

## Magic Brands (d/b/a Fuddruckers & Koo Koo Roo) Seeks Approval of a Key Employee Incentive Plan

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Magic Brands, LLC and its affiliates (which own, operate and franchise the Fuddruckers and Koo Koo Roo "fast casual dining establishment" chains) sought bankruptcy court approval late last week of their decision to implement a Key Employee Incentive Plan (or "KEIP"). The companies voluntarily filed for chapter 11 protection on April 21, 2010 in Delaware with the intent of continuing a process of closing unprofitable company-owned restaurant locations and positioning the companies for a sale of substantially all of their assets.

The proposed plan would provide bonuses to two tiers of "key employees" of the companies which would be payable upon either (1) the closing of a "sale, transfer or other disposition of substantially all of the assets of Magic and/or Fuddruckers, or more than 50% of the equity interests in Magic or Fuddruckers, in one or a series of transactions" or (2) entry by the bankruptcy court of "a final order confirming a chapter 11 plan of reorganization, as an alternative to the Sale Event . . . (other than a liquidating plan confirmed after the occurrence of a Sale Event)." The employees who would be eligible to participate in the proposed KEIP and the proposed bonus structure are:

- **Tier One.** The tier one employees are the companies' CEO, CFO, COO and Vice President of Marketing. The amount of the potential transaction bonus for each tier one employee is determined as a percentage of his or her base

salary and the percentage is based upon the "Transaction Value" (defined below). The percentage ranges from 25% of base salary (if the Transaction Value is less than \$34 million) to 125% (if the Transaction Value is more than \$49 million).

- **Tier Two.** The tier two employees are the companies' Controller, Vice President of Human Resources, two Senior Vice Presidents of Operations, Senior Vice President of Franchise Sales, Vice President of Franchise Sales, and Legal Affairs Manager. Tier two employees would receive a transaction bonus equal to 25% of base salary if the Transaction Value is less than \$34 million or 33% of base salary if the Transaction Value is greater than \$34 million.

Transaction Value is defined in the KEIP as:

- **Sale Transaction:** "the sum of the gross cash proceeds, plus the fair value (as determined by FocalPoint Securities LLC based on information provided by the Company) of any excluded assets, plus the amount of assumed liabilities."
- **Reorganization Event:** "the sum of the enterprise value of the reorganized Company and Fuddruckers, Inc. . . . as determined by FocalPoint Securities LLC using the higher of the market approach or income approach and based on

information provided by the Company, which valuation shall be disclosed in a disclosure statement approved by the Bankruptcy Court, plus the amount of normalized working capital liabilities that will be paid by the reorganized Company and Fuddrucker, Inc. in the ordinary course of business after the effective date of the plan."



If either a sale or reorganization event occur, the total bonus payments would range from \$504,375 (with \$270,000 going to tier one employees and \$234,375 going to tier two employees) to \$1,659,375 (with \$1.35 million going to tier one employees and \$309,375 going to tier two employees). The greater variability in the payments to tier one employees is explained in the motion as being premised on the belief that tier one employees' efforts are more directly tied to Transaction Value because they are "making, and will continue to make, the strategic business decisions and operations changes necessary to maximize Transaction Value." Nonetheless, the debtors argue that tier two employees should also be eligible for bonuses under the KEIP because the "consummation of a Sale Event or a Reorganization Event would not be possible without [their] diligent efforts."

The debtors assert in the motion that implementation of the KEIP is appropriate and necessary to "properly compensate and motivate the Key Employees to reach a transaction in these Chapter 11 Cases and to maximize the value of the Debtors' business by completing the restructuring to increase forecasted earnings that should attract more competitive bidding." The motion also explains that the \$34 million Transaction Value threshold for increased bonus payments was set because that is the amount at which "proceeds were estimated to result in nominal recoveries for unsecured creditors before consideration of the settlement agreement with Spirit."

Participants in the KEIP would only be eligible to receive their bonus payments if they remain employed in good standing (or were terminated without cause) at the time that the sale or reorganization event occurs.

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