NATIONAL RESTAURANT ASSOCIATION®

REPRESENTING, EDUCATING AND PROMOTING THE RESTAURANT INDUSTRY

Written Testimony

of

Fred Rosenthal
President, Jasper's Restaurants

for the hearing

Modernizing the Tax Code: Updating the Internal Revenue Code to Help Small Businesses Stimulate the Economy

before the

U.S. House of Representatives
Committee on Small Business

on behalf of the

National Restaurant Association

Thursday, April 10, 2008

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Chairwoman Velazquez, Ranking member Chabot, members of the House Committee on Small Business; thank you for the opportunity to testify before you today of behalf of the National Restaurant Association. My name is Fred Rosenthal of Bethesda, Maryland and I am the President of Jasper's Restaurants.

I have been a part of the restaurant industry for more than 40 years. I trained with many of New York's top caterers while attending New York University's School of Business for hotel and restaurant management. After graduation, I joined a new catering company in Baltimore, MD and for the next 15 years helped grow that operation to include seven banquet facilities, the largest accommodating 1500 guests. The company also expanded into contract feeding – winning several key contracts in Baltimore. After selling my interest in this catering venture, I joined Mr. Berk Motley and Mr. Patrick Noonan, opening the original Jasper's Restaurant in Greenbelt, MD in 1981. I am the principle of the entities that operate the three existing Jasper's Restaurants in Greenbelt, Crofton and Largo, and the Jasper's American Grille which opened in 2007. I am immediate past Chairman of the Board of the Restaurant Association of Maryland and continue to remain actively involved with the industry and small business issues.

I am proud to be a part of an industry that plays such a significant role in this nation's economy. There are 945,000 restaurant/foodservice outlets in this country. Seven out of ten restaurants are single-unit operators. The restaurant industry is an industry of small businesses.

This year the restaurant industry is estimated to generate $558 billion in sales, with an overall economic impact of $1.3 trillion. Every dollar spent dining out generates $2.34 in business for other industries.

We are the nation's second largest employer outside the government, employing more than 13.1 million people, representing more than 9 percent of the job-base. We are truly the cornerstone of this nation's economy.

On any given day 133 million individuals are patrons of a food establishment. Given the industry's contributions to the economy, we strongly urge the committee to include reforms to restaurant building depreciation schedules among those tax items considered to help spur this struggling economy. Depreciation schedules must also be broadly re-examined during the larger tax reform debate over the next several years.

Depreciation Schedules Must Be Updated To Help Stimulate the Economy

Depreciation schedules for commercial real estate, including restaurant buildings, have not been significantly revised since they were established. It is time to take another look at these schedules so that they more accurately reflect the life of the property. According to the tax code, commercial real estate generally has a 39 1/2-year depreciable life for the original building and for any subsequent renovations or improvements to the building. Restaurants have gained some temporary relief through tax extenders packages but nothing that provides reliable relief that will encourage longer term investment and planning.

Restaurants operate on industry average margins of four to six percent and every penny counts, especially for small businesses and independent restaurateurs. Depreciating property over a shorter amount of time has a direct impact on a restaurant's bottom line by allowing a restaurateur the immediate cash flow to reinvest in their business.

Changes have been made that allow certain industries that directly compete with restaurants to benefit from shorter schedules. These schedules range from seven years for food outlets located in amusement parks to 15 years for gas stations/convenience stores. This favorable depreciation schedule has allowed convenience stores to expand and improve their foodservice options – a direct competitor to quick service restaurant operators.

Legislative History of Accelerated Restaurant Depreciation

The economic stimulus package passed in the 107th Congress, allowed for 30 percent bonus depreciation for certain assets, (such as assets depreciated over a 20 year schedule or less). As part of the 9/11 economic stimulus package, this provision was expanded to include any leasehold improvements (currently depreciated over a 39 ? year schedule). However, owner-occupied properties were not included.

The American Jobs Creation Act of 2004 established that restaurants could depreciate qualified restaurant building improvement costs over 15 years for property in place by the end of 2005. This provision applied to both leased and owner-occupied buildings. The Tax Relief and Health Care Act of 2006 extended the existing provision through the end of 2007.

