ONE Group Hospitality, Inc.
Form 10-Q
November 16, 2015

UNITED STATES
SECURITIES AND EXCHANGE COMMISSION
Washington, D. C. 20549

FORM 10-Q

	(Mark One)
ý	QUARTERLY REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934

For the quarterly period ended September 30, 2015

OR

¨	TRANSITION REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934
	For the transition period from to

Commission File Number 000-52651

THE ONE GROUP HOSPITALITY, INC.
(Exact name of registrant as specified in its charter)

Delaware	14-1961545
(State or other jurisdiction of incorporation or organization)	(I.R.S. Employer Identification No.)
411 W. 14th Street, 2nd Floor, New York, New York	10014
(Address of principal executive offices)	Zip Code

646-624-2400
(Registrant’s telephone number, including area code)

Indicate by check mark whether registrant (1) has filed all reports required to be filed by Section 13 or 15(d) of the Securities Exchange Act of 1934 during the preceding 12 months (or such shorter period that the registrant was required to file such reports) and (2) has been subject to such filing requirements for the past 90 days. Yes ý No ¨

Indicate by check mark whether the registrant has submitted electronically and posted on its corporate Web site, if any, every Interactive Data File required to be submitted and posted pursuant to Rule 405 of Regulation S-T (§232.405 of this chapter) during the preceding 12 months (or for such shorter period that the registrant was required to submit and post such files). Yes ý No ¨

Indicate by check mark whether the registrant is a large accelerated filer, an accelerated filer, a non-accelerated filer, or a smaller reporting company. See the definitions of “large accelerated filer,” “accelerated filer” and “smaller reporting company" in Rule 12b-2 of the Exchange Act. (Check one):

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Large accelerated filer ¨	Accelerated filer ¨	Non-accelerated filer ¨ (do not check if a smaller reporting company)	Smaller reporting company x

Indicate by check mark whether the registrant is a shell company (as defined in Rule 12b-2 of the Exchange Act). Yes ¨ No ý

Number of shares of Common Stock outstanding as of November 16, 2015: 24,972,515.

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PART I
FINANCIAL INFORMATION

Item 1. Financial Statements
THE ONE GROUP HOSPITALITY, INC.

CONSOLIDATED BALANCE SHEETS

	September 30, 2015 (unaudited)	December 31, 2014
Assets		
Current assets:		
Cash and cash equivalents	$1,795,847	$7,905,004
Accounts receivable, net	4,285,218	4,408,396
Inventory	1,066,565	1,139,305
Other current assets	2,616,828	1,937,392
Due from related parties	1,369,795	1,157,134
Total current assets	11,134,253	16,547,231
Property and equipment, net	26,199,351	18,815,625
Investments	2,991,607	2,802,443
Deferred tax assets	8,424,563	35,418
Other assets	789,219	793,002
Security deposits	2,357,978	2,368,422
Total assets	$51,896,971	$41,362,141
Liabilities and Stockholders' Equity		
Current liabilities:		
Cash overdraft	$608,769	$85,598
Current portion of long term debt	1,929,167	1,495,000
Accounts payable	3,046,999	3,433,198
Accrued expenses	4,979,840	2,004,704
Due to related parties	—	19,608
Deferred revenue	188,079	127,950
Total current liabilities	10,752,854	7,166,058
Other long-term liabilities	—	67,277
Derivative liability	2,324,000	6,241,000
Long term debt, net of current portion	9,079,020	5,980,000
Deferred rent payable	11,887,118	9,435,109
Total liabilities	34,042,992	28,889,444
Stockholders' equity:		
Common stock, $0.0001 par value, 75,000,000 shares authorized; 24,972,515 and 24,940,195 shares issued and outstanding at September 30, 2015 (unaudited) and December 31, 2014, respectively	2,497	2,494
Preferred stock, $0.0001 par value, 10,000,000 shares authorized; 0 shares issued and outstanding at September 30, 2015 (unaudited) and December 31, 2014, respectively	—	—

Additional paid-in capital	31,633,461	30,966,611
Accumulated deficit	(12,721,823)	(18,005,401)
Accumulated other comprehensive loss	(492,439)	(230,696)
Total stockholders' equity	18,421,696	12,733,008
Noncontrolling interest	(567,717)	(260,311)
Total stockholders' equity including noncontrolling interest	17,853,979	12,472,697
Total Liabilities and Stockholders' Equity	$51,896,971	$41,362,141

See notes to the consolidated financial statements.

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THE ONE GROUP HOSPITALITY, INC.

CONSOLIDATED STATEMENTS OF OPERATIONS AND COMPREHENSIVE INCOME (LOSS)
(unaudited)

