Forefront

ISSUE 3 | 2017

Inside:

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This edition of Forefront highlights issues in the agriculture industry. Commodity prices have continued to tumble and the long term commitments to land leases and equipment when times were better has introduced an unanticipated distress in the industry. Horticulture growers which have also kept us busy over the last five years continue to have challenges with the economics of their distribution to big box sales channels. The ability to understand your business risk and to be able to price it into your customer relationship will give you sustainable advantages rather than following the herd (sometimes off the cliff). We have developed strategies and insights that have enlightened even our most sophisticated clients in these spaces. Automobile units are slowing but will get a bump from the need to replace damaged and irreparable vehicles from the summer hurricanes. Just when you think a market is slowing, it gets an unexpected boost. The interest rates are rising (Fed expects another rate hike in December) but it hasn't slowed M&A activity because of the cash still sitting on the sidelines from the deleveraging of the last six years. Anyway, it's a dynamic market and everybody seems to be busy.

Michigan's Agribusiness

By Carolyn Riegler

"Agribusiness is Michigan's second largest industry, and second in diversity only to California."

Most Michiganders can name the top industry impacting our economy and our everyday lives. Automobile manufacturing has been, and will likely continue to be, the number one economic driver for Michigan.

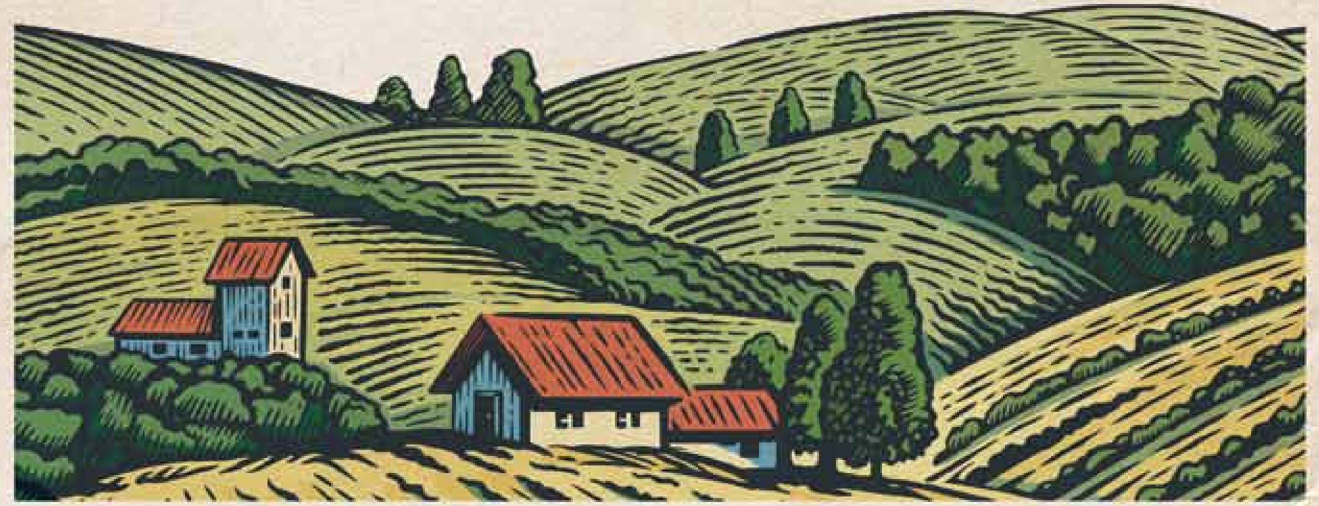
What you may find surprising is the second largest industry in Michigan is Agribusiness. The food and agriculture sector contributes over $101.2 billion annually to the state economy. According to an article in the publication "Michigan Agriculture," the sector creates about 22% of the state's employment. The Michigan Economic Development Corporation indicates that "Agribusiness is Michigan's second largest industry, and second in diversity only to California." In fact, over 300 different kinds of commodities are produced in the state on over 9.9 million acres of farm land, 98% of which are family owned.