The Minimum Wage/Small Business Tax Relief bill (H.R. 2) that passed the Senate on February 1, 2007 contained a provision which would have extended the improvement piece through March 31, 2008, and would also have added 15-year depreciation for new restaurant construction from the date of enactment through March 31, 2008. A subsequent Senate Finance Committee package included the extension of qualified leasehold and restaurant improvements through December 31, 2008 and added new construction from the date of enactment through

December 31, 2008. However, all depreciation provisions were removed from the final package that was enacted into law.

As of January 1, 2008 all schedules reverted back to 39 1/2 years, including improvements made to restaurant structures both leased and owner-occupied. When Congress passed and the President signed the Economic Stimulus Act of 2008, the legislation included a bonus depreciation tax provision as well as increased Sec. 179 small business expensing. However, the restaurant industry can not take advantage of the bonus depreciation provision for even the improvements we had previously because the provision only applies to property on a 20 year or less depreciation schedule. As a result, the positive impact of the economic stimulus package was not as great as it could have been for the restaurant industry and our communities.

There are currently two bills in the 110th Congress which address accelerated restaurant depreciation for new construction and improvements. H.R. 3622, championed by Congressmen Kendrick Meek (D-FL-17th) and Patrick Tiberi (R-OH-12th), would make permanent a 15 year depreciation schedule for newly constructed restaurants as well as restaurant improvements. The bill currently enjoys the bipartisan support with 113 cosponsors, including 10 members of this committee. Senators Kay Bailey Hutchison (R-TX) and Jon Kyl (R-AZ) introduced companion legislation, S. 2170, that also has bipartisan support.

Restaurant Building Depreciation

The National Restaurant Association believes the depreciation changes that have been made in the past for certain industries and the exclusion of the new restaurant construction provision have placed certain businesses at an economic disadvantage. The tax code should not pick winners and losers in the restaurant industry; it should allow a level playing field on which all can compete.

Within the retail industry, restaurants have a unique case for accelerated depreciation schedules. As mentioned earlier, 133 million individuals are patrons of the industry on a daily basis. Restaurants must constantly make changes to keep up with the daily structural and cosmetic wear and tear caused by customers and employees. Restaurants get more customer traffic than other commercial businesses. Many are open 24 hours a day, seven days a week. This heavy use accelerates deterioration of a restaurant building's entrance, lobbies, flooring, restrooms, and interior walls. Restaurant building structures therefore experience a daily human "assault" unlike that borne by any other types of buildings in the retail industry.

Most restaurants remodel and update their building structures every six to eight years – a much shorter timeframe than is reflected in the current depreciation schedule. Many of these refurbishments are not treated as improvements under the tax code, but as new construction because these remodeling projects require changes to structural walls. Thus, creating layer upon layer of depreciation schedules for every periodic update or new construction.

Also, many franchise agreements contractually require the evaluation of the location, and quality and configuration of the restaurant structures routinely. Franchisees are small business owners and they bear the cost of updating their buildings or completing scrape and build projects, which are often written into their agreements. While these scrape and build projects may be considered renovations in their agreements, the tax code treats these as new construction.

The above-mentioned renovations and structural improvements made to restaurants every six to eight years come at an average cost of $250,000 --$400,000. This year alone the restaurant industry is expected to spend in excess of $5.5 billion on capital expenditures for building construction and renovations. The restaurant industry is projected to spend over $70 billion over the next ten years for building construction and renovations. These more-than-modest expenditures in turn have a significant economic impact on businesses performing these renovations. Like the restaurant industry, growth in the construction industry will reverberate throughout the economy. According to the Bureau of Economic Analysis, every dollar spent in the construction industry generates an additional $2.39 in spending in the rest of the economy, while every $1 million spent in the construction industry creates more than 28 jobs in the overall economy.

If there is any question whether shortened deprecation schedules would spur economic activity consider the fact that after Congress enacted the restaurant improvement provisions in 2004, the restaurant industry spent more than $7.4 billion on new structures and building improvements in 2005 – a 42 percent increase over the $5.2 billion spent in 2004 (according to the U.S. Census Bureau).

The additional spending – fueled by a shorter depreciation schedule – created thousands of jobs in construction-related industries across the country. With more predictability we anticipate that these spending numbers will grow as restaurateurs have the ability to plan new construction and improvement projects farther out than one or two years.