	Three months ended September 30, 2015	Three months ended September 30, 2014	Nine months ended September 30, 2015	Nine months ended September 30, 2014
Revenues:				
Owned unit net revenues	$13,314,507	$10,444,821	$35,818,733	$28,722,921
Management and incentive fee revenue	1,939,376	1,945,363	6,112,629	6,207,523
Total revenue	15,253,883	12,390,184	41,931,362	34,930,444
Cost and expenses:				
Owned operating expenses:				
Food and beverage costs	3,346,841	2,811,806	9,082,231	7,482,382
Unit operating expenses	8,807,632	6,245,617	23,898,483	17,661,544
General and administrative	2,610,599	1,922,482	7,647,589	6,024,364
Depreciation and amortization	630,249	327,810	1,620,009	1,000,464
Management and royalty fees	310	(35,214)	46,959	60,324
Pre-opening expenses	1,634,171	315,905	4,399,192	1,149,078
Transaction costs	405,797	—	506,131	—
Equity in (income) of investee companies	(205,273)	(268,660)	(728,504)	(588,996)
Derivative (income) expense	(1,139,000)	991,588	(3,917,000)	(1,793,124)
Interest expense, net of interest income	1,210	(6,268)	(3,980)	52,220
Other (income) expense	127,692	(1,227,698)	(476,932)	(1,157,067)
Total costs and expenses	16,220,228	11,077,368	42,074,178	29,891,189
(Loss) income from continuing operations before provision for income taxes	(966,345)	1,312,816	(142,816)	5,039,255
Provision (benefit) for income taxes	922,427	462,898	(5,619,504)	813,580
(Loss) income from continuing operations	(1,888,772)	849,918	5,476,688	4,225,675
Loss (income) from discontinued operations, net of taxes	(62,501)	(177,050)	(23,929)	1,094,376
Net (loss) income	(1,826,271)	1,026,968	5,500,617	3,131,299
Less: net income attributable to noncontrolling interest	189,698	279,542	217,039	92,478
Net (loss) income attributable to The ONE Group Hospitality, Inc.	$(2,015,969)	$747,426	$5,283,578	$3,038,821
Amounts attributable to The ONE Group Hospitality, Inc.:				
(Loss) income from continuing operations	$(2,078,470)	$570,376	$5,259,649	$4,133,197
Loss (income) from discontinued operations, net of taxes	(62,501)	(177,050)	(23,929)	1,094,376
Net (loss) attributable to The ONE Group Hospitality, Inc.	$(2,015,969)	$747,426	$5,283,578	$3,038,821

Net (loss) income attributable to The ONE Group Hospitality, Inc.	$(2,015,969)	$747,426	$5,283,578	$3,038,821
Other comprehensive loss				
Currency translation adjustment	(30,900)	(78,177)	(261,743)	(33,955)
Comprehensive (loss) income	$(2,046,869)	$669,249	$5,021,835	$3,004,866

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Basic and diluted (loss) income per share:				
Continuing operations	$(0.08)	$0.04	$0.21	$0.17
Discontinued operations	$—	$0.01	$—	$0.04
Net (loss) income per share attributable to The ONE Group Hospitality, Inc.	$(0.08)	$0.03	$0.21	$0.13
Shares used in computing basic income per share	24,972,515	24,940,195	24,956,177	24,942,328
Shares used in computing diluted income per share	24,972,515	24,940,195	24,956,177	24,942,328

See notes to the consolidated financial statements.

THE ONE GROUP HOSPITALITY, INC.

CONSOLIDATED STATEMENTS OF CHANGES IN STOCKHOLDERS' EQUITY
(unaudited)

	Common stock							
	Shares	Par value	Additional paid-in capital	Accumulated deficit	Accumulated other comprehensive (loss) income	Total stockholders' (loss) income equity	Noncontrolling interest	Total stockholders' equity including noncontrolling interest
Balance at December 31, 2014	24,940,195	$2,494	$30,966,611	$(18,005,401)	$(230,696)	$12,733,008	$(260,311)	$12,472,697
Stock based compensation expense	32,320	3	666,850			666,853		$666,853
Member distributions						—	(524,445)	$(524,445)
Loss on foreign currency translation, net					(261,743)	(261,743)		$(261,743)
Net income				5,283,578		5,283,578	217,039	$5,500,617
Balance at September 30, 2015	24,972,515	$2,497	$31,633,461	$(12,721,823)	$(492,439)	$18,421,696	$(567,717)	$17,853,979

See notes to the consolidated financial statements.

THE ONE GROUP HOSPITALITY, INC.

CONSOLIDATED STATEMENTS OF CASH FLOWS
(unaudited)

	Nine months ended September 30, 2015	2014
Operating activities:		
Net income	$5,500,617	$3,131,299
Adjustments to reconcile net loss to net cash used in operating activities:		
Depreciation and amortization	1,620,009	1,129,064
Deferred rent payable	2,452,009	289,275
Deferred taxes	(8,389,145)	140,333
Equity in income of investee companies	(728,504)	(588,996)
Derivative income	(3,917,000)	(1,793,124)
Stock-based compensation	666,853	326,753
Changes in operating assets and liabilities:		
Accounts receivable	123,178	(805,422)
Inventory	72,740	33,708
Prepaid expenses and other current assets	(679,436)	263,438
Security deposits	10,444	109,200
Other assets	3,784	(43,109)
Accounts payable	(386,199)	(1,418,169)
Accrued expenses	2,977,787	(1,417,458)
Deferred revenue	(7,148)	83,963
Net cash used in operating activities	(680,011)	(559,245)
Investing activities:		
Purchase of property and equipment	(9,003,733)	(4,562,397)
Purchase of minority interest	—	(75,000)
Distributions from equity investees	539,340	502,753
Due from related parties	(232,269)	(60,487)
Net cash used in investing activities	(8,696,662)	(4,195,131)
Financing activities:		
Cash overdraft	523,171	442,515
Proceeds from term loan	4,215,000	6,897,940
Proceeds from equipment financing agreement	502,548	—
Repayment of term loan	(1,184,361)	(5,087,551)
Repayment of notes payable	—	(15,000)
Distributions to members	(524,445)	(760,605)
Net cash provided by financing activities	3,531,913	1,477,299
Effect of exchange rate changes on cash	(264,397)	(34,115)
Net decrease in cash	(6,109,157)	(3,311,192)
Cash and cash equivalents, beginning of period	7,905,004	11,681,086

Cash and cash equivalents, end of period	$1,795,847	$8,369,894
Supplemental disclosure of cash flow data:		
Interest paid	$246,745	$107,070
Income taxes paid	$80,148	$217,172

See notes to the consolidated financial statements.