Michigan's principal products include milk, floriculture, corn, soybeans, fruits and vegetables, cattle, hogs, poultry and sugar beets. Michigan ranks first in the nation for production of blueberries, tart cherries, begonias and petunias. Additionally, the state is ranked number one nationally in milk production, generating 10.2 billion pounds of milk valued at over $1.7 billion.

Michigan farms have been serving the nation for over 100 years with solid traditions and passing of skills to each passing generation. Despite the rich traditional foundations, todays farmers continue to innovate with new technologies, as well as welcome new participants into the fold.

The Agribusiness Industry is similar to the Automobile Industry as it relates to cyclicality and uncertainty. Natural disasters, economic and political disruption both at home and overseas will dramatically impact food commodity pricing. An additional business risk is the impact of the weather on local farmers. This unpredictable force can wipe out a whole crop or create a bumper crop filled with promise. These economic uncertainties must be managed in Agribusiness in a similar fashion to the Auto Industry. Planning, adjusting, re-engineering production/harvest methods, cost management, evaluation of capital investment opportunities are all factors at play in Agribusiness, not unlike any other business.

Carolyn Riegler
CPA, CFE, CTP, Managing Director, specializes in litigation support, dispute resolution, forensic accounting, real estate, and business valuations.



Craftweiser

TRENDS IN THE CRAFT BEER INDUSTRY

> "FOR THE PAST 10 YEARS, ON AVERAGE, 5 BREWERIES OPENED IN THE U.S. EVERY WEEK. ACCORDING TO BREWERS ASSOCIATION, THIS EXPANSION IN CRAFT BREWING HAS DRIVEN CRAFT BEER'S VOLUME SHARE WITHIN THE BEER INDUSTRY FROM 5.0% TO 12.3% FROM 2010 TO 2016."

By Matthew Rizzo & Anson Smuts

These days craft beer seems to surround us at every restaurant, pub, tap room, and beer hall – a trend that has taken off over the past decade. Growth in the industry is largely due to popularity among younger generations. Gen Xers and Millennials account for 24% and 57% of craft beer drinkers, respectively.

Over the past 10 years, commercial craft brewers of all sizes have steadily emerged to meet demand. Since 2007, the number of large (non-craft) breweries, producing over 6 million barrels, has remained relatively constant, decreasing from 17 to 14 by 2016. Microbreweries and brewpubs, producing between 1 and 15,000 barrels, added a surprising 2,435 more establishments by 2016 while regional craft breweries, producing between 15,000 and 6 million barrels, added 109 breweries. Overall, these numbers mean that for the past 10 years, on average, five breweries opened in the U.S. every week. According to Brewers Association, this expansion in craft brewing has driven craft beer's volume share within the beer industry from 5.0% to 12.3% from 2010 to 2016.

The rate at which craft beer has captured market share has slowed. With an average growth rate of 1.4% from 2011 - 2015, craft beer only captured an additional 0.1% in 2016. According to American Beer Distributors, shifting tastes has meant declining overall beer consumption per capita since 2010. Based on data from Alcohol and Tobacco Tax and Trade Bureau, this trend is reflected in the total barrels of beer produced in the U.S. annually, which decreased by 1 million barrels between 2007 and 2016, bringing the total to 189 million barrels.

With only so many beer-drinkers to go around, breweries of all sizes and styles have cause for concern. While craft brewers hope that beer drinkers continue to move from light beer to craft beer to maintain growth, larger traditional brewers, such as Anheuser-Busch, will rely heavily on craft brewery acquisitions to stay relevant and recapture market share. In the past year there have been 17 acquisitions in the brewing industry, four of which emerged from the investment arms of big name brands. Big name brands acquiring craft breweries will most likely continue to be the perennial dictum.

