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NRN NATIONAL REPORT

Emergency: Industry seeks Rx for construction delays, stat!

By Milford Prewitt

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Both in boisterous big cities where time is money and in rustic farm towns where life is slow and simple, construction delays are costing the restaurant industry millions of dollars every week, according to foodservice real-estate experts.

Some operators say they never before had known a time when it was more difficult to get the permits from zoning boards that are necessary for architectural preservation committees, historical societies, community groups and others that have a say in what gets built from city to city.

Alan Ackerberg, vice president of construction and director of design for Minneapolis-based Buca di Beppo, the 107-unit Italian dinnerhouse chain, said something as simple as a building's color scheme — which a board member may dislike — is enough to delay a project.

"And you ask these guys, 'Show me in the code where it says that,' and they can't [use a particular color]," he explained.

"They just infer something from the code that's going to cost you money and time. So much of it is a power game."

But the colors chains choose as distinct but uniform expressions of brand identity are but one of myriad design features or location elements that can rub a regulatory official the wrong way and delay the zoning and permit issuance process.

Beyond colors, there are many reasons why restaurants in the development stage either die on the vine or struggle to reach fruition. They include the shape of a roof, access to water and sewerage, the time it takes fire and health inspectors to show up to certify finished projects, the use of drive-thru window bays and a range of environmental issues.

"I've been here 26 years, and I can tell you that 10 to 15 years ago maybe you'd run into some zoning or permitting problem with maybe one out of every 10th or 15th location; now it's down to one out of four," said Bill Niegsch, chief financial officer of the 90-unit Max & Erma's casual-dining chain, based in Columbus, Ohio.

"Those local planning commissions [and] zoning boards are really making you jump through hoops these days," Niegsch continued. "And so much of it is as unreasonable as it is unbelievable. It's almost as if they don't want new businesses, new revenue streams for taxes or new employers in town."

As an example, Niegsch pointed to one of his chain's new branches, in a suburban town that he asked not be identified because he feared offending city fathers and risking retribution.

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NEWS

Industry seeks Rx for construction delays

He said the unit debuted several weeks behind schedule and about $170,000 above the company's average construction cost because one board member demanded that Max & Erma's build the restaurant with a pitched roof, either A-Shaped or triangular, instead of with the brand's traditional flat-roof construction.

Although other nearby retailers have pitched roofs on the avenue on which Max & Erma's had staked out its site, what was perplexing to Niegsch about the ruling, he said, was that the restaurant's immediate next-door neighbor was a Walgreen's with a flat roof.

In another town in another state Max & Erma's is contemplating abandoning a project where it might forfeit as much as $75,000 already spent on architectural and legal fees. In that case not only was the company prepared to spend about $200,000 on needed soil improvements to make the site more conducive for building, but the city planners also want the company to put another $200,000 in dazzling architectural features.

"The vast majority of those things can be done pretty efficiently, but what I see happening is that increasingly the fixed costs you have to invest in a new restaurant are going to make it terribly difficult for the unit to become profitable," Niegsch said. "The planning commissions say they don't want any ugly buildings in their town. But what is uglier: to have a boarded-up, closed restaurant on Main Street that couldn't make it because its fixed costs were too high?"

Brendan Sharkey, a land-use attorney who founded and is president of AmeriZone, a Hamden, Conn.-based firm that specializes in expediting zoning and permitting challenges for national chains, agreed with Niegsch that operators lately are paying more money and spending more time to surmount planning-commission critics.

He said he recently researched the uniform-franchise-offering circulars of 12 major restaurant brands just in one state, Rhode Island.

He was surprised to discover that all of the brands prominently mentioned that they were spending more money and having to do more due diligence to satisfy zoning boards and other regulatory bodies in order to construct new branches.

From that Rhode Island microcosm, Sharkey estimated that major franchisees and franchisors might be losing millions of dollars each week because of construction delays linked to zoning and permitting problems.

"Start doing the math and figure out that the average weekly gross for some of the major Q SRs is typically in the $10,000 range, from which the franchisor gets about a 6-percent royalty fee," Sharkey calculated. "Then figure that the major players talk about opening 300 to 400 new units a year.

"What you start to realize is that just in one week any construction delay related to zoning or permitting is a costly proposition for the industry. Multiply $10,000 times the 6-percent royalty fee times the number of units that hit a snag in the development stage and just in one week you are easily talking a quarter of a million dollars or more in lost revenues. For a small franchisee who is ready to go, that could be devastating if the delay lasts more than three weeks."

Sharkey asserted that restaurant chains, especially up-and-coming brands that have not developed in-house real estate and construction competencies, have begun treating permitting and zoning issues as a separate specialty requiring either outside consultants or home-grown professionals.

Paul Fetscher, president of the Great American Brokerage, Long Beach, N.Y., which specializes in restaurant and retail sites, said Sharkey's research did not surprise him.

Sharkey, in addition to what Fetscher described as quirky demands by zoning boards and skeptical neighborhood groups, said he has seen more and more projects being stalled because of environmental issues.

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Moreover, he said, when it comes to shopping-mall developments that envision restaurants as key tenants, a rash of lawsuits that only serve to increase the costs of new projects and delay them has sprung up between competing developers.

He said one lawsuit citing zoning and environmental issues delayed the construction and opening of the Palisades Center in West Nyack, N.Y., for nearly 10 years. Since opening in 1998,the 3.2 million-square-foot mall —which has restaurants that include nearly a dozen national brand-name dinnerhouses — has become one of the nation's most successful retail centers

In one of the most recent examples Fetscher cited, the real-estate development arm of Hartz Mountain Industries of New Jersey recruited the Sierra Club to join in a lawsuit against the Mills Corp. of Arlington, Va. The Mills Corp. plans to build a 2 million-square-foot shopping center called Xanadu in the Meadowlands complex, which is home to New Jersey's professional sports teams.

The lawsuit contends that Mills Corp., a major mall developer, had not researched sufficiently the environmental impact of Xanadu on the local community.

Fetscher cited a noted endangered-species case in observing,"Ever since the day when the snail darter raised its ugly head, operators have been spending more and more dollars to resolve environmental issues that often have nothing to do with their businesses."

Buca di Beppo's Ackerberg contended that if operators were to launch projects knowing that certain markets are tougher than others in terms of development hassles, the restaurants still could be finished in a timely manner.

When a brand is expanding into cities or towns where it has no significant market presence, Ackerberg argued, it is important to court relationships with local consultants and brokers, even competitors, to find out how to tailor the project in the right light.

"The thing is you don't want to be surprised,"Ackerberg said. "You don't want to be deep into the final stages of construction and suddenly get hit with something you didn't plan for.

The key is predictability. Whether it takes 120 days to build a restaurant or 200 days, it really doesn't matter. It's the surprises you want to be on guard for. Predictability is the key for a successful project."

But sometimes a developer's only choice is to walk away from a project in order to maintain the integrity of the brand, said Patrick Lenow, a spokesman for IHOP Corp. of Glendale, Calif.

He said one of the worst-performing restaurants in the 1,700-unit chain is in a former church building in which IHOP sacrificed its signature design features in order to appease an inflexible zoning board. Declining to identify the city, Lenow complied with demands to conform to community aesthetics.

"You want to be part of the community, you only want to be a good neighbor and get along with city leaders, so we opened this IHOP in a church with a strange roof shape, a parapet and an all-brick façade," Lenow said. "It looks like no IHOP anywhere in the country, and we think the reason it is underperforming is that people don't recognize it as an IHOP.

"I doubt if we'll make that mistake again. It's one of those lessons learned."

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