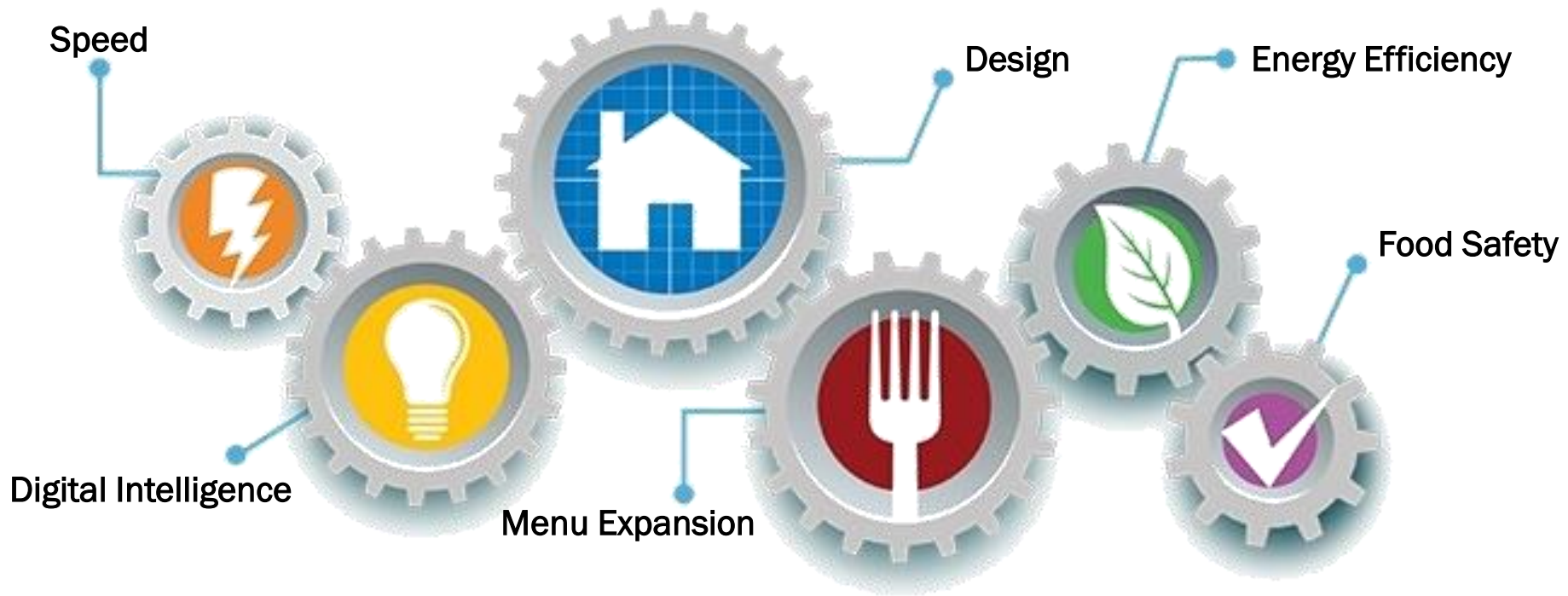


WHAT'S HOT!!

- **“Clean” food**
 - Natural, local, seasonal
- **More spice**
 - Beyond Sriracha
- **Expanded breakfast segments**
- **Craft beers**
 - India Pale Ale (IPA) rules
- **Wine types**
 - Popularity of lesser known varietals
- **Fried is back**
 - Chicken and seafood
- **Coffee segment grows**
 - Nitro is the next wave



