RESTAURANT FINANCE MONITOR®

Volume 33, Number 9 • Restaurant Finance Monitor, 2808 Anthony Lane South, Minneapolis, MN 55418 • ISSN #1061-382X

September 15, 2022

Effective Use of Equipment Leasing

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You can't pick up a restaurant periodical lately without reading how concepts are addressing consumer issues, technology and looking to refresh concepts and individual locations. And while these improvements are certainly necessary, they sometimes can be difficult to finance. This is particularly true since most restaurant companies already have used their PPP and ERC dollars. Further, if a restaurant company has underlying bank financing, the bank may be reluctant to increase that financing in these uncertain times.

One solution is to take advantage of equipment leasing, which is an overlooked source for financing new equipment, leaseholds and technology, as well as overall remodels. Sometimes franchisors provide a financing source for required improvements, and often this financing involves the use of third-party equipment leasing versus overall balance sheet financing.

The equipment leasing arena has been around since day one of restaurant financing. Early on it was just about all that was available, besides real estate sale/leasebacks, which in many cases included an equipment component.

With availability of bank financing, equipment leasing has taken a backstage to balance-sheet financing, but I think there is still an important role for equipment leasing in the restaurant industry.

First off, the definition of "equipment" can be fairly broad. It can refer to leaseholds, and may even include soft costs. In general, the Equipment Leasing Companies (ELCs) I have spoken to are flexible as it relates to what the funds can be used for. ELCs also may take unencumbered existing equipment to create a line of credit.

The rates are the one drawback I always hear when I suggest equipment leasing. This is riskier financing and many times there are personal guarantees required, but in general the ELCs are looking at the cash flow of the business with some value to the equipment or property.

A bonus is that equipment leasing has a lot of flexibility, and it may be a way to deal with a blanket lien filed by the bank for overall financing. It also may be a way to get much-needed improvement dollars, particularly if you are willing to pay a higher rate and faster amortization debt.

Also, in equipment leasing, the payoff is not like a loan that you amortize so much a month, then pay off the principle. Equipment leasing is a fixed obligation for a number of payments. You can always prepay, but it usually requires making all future payments in a lump sum.

Vendor financing is another place where equipment leasing has been used effectively, where vendors, such as ice machine manufacturers, provide the financing for their products. Also, in some franchise systems that require updated equipment—or IT, hardware and software or other improvements—the franchisor may help provide an ELC source and an effective backup guarantee for their system.

There are a couple of legal constraints of which you should be aware: The reason equipment leasing is utilized is because it can be an effective way to retake assets. For instance, when a bank makes a loan to buy equipment it does a UCC-public filing securing the equipment. Then in order to take the property back, set procedures have to be followed, which can be somewhat arduous. And a bankruptcy, if there is one, can stall the process. Whereas with equipment leasing, the equipment's title is held by the ELC.

For real-world examples, I interviewed two senior executives of two well-known ELCs. Director of Business Development Brian Bourne at KLC emphasizes the complete flexibility of equipment leasing and how it's an effective way to provide 100% financing. KLC's products allow for including leaseholds, soft costs and acquisition financing including used equipment.

Ryan Driscoll, vice president of sales for direct and franchise for Ascentium Capital, a division of Regions Bank, said there is little activity in the tax lease world and most of their customers utilize an Equipment Financing Agreement (EFA). Assets that can be financed include new store build-outs and drive-thrus.

As we all plow into this new restaurant environment, looking for new ways to finance shouldn't preclude the tried-and-true vehicles. Equipment leasing is an effective tool, and not entirely your "parents' Oldsmobile."

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