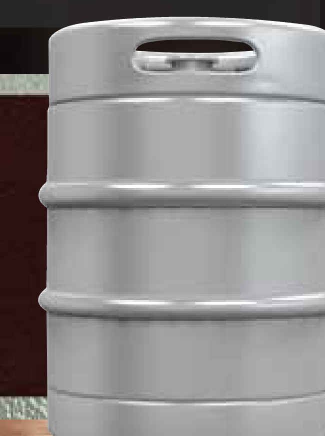
Matthew Rizzo
CPA, CVA, Senior Associate, has business valuation expertise in various types of transactions including, but not limited to mergers and acquisitions, shareholder disputes and gift tax valuations.

Anson Smuts
CMA, CFE, CVA, Senior Associate, utilizes his accounting and finance expertise in mergers and acquisitions, business valuation, intellectual property, and data analysis to identify strategies for business growth and development.

Herz, Julia; "Today's Craft Beer Lovers: Millennials, Women and Hispanics," August 15, 2016
https://www.nbwa.org/resources/2015-beer-year-economics-and-demographics-bringing-different-beers-different-people

NUMBER OF BREWERIES BY PRODUCTION SIZE

	PRODUCTION (BARRELS)	2007:	2016:	% CHANGE:
LARGE BREWERY	OVER 6 MILLION	17	14	-18%
REGIONAL BREWERY	15,000 TO 6 MILLION	117	226	93%
MICRO BREWERY	1 TO 15,000	1306	3741	186%
		1440	3981	176%



Rain On the Scarecrow

By Stephen Weber

In 1985, John Mellencamp released the song "Rain on the Scarecrow" during the height of the agricultural downturn of that era – the strongest downturn since the Great Depression of the 1930s. While it was predicted during those dark days that 40% of farms may shutter their operations, the actual figure of 25% that did is still startling. The question today is: What can today's farmers and farm credit suppliers expect?

Since the high reported in 2012, wheat has fallen from $9 per bushel to $4.50; corn has fallen from $8.50 to $3.75; soybeans have fallen from $18 to $9. Over the same period, we have seen decreasing values for land offset by somewhat-moderating prices for other inputs such as land rent, seed, and chemicals.