THE ONE GROUP HOSPITALITY, INC.

Notes to Consolidated Financial Statements
(unaudited)

Note 1 - Merger:

On October 16, 2013, The ONE Group Hospitality, Inc. (the "Company") closed a merger transaction (the “Merger”) with The ONE Group, LLC, a privately held Delaware limited liability company (“ONE Group”), pursuant to an Agreement and Plan of Merger, dated as of October 16, 2013 (the “Merger Agreement”), by and among The ONE Group Hospitality, Inc., formerly known as Committed Capital Acquisition Corporation, CCAC Acquisition Sub, LLC, a Delaware limited liability company and wholly-owned subsidiary of the Company (“Merger Sub”), ONE Group and Samuel Goldfinger as ONE Group Representative. Pursuant to the Merger Agreement, ONE Group became a wholly-owned subsidiary of the Company through a merger of Merger Sub with and into ONE Group, and the former members of ONE Group received shares of the Company, Inc. that constituted a majority of the outstanding shares of the Company.

The Merger was accounted for as a reverse-merger and recapitalization in accordance with GAAP, whereby the Company was the accounting acquiree and ONE Group was the accounting acquirer. Consequently, the assets and liabilities and the operations that are reflected in the historical financial statements prior to the Merger are those of ONE Group, and the consolidated financial statements after completion of the Merger include the assets and liabilities of the Company and ONE Group, historical operations of ONE Group and operations of the Company from the October 16, 2013 effective date. Membership interests and the corresponding capital amounts of ONE Group pre-Merger have been retroactively restated as shares of common stock reflecting the 8.09 to one exchange ratio in the Merger. All references in this Report to equity securities and all equity-related historical financial measurements, including weighted average shares outstanding, earnings per share, par value of $0.0001 per share of the Company's common stock ("Common Stock"), additional paid in capital, option exercise prices and warrant exercise prices, have been retroactively restated to reflect the Merger exchange ratio.

On June 5, 2014, the Company changed its corporate name from Committed Capital Acquisition Corporation to The ONE Group Hospitality, Inc.

Note 2 - Business and basis of presentation:

Principles of consolidation:
The accompanying consolidated financial statements of The ONE Group Hospitality, Inc. and subsidiaries include the accounts of ONE Group and its subsidiaries, Little West 12th LLC, One-LA, L.P., Bridge Hospitality, LLC, STK-LA, LLC, WSATOG (Miami), LLC, STK Miami Service, LLC (“Miami Services”), STK Miami, LLC (“STK Miami”), Basement Manager, LLC, JEC II, LLC, One TCI Ltd., One Marks, LLC, MPD Space Events LLC, One 29 Park Management, LLC (“One 29 Park Management”), STK Midtown Holdings, LLC, STK Midtown, LLC, STKOUT Midtown, LLC, STK Atlanta, LLC, STK-Las Vegas, LLC (“STK Vegas”), One Atlantic City, LLC, Asellina Marks LLC, Heraea Vegas, LLC (“Heraea”), Xi Shi Las Vegas, LLC (“Xi Shi Las Vegas”), T.O.G. (UK) Limited, Hip Hospitality Limited (“Hip Hospitality UK”), T.O.G. (Aldwych) Limited (“TOG Aldwych”), CA Aldwych Limited, T.O.G. (Milan) S.r.l. ("TOG Milan"), BBCLV, LLC, STK DC, LLC, STK Orlando, LLC, STK Chicago, LLC ("STK Chicago"), TOG Biscayne, LLC, STK Westwood, LLC, STK Denver, LLC, STK Rebel Austin, LLC, STK Dallas, LLC, STK Rebel San Diego, LLC, STK Texas Holdings, LLC, STK Holdings II, LLC, 9401415 Canada Ltd., STK Ibiza, LLC and STK Rebel (Edinburgh) Limited. The entities are collectively referred to herein as the “Company” or “Companies,” as appropriate, and are consolidated on the basis of common ownership and control. All significant

intercompany balances and transactions have been eliminated in consolidation.

Net Income (Loss) Per Common Share
Basic net income (loss) per common share is based upon the weighted-average common shares outstanding during the period. Diluted net income (loss) per common share reflects the potential dilution that would occur if common stock equivalent securities or other contracts to issue common stock were exercised or converted into common stock.

Fair value measurements
The carrying amount of the Company's accounts receivable, accounts payable and accrued expenses approximate fair value because of the short term nature of the financial instruments. The carrying value of the long term debt approximates fair value since the terms of the loan have been recently negotiated.

Nature of business:

The Company is a hospitality company that develops and operates upscale, high-energy restaurants and lounges and provides turn-key food and beverage ("F&B") services for hospitality venues including hotels, casinos and other high-end locations in the United States and England. We opened our first restaurant in January 2004 in New York City and as of November 16, 2015, we owned and operated (under lease agreements) 12 and managed (under management agreements) 15 restaurants and lounges globally, including 10 STKs in major metropolitan cities in the United States and Europe (of which 7 are owned and 3 managed). In addition, we provided food and beverage services in five hotels and casinos, one of which is under a lease agreement and four of which are under separate management agreements. We generate management and incentive fee revenue from those restaurants and lounges that we manage on behalf of our F&B hospitality clients.