We urge the members of this committee to consider this information as evidence of the need to keep the restaurant industry strong in order to help keep the nation's overall economy strong.

Over the years, the House Small Business Committee has been a staunch advocate for tax relief for the country's small businesses, including restaurants. We encourage the committee to continue to support such efforts, we ask the members that haven't already done so, to lend their names to H.R. 3622 and ask that any reforms to the tax code be done with the goal of leveling the playing fields for businesses, not further exploiting them or playing favorites.

If this is done, it will free up valuable resources to allow restaurants to do their part to reinvigorate this nation's economy.

Thank you.

Enclosures

Freshly prepared foods boost bottom lines for convenience stores

BY LISA JENNINGS

Long gone are the days when dinner from a convenience store meant little more than a microwaved frozen burrito and a soda.

Across the country, C-store chains are adding more in the way of freshly prepared foods — in ways that are competing directly with quick-service restaurants.

For most C-stores, customers come for gas, cigarettes or other retail items. The smell of a freshly baked pizza or the convenience of a carryout chicken dinner is likely to cause customers to add to their purchases, retailers reason. And because such fresh foods typically are higher-margin items, C-stores are seeing a significant boost to their bottom lines.

Segment leader 7-Eleven, a global chain with 32,312 units, for example, has been adding fresh-food offerings for several years. About 4,700 units in larger U.S. markets offer sandwiches, salads, fresh fruits and baked goods that are delivered daily from commissary kitchens. Earlier this year, the Dallas-based company installed new high-speed ovens in 111 Utah stores to test a new hot-foods menu that will add freshly baked pizzas, chicken wings, churros and cinnamon rolls to the lineup.

Ankeny, Iowa-based Casey's General Store, which is operator or franchisor of more than 1,430 namesake units in nine Midwestern states, is also building foodservice operations with higher gross-profit margins in mind.

What began with from-scratch pizzas in 1984 has grown to a menu of sandwiches, pork and chicken fritters, chicken tenders, hamburgers and hot dogs, doughnuts, biscuits, pastries, and more.

According to the company's annual report, non-gas items accounted for 30 percent of sales but resulted in 75 percent of gross profits from retail sales. Gross profit margins from prepared foods averaged about 62 percent over the past three years, compared with margins from gas sales averaging 5 percent.

Casey's net sales for prepared foods and fountain items totaled in excess of $260 million for the fiscal year ended April 30.

JOE RAEDLE/GETTY

7-Eleven recently installed high-speed ovens in 111 Utah stores to test a new hot-foods menu.

"The additional fountain choices contributed to this category's excellent performance in fiscal 2007, but the real star was our proprietary prepared food program," said Robert Myers, president and chief executive of Casey's. "We kept the warmers full of the right product at the right time of day and were rewarded with another year of impressive gross-profit improvement."

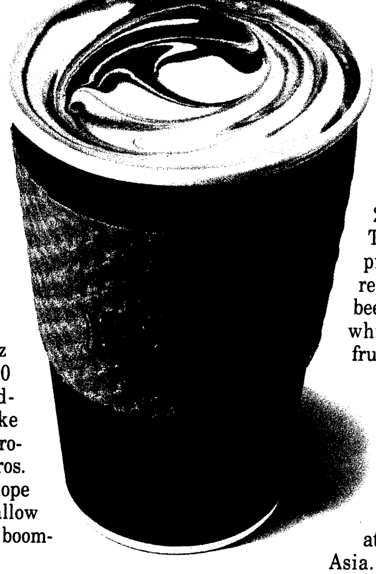
Altoona, Pa.-based Sheetz Corp., with approximately 330 stores throughout the Mid-Atlantic region, recently broke ground on a new $36 million production facility called Sheetz Bros. Kitchen that company officials hope will improve efficiencies and allow the chain to build on its already booming foodservice program.

Sheetz offers a full line of in-store prepared foods, from deli sandwiches and burgers to salads and wraps.

The new commissary will enable the company to add new premade foodservice items, said president Stan Sheetz. However, company officials had not yet determined what might be added to the menu.

The second-largest C-store operator in North America — Alimentation Couche-Tard Inc., based in Laval, Quebec — owns the Circle K brand, with more than 2,000 U.S. locations, as well as the Mac's and Couche-Tard stores in Canada, for a total of nearly 5,000 outlets.