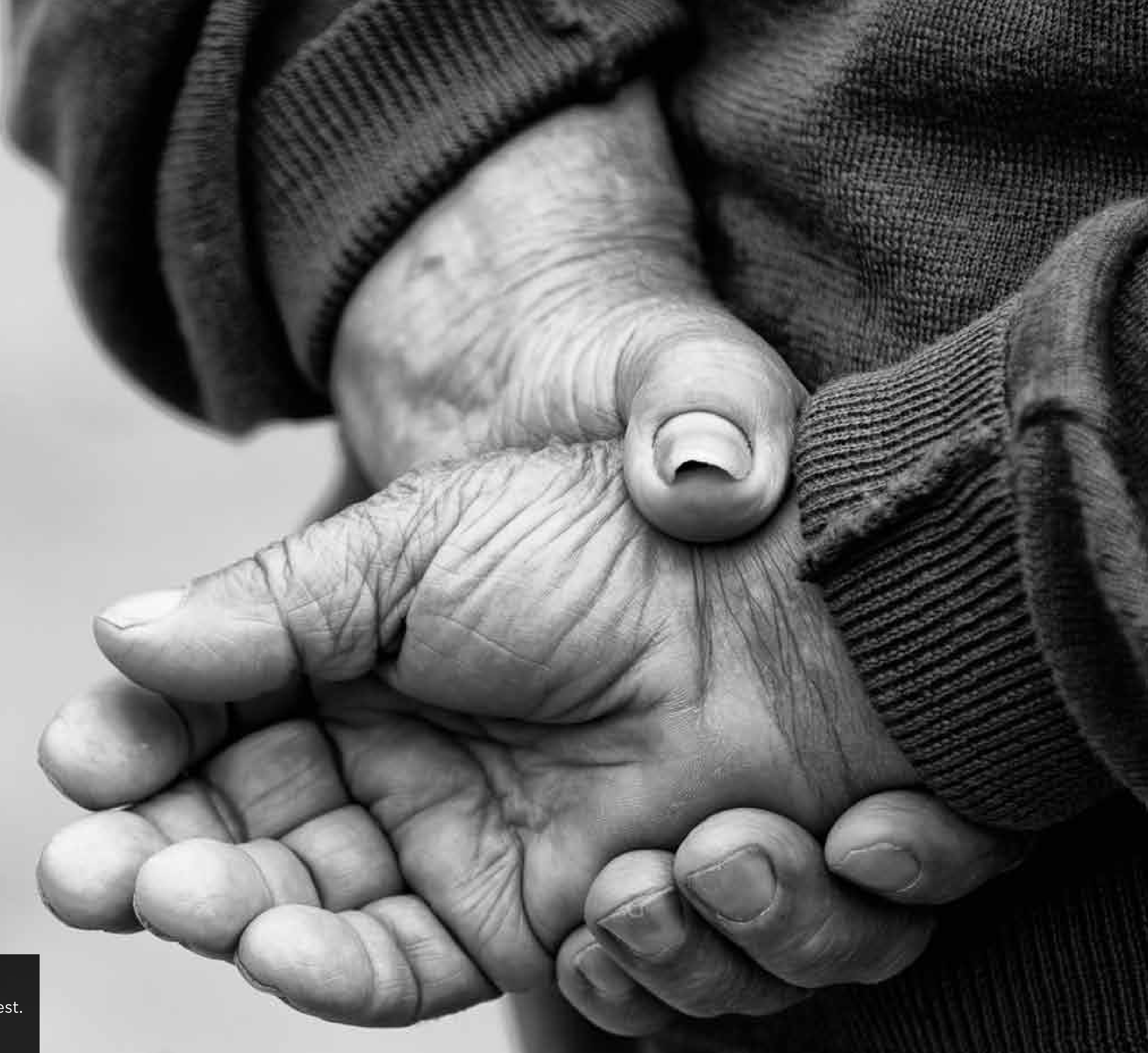
Banks and other finance sources have been able to provide credit for working capital, as opposed to loans for land and equipment. The Wall Street Journal ("WSJ") reported recently that these types of short term credit accounts are up 38% since 2015. However, the WSJ also reported that the volume of new loans for farm operations fell by 7% in the first half of 2017. Banks are increasing their credit requirements and turning away underperforming/undercapitalized operations. Additionally, creditors may be fearful of lending to smaller agricultural operations as Chapter 12 of the U.S. Bankruptcy Code prevents unsecured creditors from forcing a smaller farm into bankruptcy.

Farmers who were able to hold funds and build equity during the "boom" years of 2009-2012 are weathering this downturn. Farmers who over-expanded by increasing their size and spending for new equipment and capital improvements are struggling. Until grain prices return to their higher levels, they will continue to suffer. Sadly, the USDA and Food & Agricultural Policy Research Institute report only slightly higher prices are expected for corn and soybeans through 2022.

For the farmers (and their lenders), the boom and bust cycle of agriculture is expected. Fortunately, for farmers, input prices are not rising quickly and interest rates remain low.

FUTURE FARMERS MUST CONSIDER:

1. Making use of all subsidies available from the U.S. Government to offset poor harvest.
2. Making use of government programs to take acres from production.
3 Forecasting optimal crop mix to maximize profits.
4. Making use of cheaper equipment options such as leasing instead of buying costly large pieces of equipment to improve cash flow.
5. Forecasting operational inputs (seed varieties, fertilizer and other chemical usage) to optimize cost and cash flow.



Stephen Weber
CPA/CFF, CTA, Director, works with many different types of clients in the fields of turnaround management and business refinancing, litigation support, forensic accounting and fraud investigation, as well as performance improvement plans.