Unaudited interim financial information:
The accompanying unaudited consolidated financial statements have been prepared in accordance with U.S. generally accepted accounting principles (“GAAP”) for interim financial information. Accordingly, they do not include all the information and disclosures required by GAAP for complete financial statements. Operating results for the three and nine months ended September 30, 2015 are not necessarily indicative of the results that may be expected for the year ending December 31, 2015 or for any other interim period or other future year. In the opinion of management, the unaudited condensed consolidated financial statements include all adjustments, consisting of normal recurring adjustments, considered necessary for a fair presentation. These unaudited condensed consolidated financial statements and related notes should be read in conjunction with the consolidated financial statements and notes for the fiscal year ended December 31, 2014 included in the Company’s Annual Report filed on Form 10-K/A for the year ended December 31, 2014 filed with the Securities and Exchange Commission (the “SEC”) on April 1, 2015.

Note 3 – Recent accounting pronouncements:
In May 2014, the Financial Accounting Standards Board ("FASB") issued Accounting Standards Update ("ASU") No. 2014-09, “Revenue from Contracts with Customers” (Topic 606). ASU 2014-09 addresses the reporting of revenue by most entities and will replace most existing revenue recognition guidance in U.S. GAAP when it becomes effective. This update is effective in fiscal periods beginning after December 15, 2017. Early application is permitted only as of annual reporting periods beginning after December 15, 2016. The impact on our financial statements of adopting ASU 2014-09 is currently being assessed by management.

In August 2014, the FASB issued ASU No. 2014-15 “Disclosure of Uncertainties About an Entity’s Ability to Continue as a Going Concern,” which provides guidance on determining when and how to disclose going concern uncertainties in the financial statements. The new standard requires management to perform interim and annual assessments of an entity's ability to continue as a going concern. The update is effective for annual periods ending after December 15, 2016, and interim periods thereafter. Early adoption is permitted. The impact on our financial statements of adopting ASU 2014-15 is currently being assessed by management.

In February 2015, the FASB issued ASC 2015-02, "Consolidation (Topic 810) - Amendments to the Consolidation Analysis." This standard modifies existing consolidation guidance for reporting organizations that are required to evaluate whether they should consolidate certain legal entities. ASU 2015-02 is effective for fiscal years beginning after December 15, 2015, and requires either a retrospective or a modified retrospective approach to adoption. Early adoption is permitted. The Company does not expect this standard to have a significant impact on its consolidated financial statements.

In April 2015, the FASB issued ASU 2015-03, “Interest- Imputation of Interest (Subtopic 835-30): Simplifying the Presentation of Debt Issuance Costs.” The update simplifies the presentation of debt issuance costs by requiring that debt issuance costs be presented in the balance sheet as a direct deduction from the carrying amount of debt liability, consistent with debt discounts or premiums. The recognition and measurement guidance for debt issuance costs are not affected by the amendments in this update. For public companies, this update is effective for interim and annual periods beginning after December 15, 2015, and is to be applied retrospectively. Early adoption is permitted. This standard is subsequently updated by ASU 2015-15, "Presentation and Subsequent Measurement of Debt Issuance Costs Associated with Line-of-Credit Arrangements," which codifies an SEC staff announcement relative to debt issuance costs for line-of-credit arrangements. The Company does not expect these updates to have a significant impact on its consolidated financial statements and has not yet concluded whether it will adopt ASU 2015-03 and ASU 2015-15 prior to their effective dates.

In July 2015, the FASB issued ASU 2015-11, "Simplifying the Measurement of Inventory." The update states that inventory should be measured at the lower of cost and “net realizable value.” Net realizable value is defined as the “estimated selling prices in the ordinary course of business, less reasonably predictable costs of completion, disposal and transportation.” ASU 2015-11 eliminates the guidance that entities consider replacement cost or net realizable value less an approximately normal profit margin in the subsequent measurement of inventory when cost is determined on a first-in, first-out or average cost basis.

The amendment is effective for interim and annual periods beginning after December 15, 2016. Early application is permitted and should be applied prospectively. The Company does not expect this standard to have a significant impact on its consolidated financial statements and has not yet concluded whether it will adopt ASU 2015-11 prior to the effective date.

Note 4 - Inventory:

Inventory consisted of the following:

	At September 30, 2015	At December 31, 2014
Food	$187,213	$134,355
Beverages	879,352	1,004,950
Totals	$1,066,565	$1,139,305

Note 5 - Property and equipment, net:

Property and equipment, net consisted of the following:

	At September 30, 2015	At December 31, 2014
Furniture, fixtures and equipment	$8,279,065	$7,336,956
Leasehold improvements	26,149,307	20,719,230
Less accumulated depreciation and amortization	13,814,832	13,833,271
	20,613,540	14,222,915
Construction in progress	4,551,867	3,871,670
Restaurant supplies	1,033,944	721,040
Total	$26,199,351	$18,815,625

Depreciation and amortization related to property and equipment included in continuing operations amounted to $630,249 and $327,810 in the three months ended September 30, 2015 and 2014, respectively, and $1,620,009 and $1,000,464 in the nine months ended September 30, 2015 and 2014, respectively. Additionally, included in discontinued operations for the nine months ended September 30, 2014 was depreciation of $128,600.