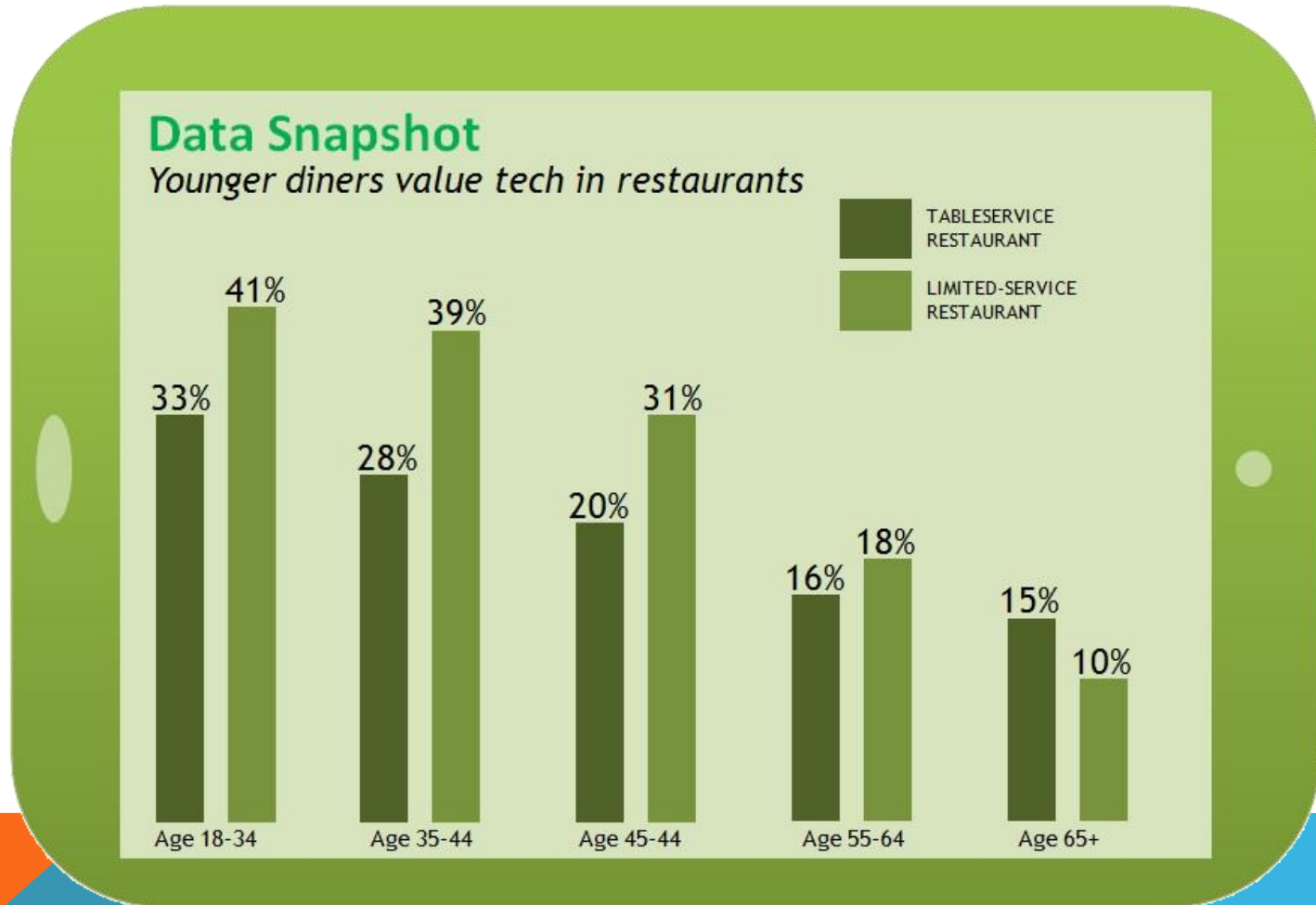
WHERE ARE WE GOING?



Smarter, Smaller, Faster



AND THEN THERE IS... TECHNOLOGY!