Organic Food

By Susan Koss

The organic food industry has exploded in the last decade as consumers gravitate towards natural, whole food diets. Despite the, on average, 46% higher price, shoppers are scrutinizing labels more closely and looking for organic products. So what does “organic” really mean? According to the U.S. Department of Agriculture (“USDA”), USDA certified organic foods are grown and processed according to federal guidelines addressing, among many factors, soil quality, animal raising practices, pest and weed control, and use of additives. Organic producers rely on natural substances and physical, mechanical or biologically based farming methods to the fullest extent possible. Produce can be called organic if it’s certified to have grown on soil that had no prohibited substances applied for three years prior to harvest. Prohibited substances include most, not all, synthetic fertilizers and pesticides.

The transition to organic demand has sparked dramatic growth of 137% over the last 10 years. Organic food currently accounts for about 5.3% of all food sales in the United States. As the industry continues to grow, there have been some major sales transactions in the market. The biggest one is the recent purchase of Whole Foods by Amazon. Whole Foods was purchased by the online giant for $13.7 billion in June. Whole Foods, known for its ability to effectively partner with its network of small and local farmers and producers, is now owned by an entity known for its large centralized approach to logistics. If Amazon chooses to centralize Whole Foods operations, this could have a negative impact on its current suppliers. Amazon also recently announced it would be cutting Whole Foods’ prices on certain produce and protein products in order to make products more affordable for all consumers. Consequently, Amazon could seek to lower the costs of Whole Foods’ products by demanding concessions from small farmers and producers already dealing with low margins.

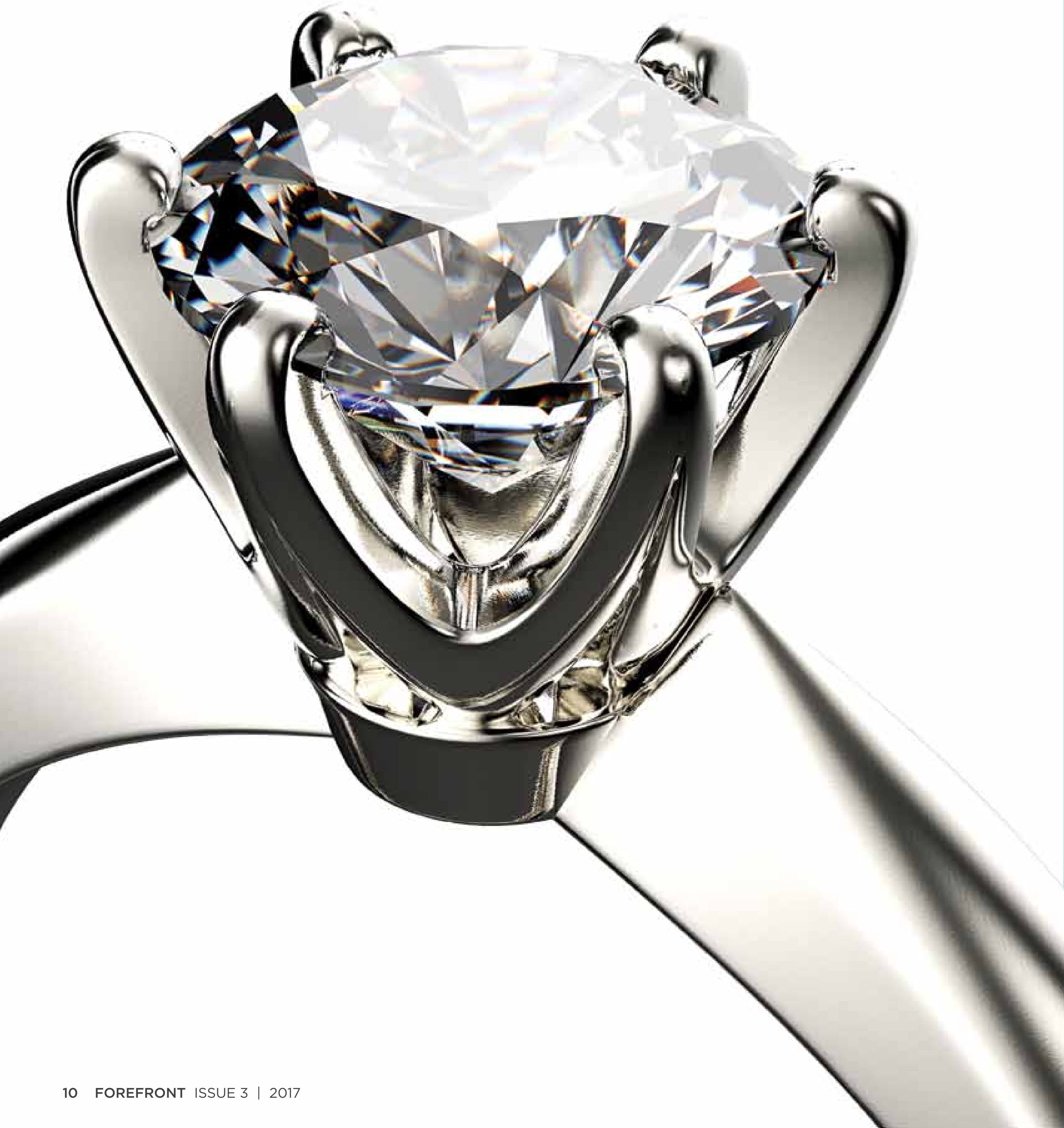
According to the USDA, the lower margins in organic farming are due to higher production costs and lower yields. Lower yields mean less product is harvested per acre via organic farming compared to conventional farming. Production practices used on organic and conventional field crop operations are quite different. For example, most conventional producers of corn and soybeans use genetically modified seed varieties not allowed for certified organic crop production. Most organic producers use mechanical practices, such as tillage and cultivating for weed control, while conventional producers rarely use a cultivator and rely mainly on chemical weed control. Organic corn and soybean producers more often rotate row crops with small grain and meadow crops and include an idle year in the rotation. Conventional producers of these crops mainly use a rotation consisting of continuous row crops.