Note 6 – Accrued expenses:

Accrued expenses consisted of the following:

	At September 30, 2015	At December 31, 2014
Sales tax payable	$692,145	$168,172
Payroll and related	1,122,294	435,259
Current and deferred income taxes payable	2,628,404	494,152
Due to hotels	200,000	200,000
Other	336,997	707,121
Totals	$4,979,840	$2,004,704

Note 7 - Long term debt:

Long term debt consists of the following:

	September 30, 2015	December 31, 2014
Term Loan Agreements	$10,555,639	$7,475,000
Equipment Financing Agreement	452,548	—
	11,008,187	7,475,000
Less: Current portion of Long Term Debt	1,929,167	1,495,000
Long Term Debt, net of Current Portion	$9,079,020	$5,980,000

Future minimum loan payments:	
2015	$423,750
2016	2,397,500
2017	2,631,666
2018	2,434,215
2019	2,418,556
Thereafter	702,500
Total	$11,008,187

On December 17, 2014, the Company entered into a Term Loan Agreement with BankUnited, N.A. in the amount of $7,475,000 maturing December 1, 2019 (the "Term Loan Agreement"). The Term Loan Agreement replaced the existing credit agreement which was terminated and the aggregate principal amount of the existing loans outstanding of $6,395,071 was converted into the Term Loan Agreement. Commencing on January 1, 2015, the Company made the first of sixty (60) consecutive monthly installments of $124,583 plus interest that will accrue at an annual rate of

5.0%. Our obligations under the Term Loan Agreement are secured by substantially all of our assets. The outstanding balance under the Term Loan Agreement at September 30, 2015 and December 31, 2014 was $6,340,639 and $7,475,000, respectively.

On June 2, 2015, the Company entered into a second term loan agreement (the "Second Term Loan Agreement") with BankUnited, N.A., wherein BankUnited, N.A. agreed to make multiple advances to the Company in the aggregate principal amount of up to $6,000,000. Commencing on April 1, 2016 the Company will pay fifty-four (54) consecutive equal monthly installments, with each such installment to be in the principal amount of $111,111 or such lesser amount as shall be equal to the quotient of (x) the outstanding principal amount of all advances on March 31, 2016, divided by (y) fifty-four (54); provided, however, that the final principal installment shall be in an amount equal to the aggregate principal amount of all advances outstanding on September 1, 2020, or such earlier date on which all outstanding advances shall become due and payable, whether by acceleration or otherwise. This second term loan bears interest at a rate per annum equal to 5.0%. Our obligations under the Second Term Loan Agreement are secured by substantially all of our assets. The outstanding balance under the Second Term Loan Agreement at September 30, 2015 was $4,215,000.

The Term Loan Agreement and the Second Term Loan Agreement contain certain affirmative and negative covenants, including negative covenants that limit or restrict, among other things, liens and encumbrances, indebtedness, mergers, asset sales, investments, assumptions and guaranties of indebtedness of other persons, change in nature of operations, changes in fiscal year and other matters customarily restricted in such agreements. The financial covenants contained in these agreements require the borrowers to maintain a certain adjusted tangible net worth and a debt service coverage ratio.

The Company was in compliance with all of its financial covenants under the Term Loan Agreement and Second Term Loan Agreement as of September 30, 2015 and the Company believes based on current projections that the Company will continue to comply with such covenants through the remainder of 2015.

On June 5, 2015, the Company entered into a $1,000,000 Equipment Finance Agreement (the "Agreement") with Sterling National Bank. The Agreement covers certain equipment in our STKs that are under construction in Orlando and Chicago. At September 30, 2015, a deposit of $452,548 had been made on the equipment with the remainder to be financed once the equipment has been installed. The Agreement calls for sixty (60) monthly payments of $16,667 plus interest commencing July 1, 2015.

Interest expense recognized related to these agreements amounted to $94,677 and $26,823 for the three months ended September 30, 2015 and 2014, respectively, and $246,745 and $134,629 for the nine months ended September 30, 2015 and 2014, respectively. Capitalized interest amounted to $93,464 and $26,481 for the three months ended September 30, 2015 and 2014, respectively, and $250,717 and $58,333 for the nine months ended September 30, 2015 and 2014, respectively.

As of September 30, 2015, the issued letters of credit in the total amount of approximately $1.5 million for our STK locations in Orlando, Florida, Chicago, Illinois and Westwood, California remain outstanding for security deposits.

Note 8 - Nonconsolidated variable interest entities:

Accounting principles generally accepted in the United States of America provide a framework for identifying variable interest entities (VIEs) and determining when a company should include the assets, liabilities, noncontrolling interests, and results of activities of a VIE in its consolidated financial statements. In general, a VIE is a corporation, partnership, limited-liability corporation, trust, or any other legal structure used to conduct activities or hold assets that (1) has an insufficient amount of equity to carry out its principal activities without additional subordinated financial support, (2) has a group of equity owners that are unable to direct the activities of the entity that most significantly impact its economic performance, or (3) has a group of equity owners that do not have the obligation to absorb losses of the entity or the right to receive returns of the entity. A VIE should be consolidated if a party with an ownership, contractual, or other financial interest in the VIE that is considered a variable interest (a variable interest holder) has the power to direct the VIE’s most significant activities and the obligation to absorb losses or right to receive benefits of the VIE that could be significant to the VIE. A variable interest holder that consolidates the VIE is called the primary beneficiary. Upon consolidation, the primary beneficiary generally must initially record all of the VIE’s assets, liabilities, and noncontrolling interests at fair value and subsequently account for the VIE as if it were consolidated based on majority voting interest. At September 30, 2015 and December 31, 2014, the Company held investments that were evaluated against the criteria for consolidation and determined that it is not the primary beneficiary of the investments because the Company lacks the power to direct the activities of the variable interest entities that most significantly impacts their economic performance. Therefore, consolidation in the Company’s financial statements is not required. At September 30, 2015 and December 31, 2014, the Company held the following equity investments:

	At September 30, 2015	At December 31, 2014
Bagatelle NY LA Investors, LLC ("Bagatelle Investors")	$68,469	$357,896
Bagatelle Little West 12th, LLC ("Bagatelle NY")	2,391,000	1,938,252
Bagatelle La Cienega, LLC ("Bagatelle LA")	—	—
One 29 Park, LLC ("One 29 Park")	532,138	506,295
Totals	$2,991,607	$2,802,443

	Three Months Ended September 30,		Nine Months Ended September 30,	
	2015	2014	2015	2014
Equity in income of investee companies	$(205,273)	$(268,660)	$(728,504)	$(588,996)

Bagatelle Investors is a holding company that has interests in two operating restaurant companies, Bagatelle NY and Bagatelle LA. All three entities were formed in 2011. The Company holds interests in all three entities. The Company holds a 31.24% ownership over Bagatelle Investors as of September 30, 2015 and December 31, 2014. The Company holds a 5.23% direct ownership over Bagatelle NY and has indirect ownership through Bagatelle Investors as well as one of its subsidiaries of 45.90% for a total effective ownership of 51.13% as of September 30, 2015 and December 31, 2014. The Company holds a 5.23% direct ownership over Bagatelle LA and has indirect ownership through Bagatelle Investors as well as one of its subsidiaries of 38.10% for a total effective ownership of 43.33% as of September 30, 2015 and December 31, 2014. The Company holds a 10% direct ownership over One29 Park as of September 30, 2015 and December 31, 2014. The Company accounts for its investment in One 29 Park under the equity method since it has ability to exercise significant influence over the entity.

During the quarter and year ended September 30, 2015 and December 31, 2014, respectively, the Company provided no explicit or implicit financial or other support to these VIEs that were not previously contractually required.

The amounts presented above represent maximum exposure to loss.

Note 9 - Related party transactions:

Due from related parties consists of amounts related to the Company and its related entities which arose from noninterest bearing cash advances and are expected to be repaid within the next twelve months. As of September 30, 2015 and December 31, 2014, these advances aggregated to a total of $1,369,795 and $1,157,134, respectively.

The Company incurred approximately $104,000 and $144,000 for the three months ended September 30, 2015 and 2014, respectively, and $382,000 and $380,000 for the nine months ended September 30, 2015 and 2014, respectively, for design services at various restaurants to an entity owned by one of the Company’s shareholders. Included in accounts payable and accrued expenses at September 30, 2015 and December 31, 2014 is a balance due to this entity of approximately $45,000 and $0, respectively.

The Company incurred approximately $213,000 and 168,000 for the three months ended September 30, 2015 and 2014, and $422,000 and $385,000 for the nine months ended September 30, 2015 and 2014, respectively, for legal fees to an entity owned by one of the Company’s shareholders. Included in accounts payable and accrued expenses at

September 30, 2015 and December 31, 2014 is a balance due to this entity of approximately $187,000 and $70,000, respectively. The Company also received rental income on office space sublet to this entity of $40,207 and $24,000 for the three months ended September 30, 2015 and 2014 and $98,452 and $72,000 for the nine months ended September 30, 2015 and 2014, respectively, there were no receivables outstanding at September 30, 2015 and December 31, 2014, respectively.

The Company incurred approximately $3.6 million and $807,000 for the three months ended September 30, 2015 and 2014, respectively, and $8.3 million and $3.1 for the nine months ended September 30, 2015 and 2014, respectively, for construction services to an entity owned by one of the Company's shareholders. Included in accounts payable at September 30, 2015 and December 31, 2014 is a balance due to this entity of $187,000 and $6,669, respectively.

Note 10 – Derivative liability:

On October 16, 2013, the Merger provided for up to an additional $14,100,000 of payments to the former holders of ONE Group membership interests (the "TOG Members") and to a liquidating trust (the "Liquidating Trust") established for the benefit of the TOG Members and the holders of warrants to acquire membership interests of ONE Group (the "TOG Warrant Owners") based on a formula as described in the Merger Agreement and which is contingent upon the exercise of outstanding Company warrants to purchase 5,750,000 shares of Common Stock at an exercise price of $5.00 per share (the "Parent Warrants"). The Company is required to make any payments on a monthly basis. Additionally, certain ONE Group employees are entitled to receive a contingent sign-on bonus of an aggregate of approximately $900,000 upon the exercise of the Parent Warrants. Any Parent Warrants that are unexercised will expire on the date that is the earlier of (i) February 27, 2016 or (ii) the forty-fifth (45th) day following the date that the Company's Common Stock closes at or above $6.25 per share for 20 out of 30 trading days commencing on February 27, 2014.

