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The Best Financing Ideas of 2014

By Dennis L. Monroe

2014 was an exciting year: Financing not only continued to be available, but we saw several new and innovative approaches. Here are my thoughts on the best financing ideas of 2014:

Effective Use of IPOs
We've seen a number of significant restaurant IPOs in 2014: Potbelly, Zoe's Kitchen and Papa Murphy's. Much was spurred by strong valuations and the market accepting smaller IPOs; private equity groups seeking to exit their investments; and certain changes in the securities laws that made smaller IPOs more accessible, less complicated and requiring less filing. I think the trend of smaller IPOs will continue in 2015. Certainly, smaller IPOs set up the company for add-on offerings which help with further funding for growth.

The Growth of Crowd Funding
Crowd funding is becoming common in the restaurant industry, particularly with the advent of new companies that package crowd funding in the form of both debt and equity.

There are primarily two types of crowd funding used today:

1. **Donation/rewards-based crowd funding**, which involves straight contributions in exchange for small, nominal rewards (on websites such as Kickstarter and Indiegogo), has been around for several years and is popular among independent and start-up restaurant concepts. These campaigns generally raise smaller amounts (anywhere from $10,000 to $100,000) and are seen as a form of goodwill or community involvement to help build upon a project or idea. No equity is exchanged, so they are a great way for restaurants to fund initial seed money or special projects without giving up ownership.

2. **Accredited Investor Portals**, which involve equity and debt offerings (through websites such as AngelList, EquityNet, and EarlyShares) were made possible by Title II of the JOBS Act and the easing of the general solicitation and general advertising rules. These websites essentially bring Rule 506(c) offerings online, as only accredited investors are allowed to access and purchase securities. The portals must be managed by a registered broker/dealer, who verifies accredited investor qualifications and processes subscriptions.

Title III of the JOBS Act promised to open up crowd funding to non-accredited investors; however, the final rules have been delayed in rulemaking, as the SEC has grappled with how to properly protect non-accredited investors without placing undue limitations and reporting hardship on issuers. Several bills were introduced in Congress this summer to help put in some parameters and resurrect Title III.

Private Equity's Interest in Emerging Concepts
In 2014, PE groups showed significant interest in emerging concepts. Buffalo Wild Wings stepped into this world again and acquired Rusty Taco. Sentinel Capital Partners bought Newk's—both deals show PE's interest in smaller, emerging concepts. Private equity is creating its own deals by acquiring operating companies and serving as the primary operator. I see no end in sight for PE funding emerging concepts.

EB-5 Funding Stepping up to Its Next Level
EB-5 funding has evolved into the mainstream. This year LCR Capital Partners launched an EB-5 project dedicated to the franchise sector. This looks much like a favorable loan program and seems to fit the needs of our industry. Individual EB-5 funding through various kinds of intermediaries also continues to grow. For example, new groups have emerged that offer bridge financing, so the restaurant owner has an opportunity to access EB-5 funding right away instead of waiting for the process to conclude, which can take up to six months.

Greater Interest by Small Community Banks
Community banks have become viable sources for funding restaurant development. They have been buying loans and doing other things to get a higher rate of return than they can get on their investments, thereby becoming good sources of funding. If you take the time to explain the value of restaurants and cash flow (and do a little background on how restaurant loans are underwritten), it is amazing how responsive they can be.

Creative Use of 401(k)s or Self-Directed IRAs for Financing
If the account is set up correctly, money from for these types of accounts can be a useful source for investing in the restaurant industry—particularly since the return is higher than the current market's. Normally these types of investments are known as an alternative investment class. Often, the financial company that manages your 401(k) or self-directed IRA is reluctant to approve this investment type, and it will typically require a waiver and release from you in order to proceed. But the cash flow that comes from restaurants and the growth potential could bring a wonderful return on retirement investment.

Owner-Created and Sold Private Placements
The greatest growth has been in private placement financings. Again, with the liberalization of some of the securities laws (especially relating to the solicitation and advertising to accredited investors and the improving economy), private placements have become more popular. The private placements are not using a broker; in most cases,they are being sold by the

restaurant owner to friends, family and close business associates. Normally, private placements are structured as a preferred class of stock, with the investor getting the money back first and possibly getting a modest return before the owner can take out a significant distribution. There is usually a management fee associated with this to keep the owner interested.

Use of Institutional Investors

One of the game changers in 2014 was the ability of Flynn Restaurant Group to secure funding from a retirement fund and refinance its existing debt. We haven't seen many institutional investors play in the non-public restaurant space or with franchisee companies. The results Flynn achieved in its institutional transaction is a tremendous accomplishment.

I think 2015 will be more of the same, with more refinances and syndications as people try to continue to take advantage of low interest rates. Financing across multi-concept lines will continue to get easier. Lastly, crowd funding will be a much bigger part of our industry—and that's exciting.

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