Organic farms also have the risk of GMO contamination. For all of these reasons, the inputs for organic farming are generally more costly than conventional farming and the margins are lower.

It is possible that price pressure from Amazon could force out small organic farms. Or it’s possible that Amazon will create a platform for affordable organic products for consumers without disrupting its supply chain. The markets are already starting to show bearish signals for Amazon/Whole Foods competitors; with the S&P 500 Packaged Food & Meats index down over 9% since the merger was announced. One thing is for sure, the organic food industry and all of its players will be carefully monitoring Amazon’s every move.

Susan Koss
CPA/ABV/CFF, CVA, Partner and Managing Director, leads the firm’s Litigation Support Practice Group. She specializes in litigation support, business valuation, quality of earnings and forensic accounting.

On August 14, 2017, Judge Swain ordered Costco to pay Tiffany more than $19 million in economic damages for selling generic diamond engagement rings that were marketed using Tiffany's name.



IS IT A TIFFANY RING?

By Andrew Malec, Ph.D.

In a past article, I wrote that a trademark is one of the most valuable types of intellectual property that a company owns because it identifies the brand owner and typically consists of a name, logo, design, or symbol. Companies need to understand the value of their trademark, as well as protect one of their most valuable assets – their brand. Tiffany & Co., the iconic jewelry store in New York, agrees.

In 2013, Tiffany and Co. ("Tiffany") sued Costco Wholesale Corporation ("Costco") in Federal Court for trademark infringement when it learned that salespersons at Costco were responding to customer inquiries by calling certain diamond rings "Tiffany" rings. Although the case involved approximately 2,500 rings, Tiffany sued to protect its brand.

The rings in question had a pronged setting that Costco said is commonly known as a "Tiffany Setting". Costco alleged that "Tiffany" is a generic term for a general setting type or style of engagement ring and asserted that Tiffany does not own any trademark rights to exclude Costco from using the word "Tiffany" to indicate that a ring has that type of setting. Costco contends that the rings were not marked with the Tiffany name and were not sold using Tiffany's trademark blue boxes. However, Judge Swain was not swayed. Judge Swain noted that Costco's salespersons were not disturbed when customers expressed concern that the rings were not actually manufactured by Tiffany. Judge Swain further noted that Costco's upper management in trial testimony, and actions in the years prior to trial, displayed at best a cavalier attitude toward Costco's use of the Tiffany name.