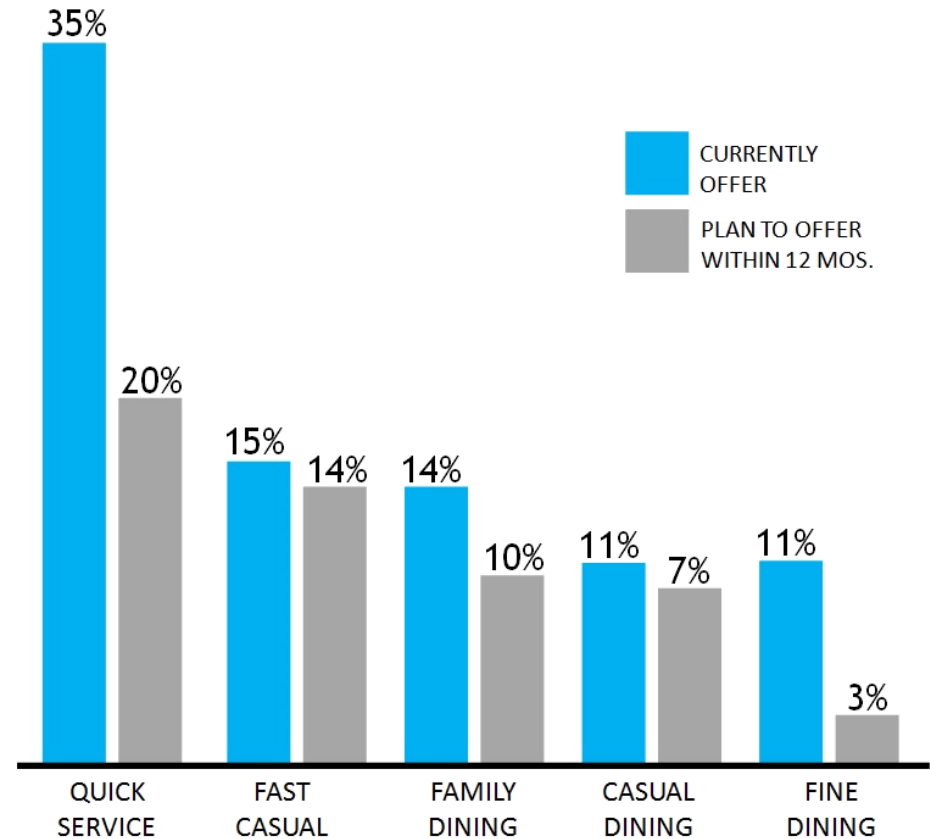


Source: National Restaurant Association, Restaurant Trends Survey 2014



THE MOBILE MOVEMENT

Adoption of mobile payment is growing across the board, but quick-service operators lead the pack, with more than half offering or planning to offer the service.



Source: National Restaurant Association, Restaurant Trends Survey 2014



MENU JOINS THE TECH MOVEMENT

Consumers use smartphones or tablets for following activities at least once a month:

- 31%** View menus
- 28%** Look up locations, directions or hours
- 27%** Order from restaurant's website or app
- 23%** Read online reviews
- 23%** Use rewards or special deals
- 18%** Make reservations
- 16%** Look up nutrition information
- 11%** Pay for meals
- 9%** Order via aggregate website or app (Seamless, Grubhub, etc.)



DELIVERY OF THE FUTURE



WHAT THINGS COST*

	<u>Full-Service</u>	<u>Limited Service</u>
Cost of Sales	32%	31%
Salaries-Wages	33%	34%
Direct Operating	15%	12%
G&A	5%	5%
Occupancy	8%	10%
Pre-Tax Profit	<u>7%</u>	<u>8%</u>
	100%	100%

*National Restaurant Association



LABOR ISSUES



- Minimum Wage
- Salary Exception
- Tip Claim – Tip Share
- Service Charges
- Menu Price Increase
- Insurance – Benefits
- Joint Employment



EXPANSION AND EXIT STRATEGIES



- Expansion
 - Capital and Operational Needs
- Structuring and Preparing for a Capital Event
- Franchising
- Succession Planning



OPERATING CONCERNS, STRUCTURE FOR EXPANSION

Capital Concerns

- Corporate Owned Chain
 - Operator capitalizes all aspects of the expansion
 - Assumes most of the liabilities
 - Usually seeking private investor money
 - Be mindful of complex structuring from outset as it may be a barrier for a larger capital event or institutional investor