About 300 stores under the three brand names include quick-service restaurants operated by brand partners such as Subway, Dunkin' Donuts, Blimpie, Noble Roman's and Quiznos Sub, according to the company's 2006 annual report. Alimentation Couche-Tard is also testing the development of proprietary foodservice offerings based on regional preferences. Breakfast items have been well-received in Canada, for example, while West Coast customers prefer fresh fruits, sushi and Chinese food.



Altoona, Pa.-based Sheetz offers a full line of beverages and prepared foods, including coffee, deli sandwiches and salads.

Among the fast-growing rivals to the Second 100 convenience players is Famima!!, a Japan-based brand with 12 stores in Los Angeles. Famima Corp., the U.S. subsidiary based in Torrance, Calif., is owned by Tokyo-based FamilyMart Group, which operates more than 13,000 convenience stores in Asia. The group plans to have 20 stores in Southern California before the end of 2007 and to begin opening units in New York by 2009.

In Los Angeles, the Famima concept is so foodservice-focused that the stores may be more accurately described as quick-service restaurants where guests can also buy shampoo and a gallon of milk.

Famima commissaries deliver freshly prepared dishes ranging from roasted-garlic tomato soup and sushi to pad thai noodles and chicken-artichoke paninis that can be grilled in the stores. Instead of the C-store staple of hot dogs, Famima offers hot steamed Chinese buns at the checkout counter, as well as exotic pastries and specialty coffees.

Freshly prepared foods at Famima stores account for about 40 percent of sales, said Shiro Inoue, Famima Corp.'s president and chief executive. He predicts the chain will see $50 million in revenue in fiscal 2007, if all the planned stores open on schedule. ■

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CONVENIENCE STORE CHAINS RANKED BY U.S. SYSTEMWIDE SALES

LATEST-YEAR RANK	PREC.-YEAR RANK	CHAIN	FISCAL YEAR END	U.S. SYSTEMWIDE FOODSERVICE SALES* (BY FISCAL YEAR, IN MILLIONS) LATEST	PRECEDING	PRIOR
1	1	Sheetz	Sept. '06	$290.0	$268.0	$249.7
2	3	Casey's General Stores	April '07	262.0	232.0	208.0
3	2	Circle K	June '07	249.0	239.0	232.7
		TOTALS:		$801.0	$739.0	$690.4

*Actual results, estimates or projections. Source: NRN Research

CONVENIENCE STORE CHAINS RANKED BY GROWTH IN U.S. SYSTEMWIDE SALES (Year-to-year percentage change)

LATEST-YEAR RANK	PREC.-YEAR RANK	CHAIN	FISCAL YEAR END	LATEST* VS. PRECEDING	PRECEDING* VS. PRIOR
1	1	Casey's General Stores	April '07	12.93	11.54
2	2	Sheetz	Sept. '06	8.21	7.33
3	3	Circle K	June '07	4.18	2.71
		AVERAGE:		8.44	7.19

*Actual results, estimates or projections. Source: NRN Research

CONVENIENCE STORE CHAINS RANKED BY NUMBER OF U.S. UNITS

LATEST-YEAR RANK	PREC.-YEAR RANK	CHAIN	FISCAL YEAR END	YEAR-END NUMBER OF UNITS* LATEST	PRECEDING	PRIOR
1	1	Circle K	June '07	2,250	2,149	2,105
2	2	Casey's General Stores	April '07	1,431	1,413	1,358
3	3	Sheetz	Sept. '06	328	317	302
		TOTALS:		4,009	3,879	3,765

*Actual results, estimates or projections. Source: NRN Research

CONVENIENCE STORE CHAINS RANKED BY GROWTH IN NUMBER OF U.S. UNITS (Year-to-year percentage change)

LATEST-YEAR RANK	PREC.-YEAR RANK	CHAIN	FISCAL YEAR END	LATEST* VS. PRECEDING	PRECEDING* VS. PRIOR
1	3	Circle K	June '07	4.70	2.09
2	1	Sheetz	Sept. '06	3.47	4.97
3	2	Casey's General Stores	April '07	1.27	4.05
		AVERAGE:		3.15	3.70