The Company estimates the fair value of the derivative liability using the Monte Carlo method, which is comprised of the $14,100,000 in payments and the $900,000 in contingent sign-on bonus for a total of $15,000,000. The fair value of the derivative liability was initially measured on October 16, 2013 and is re-measured at the end of every reporting period with the change in value over the period reported in the statements of operations and comprehensive income (loss) as a derivative income or loss. In applying the Monte Carlo method, the Company uses the following key inputs and assumptions; the stock price on the valuation date, the exercise price of the warrants of $5.00, the trigger price of $6.25, the expected volatility which is based on an analysis of comparable companies historical stock price volatilities for a period comparable to the term of the warrants, the expected months until effective registration statement, the term based on the period from the valuation date until the two-year period following the expected date of the effective registration, the risk-free rate based on the rate of US treasury securities with the same term and the discount rate based on the aggregate of the expected short-term margin and the risk-free rate.

The following tables summarize the inputs and assumptions used in valuing derivative liabilities:

	September 30, 2015		December 31, 2014	
Fair value of derivative liability (3)	$2,324,000		$6,241,000	
Significant assumptions (or ranges):				
Trading market values (1)	$3.55		$4.85	
Term (years) (2)	4 months, 27 days		1 year, 58 days	
Expected volatility (1)	67.0	%	26.8	%
Risk-free rate (2)	0.05	%	0.32	%
Discount rate (3)	0.91	%	1.18	%
Effective Exercise price (2)	$5.00		$5.00	
Trigger price (2)	$6.25		$6.25	

Fair value hierarchy:

(1) Level 1 inputs are quoted prices in active markets for identical assets and liabilities, or derived therefrom.
(2) Level 2 inputs are inputs other than quoted prices that are observable.

(3) Level 3 inputs are unobservable inputs. Inputs for which any parts are level 3 inputs are classified as level 3 in their entirety.

The Company recorded $1,139,000 and $3,917,000 of income from the change in the fair value of the derivative liability balance during the three and nine months ended September 30, 2015.

Note 11 - Commitments and contingencies:

Operating leases:
The Company is obligated under several operating leases for the restaurants, equipment and office space, expiring in various years through 2031, which provide for minimum annual rentals, escalations, percentage rent, common area expenses or increases in real estate taxes.

Future minimum rental commitments under the leases and minimum future rental income per the sublease in five years subsequent to September 30, 2015 and thereafter are as follows:

Year Ending December 31,	Expense	Income	Net Amount
2015	$ 1,490,030	$ (314,829)	$ 1,175,201
2016	8,337,502	(1,279,269)	7,058,233
2017	8,183,697	(1,059,545)	7,124,152
2018	8,306,805	(1,079,640)	7,227,165
2019	8,434,651	(1,116,229)	7,318,422
Thereafter	110,944,547	(3,084,946)	107,859,601
Total	$ 145,697,232	$ (7,934,458)	$ 137,762,774

Rent expense (including percentage rent of $71,428 and $101,936 for the three months ended September 30, 2015 and 2014, respectively and $239,204 and $329,545 for the nine months ended September 30, 2015 and 2014, respectively), included in continued operations, amounted to $937,700 and $779,164 for the three months ended September 30, 2015 and 2014 and $2,832,266 and $2,802,466 for the nine months ended September 30, 2015 and 2014, respectively. Rent expense included in continuing operations has been reported in the consolidated statements of operations and comprehensive loss net of rental income of $179,186 and $188,480 for the three months ended September 30, 2015 and 2014, respectively and $545,348 and $600,099 for the nine months ended September 30, 2015 and 2014, respectively, related to subleases with related and unrelated parties which expire through 2025.

License and management fees:
Pursuant to its amended and restated operating agreement executed in June 2007, Bridge Hospitality, LLC is obligated to pay management fees equal to 2% of revenues to a member for the life of the agreement. Management fees amounted to $258 and $19,156 for the three months ended September 30, 2015 and 2014, respectively and $39,132 and $60,324 for the nine months ended September 30, 2015 and 2014, respectively. Included in accounts payable at September 30, 2015 and December 31, 2014 are amounts due for management fees of $0 and $27,365, respectively.

In January 2010, STK Vegas entered into a management agreement with a third party for a term of 10 years, with two five-year option periods. Under this agreement, STK Vegas shall receive a management fee equal to 5% of gross sales, as defined (“gross sales fee”) plus 20% of net profits prior to the investment breakeven point date and 43% of net profits thereafter (“incentive fee”). In addition, STK Vegas is entitled to receive a development fee equal to $200,000. The Company has elected to receive a credit against a portion of its obligation (estimated at approximately $387,000) to fund the build-out in lieu of receiving the $200,000. Management fees amounted to $1,015,876 and $1,059,993 for the three months ended September 30, 2015 and 2014, respectively, and $3,589,914 and $3,604,433 for the nine months ended September 30, 2015 and 2014, respectively.

In July 2009, One 29 Park Management entered into an agreement with a third party. Under this agreement, One 29 Park Management shall receive a management fee equal to 5% of gross revenues, as defined, from the restaurant, banquets, room service and rooftop sales and 50% of the base beverage fee, as defined, for the life of the management agreement which expires in 2025. Management fees amounted to $148,521 and $163,199 for the three months ended September 30, 2015 and 2014, respectively, and $425,469 and $462,313 for the nine months ended September 30, 2015 and 2014, respectively.