OPERATING CONCERNS, STRUCTURE FOR EXPANSION

- **Capital Concerns**
 - Franchise – Not Always Quickest and Cheapest
 - Franchisees provide capital to open their locations
 - Operator though must fund regulatory requirements and compliance issues
 - Need to hire franchise management (in-house or third party) system
 - Significant capital spent on marketing the concept to potential franchisees
 - Must have working capital to sustain the system until franchisees pay initial fees and start paying royalties
 - Debt is usually more easily available
 - Structure may be simpler and more attractive to institutional money



OPERATING CONCERNS, STRUCTURE FOR EXPANSION

Structuring – Corporate v. Franchise

- Launching a second corporate owned restaurant is fairly simple, though operating and managing it only gets more complex with more administration and oversight needed – from a distance – training is vital



OPERATING CONCERNS, STRUCTURE FOR EXPANSION

Structuring – Corporate v. Franchise

- Launching a franchise system is not easy, though you are not responsible for on-site management
- In addition to operating your original restaurant location (and any other corporate locations), the principal will now be:
 - Managing and growing a franchise system
 - Marketing the concept
 - Supporting Franchisees, while also driving the concept development and implementation



OPERATING CONCERNS, STRUCTURE FOR EXPANSION

Regulatory Issues

- Franchising is regulated by the Federal Trade Commission as well as state governments
- Before offering franchises for sale, the principal needs to prepare a Franchise Disclosure Documents (FDD)
 - Requires revealing information such as business's financial statements



OPERATING CONCERNS, STRUCTURE FOR EXPANSION

Regulatory Issues

- With a corporate owned chain, the operator needs to comply with the usual state and local laws and licensing requirements regarding restaurants, but the regulations may be less complex.
- Though franchisor will be the guiding factor and backstop to assist franchisees through hurdles



OPERATING CONCERNS, STRUCTURE FOR EXPANSION



Employment Complexities

- Multi-Jurisdictional Operations
- Multiple Governing Bodies
- Ever Changing Landscape of Laws



OPERATING CONCERNS, STRUCTURE FOR EXPANSION

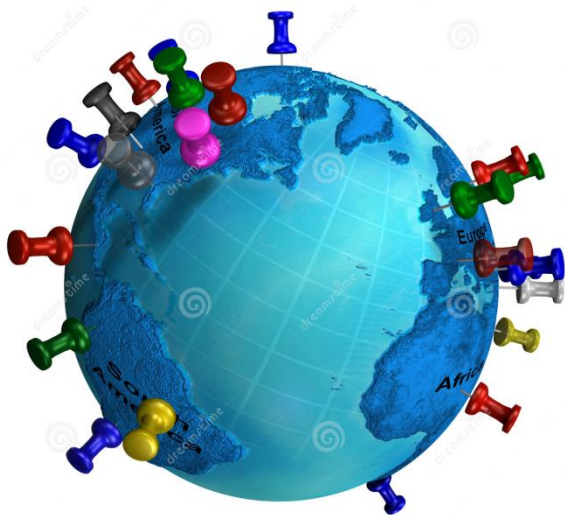
Site Selection



- Leverage in Real Estate Negotiations
 - Market is quite high for commercial retail real estate in prime markets and emerging markets
 - Pressure to grow could lead to poor site selection or ill-fated real estate deals – landlord can be most important partner
 - Prime location not always sustainable



OPERATING CONCERNS, STRUCTURE FOR EXPANSION



Geographic reach

- Consistency through systems, relationships and training is critical
- If you want to be the next Five Guys, franchising may be better way to achieve that goal
- If you just want to open a handful more locations in your city or state, you're better off structuring as a corporate owned/managed chain



OPERATING CONCERNS, STRUCTURE FOR EXPANSION



Geographic reach

- Managing restaurants over a wide geographic area unwieldy very fast
- Often overlooked:
 - The administrative work that comes with multiple business operations – build a solid team
 - The traveling required and the strains of it