On August 14, 2017, Judge Swain ordered Costco to pay Tiffany more than $19 million in economic damages ($11.1 million in compensatory damages for trademark infringement, and $8.25 million in punitive damages) for selling generic diamond engagement rings that were marketed using Tiffany's name. Back in October 2016, a New York jury awarded Tiffany $5.5 million in compensatory damages and $8.25 million in punitive damages. Judge Swain found that although the jury awarded Tiffany $5.5 million in compensatory damages, the $3.7 million determined to be lost profit was sufficient. Judge Swain then trebled (i.e., tripled) that amount arriving at $11.1 million in compensatory damages.

This case shows that retaining an economic expert is important. Even though the jury awarded compensatory damages, Judge Swain felt that it did not reflect appropriate economic damages. Instead, Judge Swain relied on the determined lost profits amount. Therefore, it is important to retain an economic damages expert to ascertain appropriate economic damages in a litigious matter should liability be found.

Andrew Malec, Ph.D.
Partner and Managing Director, is the head of the firm's Intellectual Property ("IP") Practice Group. He is a recognized expert in providing economic advisory services, litigation support, and valuation opinions.

O'Keefe in the news

O'Keefe's highly credentialed professionals have advanced business degrees and professional certifications such as: Certified Public Accountant (CPA), Certified Turnaround Professional (CTP), Financial Forensics (CFE, CFF and MAFF), Accredited in Business Valuation (ABV), and others. We are proud to congratulate Carolyn Riegler, Matt Rizzo, Anson Smuts and Griffin Wagner on their recent designations.

Carolyn Riegler has received her designation as a Certified Turnaround Professional (CTP) from the Turnaround Management Association.

Matthew Rizzo earned the designation of Certified Public Accountant (CPA) from the American Institute of Certified Public Accountants (AICPA). Additionally, Mr. Rizzo was named an Emerging Leader by The M&A Advisor as part of their 8th annual "Emerging Leaders" awards. He was chosen for his industry accomplishments and expertise from a pool of nominees by an independent judging panel of distinguished business leaders. Tuesday, September 19th, The M&A Advisor hosted a black tie Awards Gala at the New York Athletic Club in Manhattan to introduce the Emerging Leaders Award Winners to the business community and celebrate their achievements.

Anson Smuts received the designation of Certified Fraud Examiner (CFE) from the Association of Certified Fraud Examiners. Mr. Smuts has also joined the Detroit Chapter of Turnaround Management Association's NextGen Board of Directors as Chair of the membership committee. NextGen was organized for the next generation of turnaround and corporate restructuring professionals with networking and educational opportunities tailored to those in the early stages of their career.

Griffin Wagner earned the designation of Certified Valuation Analyst (CVA) from the National Association of Certified Valuation Analysts (NACVA).

O'Keefe welcomes **Katie Gerdes**, Associate, to the team. Prior to joining O'Keefe, Ms. Gerdes served as assistant controller for a $1 billion tier one auto-supplier. She began her career in public accounting as an auditor servicing privately held middle-market companies in various industries, including manufacturing, construction, financial services, and nonprofits.

Carolyn Riegler and Judy Wallace were promoted to Managing Directors.

Carolyn Riegler has 30 years of professional experience in financial and operational capacities to provide clients with financial consulting services, litigation support services, real estate valuation, business turnaround and operational advisory services.

Prior to joining O'Keefe, Ms. Riegler was a Chief Financial Officer of multiple privately held businesses. Her experience was focused in the real estate industry where she spearheaded growth initiatives and turnaround efforts for a multi-state middle market real estate holding company. In addition, she worked with a global CPA firm for 10 years auditing and advising clients in a multitude of industries. Ms. Riegler's experience includes advising on complex real estate transactions, legal structure analysis, fraud and forensic investigations, and damage claim evaluations.

