



TAKING FLIGHT

AUSPEX CAPITAL'S Q2 2020 NEWSLETTER



BEYOND COVID-19: A LOOK AHEAD FOR THE RESTAURANT INDUSTRY

On April 15, Auspex Capital's Managing Director, Christopher Kelleher, joined a panel of restaurant finance and legal experts for a *Franchise Times* webinar to discuss the outlook for the restaurant industry. Access a recording of the webinar on Auspex Capital's website.

PAYCHECK PROTECTION PROGRAM: PREPARING FOR THE LOAN FORGIVENESS AUDIT

The federal government's Paycheck Protection Program ('PPP') has made \$660 billion in potentially forgivable loans available to small businesses struggling to survive the economic disruption caused by the COVID-19 pandemic. Although the program was crafted with unusual bi-partisan support and was initially very well received by both the business community and the general public, in recent weeks the program has been tainted by the revelation that a significant number of large loans were made to high profile companies like Ruth's Chris, Shake Shack and the Los Angeles Lakers that do not fit the public perception of a needy small business. In the wake of the intense negative publicity, Secretary of the Treasury, Steven T. Mnuchin, announced that prior to approving forgiveness for any PPP loan of \$2.0 million or more, the Small Business Administration ("SBA") will conduct an audit of the borrower to confirm that the need certification provided by the borrower was true and accurate.



Although there has been very little guidance from the SBA about the scope and depth of the audits, it is imperative that any PPP borrower that got a loan of \$2.0 million or more be fully prepared for what will likely be a detailed and comprehensive audit. While the audit will likely not take place for several months, the time to prepare for it is now when the facts and circumstances that drove the decision to take the PPP loan are still fresh and clear. We recommend that each entity that received a PPP loan of \$2.0 million or more prepare a detailed and thoughtful memorandum which clearly and persuasively makes the case for taking the loan. The outline below will help you organize your presentation.

A. Critical Dates

1. Application Date(s)
2. Funding Date(s)
3. May 7, 2020 (Final Date to Return Funds with no questions asked)

B. Original Certification Standard

Borrower to certify that: *"Current economic uncertainty makes this loan request necessary to support the ongoing operations of the applicant."*

C. Revised Certification Standard

Added to the original certification standard was the following: *"Borrowers must make this certification in good faith, taking into account their current business activity and their ability to access other sources of liquidity sufficient to support their ongoing operations in a manner that is not significantly detrimental to the business."*

D. Suggested Documentation Necessary to Support the Required Certification

1. Financial Performance Issues:

1. Daily sales trends at each Critical Date
2. Daily transaction count trends at each Critical Date
3. Cash on hand at each Critical Date
4. Total working capital at each Critical Date
5. Projected cash burn rate at each Critical Date
6. Overall brand sales and transaction count trends at each Critical Date

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We're pleased to welcome two professionals to our team - Ben Nguyen and Karen Li!

Christopher Kelleher, Managing Director

AUSPEX WELCOMES TWO NEW TEAM MEMBERS

The Auspex Capital team continues to grow, adding two new professionals to our ranks. Auspex welcomes Ben Nguyen and Karen Li. In January, Ben officially joined the team after a very successful internship with us last year, and Karen Li joined the team in February as a Senior Analyst. Prior to joining Auspex Capital, Karen was a Senior Financial Quantitative Analyst at East West Bank. We're pleased to welcome both of these talented individuals to the team!



Ben Nguyen and Karen Li

PAYCHECK PROTECTION PROGRAM: PREPARING FOR THE LOAN FORGIVENESS AUDIT

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II. Senior Lender Issues:

7. Document lender's ability to declare a loan in default as a result of a Material Adverse Change
8. Calculate pro forma financial covenants at each Critical Date to assess the risk of breaches which would allow the lender to terminate future funding obligations and potentially accelerate loan repayment
9. Document the temporary nature of lender relief packages that, while they provided some temporary relief, rapid re payment requirements impact near term solvency/viability.
10. Revolving line of credit annual out of debt requirements.
11. Identify any near-term balloon loan maturities.

III. Other Business Issues:

12. Identify any supply chain disruption issues, potential protein shortages and commodity cost volatility that are, or are likely to, impact the business.
13. Document the temporary nature of franchisor, landlord or vendor relief packages. While the programs may have provided some temporary relief, rapid repayment requirements impact near-term solvency/viability.

14. Status of dining rooms open/closed at each Critical Date
15. Local City/County/State Ordinances, regarding shelter in place at each Critical Date
16. Change to hours of operation due to local government ordinances
17. Document day / date of stimulus checks
18. Document any on-going remodel / construction projects
19. Document any remodel / construction / purchases that were put on hold
20. Document any emergency capital expenditures
21. Document any staffing issues and incentives / bonuses offered to retain / attract employees
22. Document any restaurant closures as a result of any employees testing positive with COVID-19
23. Document any layoffs, furloughed employees
24. Document employees brought back to work as a result of PPP funding

AUSPEX SUPPORTS CLIENTS THROUGH THE COVID-19 CRISIS

In response to the significant impact the COVID-19 crisis is having on the restaurant industry, Auspex Capital has ramped up its debt restructure and strategic advisory practice. We are actively working with clients in support of their PPP application process, developing strategies to maximize PPP loan forgiveness, crafting of creative payment deferral programs with franchisors, lenders, landlords and other critical vendors, and assisting management with the development and continuous refinement of cash flow models to help them navigate through the crisis. "Auspex has eight senior bankers on its team, all of whom have at least 10 years of experience in restaurant finance. We were all heavily involved helping our restaurant clients successfully navigate through the 2008-2010 financial crisis and we are all now committed to getting our clients through the current contagion," said Chris Kelleher, managing director of Auspex. For more information about Auspex Capital's capabilities and how we can help, please contact Chris Kelleher at ckelleher@auspexcapital.com or (562) 424-2455.