FINANCING EXPANSION...WHERE IS THE CAPITAL

Equity Financing

- Traditional – Regulation D – 506(b)
- Crowdfunding - Regulation D – 506(c)
 - JOBS Act - Title II
 - JOBS Act – Title III



FINANCING EXPANSION...WHERE IS THE CAPITAL

Debt Financing

- Traditional – Convertible or Otherwise
 - Apple Pie
- SBA Loans
- Crowdfunding



Traditional 506(b) Offering

506(c) Title II Offering

Communications with Investors	Companies may not advertise their security offering. Generally, companies may approach potential investors if there is a substantive, pre-existing relationship.	General advertising permitted. Companies may advertise via social media, email, or offline. No substantive, pre-existing relationship with potential investors required.
Eligible investors	Accredited investors and up to 35 non-accredited investors who meet sophistication requirements.	Only accredited investors.
Accreditation Process	Self-certification via a questionnaire is the general standard.	Companies must take reasonable steps to verify accredited investor status. Self-certification via a questionnaire is not permissible.
Offering size	No limit on offering size.	No limit on offering size.
Disclosure	Companies must decide on what information to provide to accredited investors, but that information must not violate antifraud prohibitions. If non-accredited investors are included, companies must provide those investors with disclosure documents that are generally the same as those used in registered offerings. If a company provides information to accredited investors, it must make that information available to non-accredited investors as well. Companies must be available to answer questions from potential investors.	Companies must decide on what information to provide to accredited investors, but that information must not violate antifraud prohibitions. Companies must be available to answer questions from potential investors.
Filing Requirements	Form D and Blue Sky in states where offering	Form D and Blue Sky in states where offering



TYPES OF CROWDFUNDING

Donation

Contributors support a cause they believe in

Rewards

Contributors receive non-monetary incentives

Equity

Investors receive ownership of business

Debt

Investors receive monthly principal and interest



TITLE III CROWDFUNDING

- **May 6, 2016**
 - Becomes effective
- **January 29, 2016**
 - Crowdfunding Portals were able to start applying to the SEC



TITLE III CROWDFUNDING

Allows a company looking for capital to:

- Advertise to potentially every investor in the world, using the Internet
- Raise up to \$1 million of capital every 12 months
 - From everybody, including non-accredited investors
 - At potentially a much lower cost than has ever been possible before



POSSIBLE USES OF TITLE III CROWDFUNDING

If you want or need to raise money from more than a handful of non-accredited investors.



EXAMPLE 1

A restaurant company needs \$5 million to expand into multiple units and brand the company. It could raise a majority of the money it needs from accredited investors, but would also like to involve non-accredited neighbors. Can raise up to \$1 million through marketing to the communities you plan to open in.



POSSIBLE USES OF TITLE III CROWDFUNDING

EXAMPLE 2

The restaurant company wants to raise \$875,000 for its new concept and does not feel it has connections to or exposure to a large network of accredited investors. This may be the same case for a new early expansion unit in a new market.



POSSIBLE USES OF TITLE III CROWDFUNDING



EXAMPLE 3

A company needs \$350,000 for a new branding and marketing platform. With a clever social media campaign, the company might identify thousands of potential investors from those that are fans of the existing brand.

Remember though that there are administrative and tax costs associated with having many smaller investors so structure properly.



PROBABLY SHOULD NOT USE TITLE III

- If your restaurant enterprise just needs capital and nothing else, then you're probably going to have an easier time raising the capital from accredited investors using more traditional methods under 506(b) or Title II.
- If you need lots of capital from non-accredited investors, then you might as well use Title IV (Regulations A+). This is a private placement more akin to a public offering though and has many hurdles and disclosure and compliance requirements



DEBT OPTIONS -

- More exposure but usually cheaper money that restaurateurs don't always think about because the \$\$\$ are smaller
- Private Debt
- Bank Debt
 - Traditionally Sourced (SBA)
 - Online Sourcing
- Crowdfunded Debt



QUESTIONS?





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