Judy Wallace brings 30 years of professional experience in financial consulting services, including acting as a Chief Restructuring Officer. She is also well versed in areas including operational cost savings, inventory control, cash flow management and improvement, overall operations and ERP system implementation and upgrade.

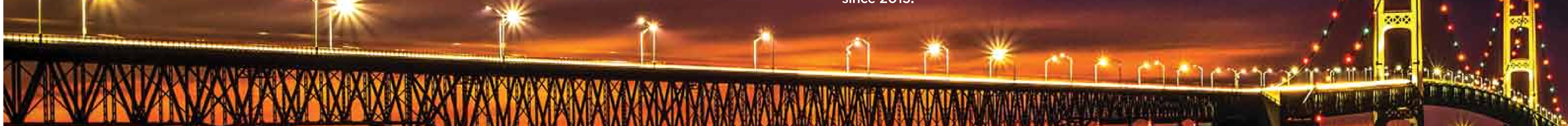
Prior to joining O'Keefe, Ms. Wallace served as the Vice President of Finance and Operations for a privately held business, managing all financial and operational activities. In addition, she worked as a senior manager in public accounting/auditing with a large CPA firm, before moving to private industry. She serves as Treasurer and audit committee member, respectively, for two not-for-profit organizations, supporting the local arts, educational, and low-income communities.

Amanda Rymiszewski received the Alumni Community Service Award presented by The Oakland University Alumni Association. The award recognizes distinctive service of a humanitarian nature and citizenship through community, public or OU service activities.

Friday, October 13th, the Oakland University Alumni Association hosted the Annual Alumni Awards Banquet at Meadow Brook Hall in Rochester during Fall Homecoming and Reunion Weekend. This event brought together hundreds of OU graduates to honor achievements in business, community service, volunteerism and more.

Pat O'Keefe has been named CEO of Grow Michigan, LLC.

O'Keefe has been retained to provide administrative and loan management functions for Grow Michigan. Grow Michigan, LLC extends the capabilities of senior debt providers by offering a highly efficient, cost effective and complimentary capital structure for growing Michigan small businesses in a broad range of industries. Grow Michigan investors include 19 financial institutions doing business in the State and the Michigan Strategic fund. Grow Michigan, to date, has invested $51.1 million in transactions involving a total leveraged capital investment of $353.2 million, involving 2,795 jobs since 2013.



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Did you know:

O'Keefe is a trusted resource for mergers and acquisitions

Mergers and Acquisitions
Buying (or selling) a business is a non-recurring activity for most middle market companies. For this reason, internal resources assigned to the task often lack the experience and time required. This creates risk in successfully executing the strategic and economic outcomes anticipated. O'Keefe is a trusted resource to assist in the planning and execution of transaction strategies. We work collaboratively with our client's legal advisors to ensure the transaction is properly documented and to avoid unnecessary risk.

Buy-Side Representation:
- Research and identification of appropriate strategic targets
- Modeling projected financial expectations to all stakeholders
- Due diligence to validate assumptions
- Assist in securing loans and/or raising equity to make acquisitions

Sell-Side Representation:
- Identification and solicitation of strategic and financial buyers
- Preparation of marketing materials
- Pre-sale due diligence to identify potential pitfalls that would delay or derail the sale or result in unexpected purchase price reduction
- Preparation of business valuations to support the transaction price

MICHIGAN LAWYERS WEEKLY
Reader Rankings 2017
BEST LITIGATION CONSULTING SERVICES
TOP RANKED

O'Keefe Named "Best Litigation Consulting Services"
in the First Annual Michigan Lawyers Weekly Reader Rankings. The poll, based on readers' votes, ranked a variety of businesses that serve the legal community in several categories, including advertising, financial institutions, trial services, technology and hospitality.

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