*Actual results, estimates or projections. Source: NRN Research

NATIONAL RESTAURANT ASSOCIATION®

REPRESENTING THE RESTAURANT INDUSTRY

The Cornerstone of the Economy, Career Opportunities and Community Involvement

October 18, 2007

The Honorable xxxx
U.S. House of Representatives
XXX House Office Building
Washington, DC 20515

Dear Representative XXX:

On behalf of the nation's 935,000 restaurant locations nationwide and our 53 state restaurant association partners, **I urge you to cosponsor H.R. 3622, the accelerated restaurant depreciation bill.**

Recently introduced by Congressmen Kendrick Meek (D-FL-17th) and Patrick Tiberi (R-OH- 12th), the legislation would allow accelerated depreciation schedules for newly constructed restaurant properties as well as improvements made to restaurant properties. The legislation would allow the cost of the construction and/or improvements to be written off over a 15-year period rather than the current 39 ½ year schedule. As most agree, the 39 ½ year schedule is outdated and does not reflect the true "life" of a restaurant building which experiences a daily assault by customers and employees lasting up to 18-24 hours a day, unlike most other retail buildings.

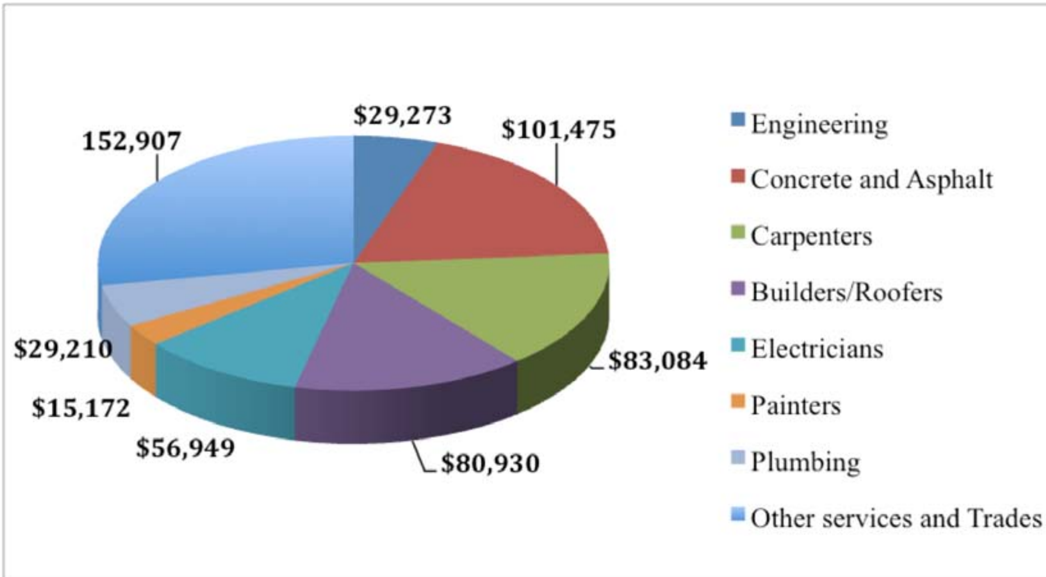
From quick service to fine dining, every sector of the industry supports an accelerated depreciation schedule. Some of our toughest competition in the marketplace enjoy seven or fifteen year schedules themselves, and we continue to be at a competitive disadvantage. In addition, there is inconsistency within the restaurant industry where those who lease their properties can use an accelerated 15-year schedule for improvements.

I ask you to bring fairness, consistency and uniformity to the tax code by cosponsoring H.R. 3622 and allowing restaurateurs to write off new construction and improvements to their buildings over a 15 year schedule. If you need additional information, please contact Michelle Reinke, Director, Legislative Affairs at mreinke@dineout.org or 202-331-5900.

Sincerely,

John Gay
Senior Vice President
Government Affairs and Public Policy

Pizza Hut Restaurant Franchisee
Construction Cost Estimate



Total Capital Expenditure = $549,000

This is an example of just some of the costs associated with constructing a new Pizza Hut restaurant. It is based on an actual restaurant built in the Midwest in 2005. Costs can be significantly higher in some locations.

*The vast majority of this expense represents **<u>direct local economic stimulus</u>**.*