In July 2010, Hip Hospitality UK entered into a management agreement with a third party to manage and operate the food and beverage operations in the Hippodrome Casino in London. Under this agreement, Hip Hospitality UK shall receive a management fee equal to 5.5% of total revenue, as defined, as well as an incentive fee if certain conditions are met, for the life of the management agreement which expires in 2022. Management fees amounted to $148,191 and $195,792 for the three months ended September 30, 2015 and 2014, respectively, and $476,608 and $554,039 for the nine months ended September 30, 2015 and 2014, respectively. Included in accounts receivable and other assets at September 30, 2015 and December 31, 2014 are amounts due for management fees and reimbursable expenses of $313,685 and $377,320, respectively.

In December 2011, TOG Aldwych entered into a management agreement with a third party to operate a restaurant, bar and lounges in the ME Hotel in London. Under this agreement, TOG Aldwych shall receive a management fee equal to 5% of receipts received from food and beverages operations. In addition, TOG Aldwych is entitled to receive a monthly marketing fee equal to 1.5% of receipts received from food and beverages operations and an additional fee equal to 65% of net operating profits, as defined, for the life of the management agreement which expires in 2032. Management fees amounted to $346,448 and $430,450 for the three months ended September 30, 2015 and 2014, respectively, and $940,997 and $1,129,341 for the nine months ended September 30, 2015 and 2014, respectively. Included in accounts receivable at September 30, 2015 and December 31, 2014 are amounts due for management fees of $929,689 and $200,124, respectively.

In June 2014, TOG (Milan) S.R.L. entered into a management agreement with Sol Melia Italia S.R.L. to operate a restaurant, rooftop bar and food and beverage services at the ME Milan Il Duca hotel in Milan, Italy. TOG (Milan) S.R.L. shall receive a management fee equal to 5% of operating revenue, as defined, and an additional fee equal to 65% of net operating revenue, as defined, for the life of the management agreement which expires in 2025. In addition, TOG (Milan) S.L.R. is entitled to receive a monthly marketing fee equal to 1.5% of operating revenues. Management fees amounted to $154,241 for the three and nine months ended September 30, 2015. Included in accounts receivable and other assets at September 30, 2015 are amounts due for management fees of $430,084.

Note 12 - Discontinued operations:
Management decided to cease operations for the following entities in 2014: Miami Services and Tenjune.

On May 1, 2014, the Company entered into a settlement agreement and mutual general release with the landlord of the Bagatelle in Las Vegas, which closed in 2014. In connection with this release, the Company agreed to make certain payments to the landlord and on May 22, 2014 made a payment for the remaining balance on an operating lease for certain equipment that was at the location.

On May 30, 2014, the Company entered into a termination, mutual release and settlement agreement with a third party in Las Vegas (“Owners”) for the management agreement for the Heraea property and the lease agreement for the Xi Shi property in Las Vegas. In connection with this release, the Company agreed to make certain payments to the Owners.

The following table shows the components of assets and liabilities that are classified as discontinued operations in the Company's consolidated balance sheets as of September 30, 2015 and December 31, 2014:

	September 30, 2015	December 31, 2014
Other current assets	$48,343	$67,676
Due from related parties	806,846	814,227
Assets of discontinued operations - current	855,189	881,903
Property and equipment, net	169,175	169,175
Security deposits	75,000	75,000
Assets of discontinued operations - long term	244,175	244,175
Accounts payable and accrued liabilities	409,108	551,266
Due to related parties (1)	3,606,667	3,654,552
Liabilities of discontinued operations - current	4,015,775	4,205,818
Net assets	$(2,916,411)	$(3,079,740)

(1) Note - due to related parties represents amounts due to consolidating entities that are eliminated in consolidation.

Summarized operating results related to these entities are included in discontinued operations in the accompanying consolidated statements of operations and comprehensive loss for the three and nine months ended September 30, 2015 and 2014:

	Three Months Ended September 30, 2015	Three Months Ended September 30, 2014	Nine Months Ended September 30, 2015	Nine Months Ended September 30, 2014
Revenue	$—	$—	$—	$102,330
Costs and Expenses	(62,501)	(177,050)	(23,929)	1,196,706
Net loss from discontinued operations, net of taxes	$62,501	$177,050	$23,929	$(1,094,376)

Note 13 - Litigation:
The Company is party to claims in lawsuits incidental to its business. In the opinion of management, the ultimate outcome of such matters, individually or in the aggregate, will not have a material adverse effect on the Company's consolidated financial position or results of operations.

Note 14 - Stockholders' equity:
The Company is authorized by its amended and restated certificate of incorporation to issue up to 75,000,000 shares of Common Stock, par value $0.0001 per share, and 10,000,000 shares of preferred stock, par value $0.0001 per share. As of September 30, 2015 and December 31, 2014, there were 24,972,515 and 24,940,195, outstanding shares of Common Stock, respectively, and no outstanding shares of preferred stock.

Note 15 - Stock-based compensation:
In October 2013, the board of directors approved the 2013 Employee, Director and Consultant Equity Incentive Plan (the "2013 Plan") pursuant to which the Company may issue options, warrants, restricted stock or other stock-based awards to directors, officers, key employees and other key individuals performing services for the Company. The 2013 Plan has reserved 4,773,992 shares of common stock for issuance. All awards will be approved by the board of directors or a committee of the board of directors to be established for such purpose.

The Company's outstanding stock options have maximum contractual terms of up to ten years, principally vest on a quarterly basis ratably over five years and were granted at exercise prices equal to the market price of the Company's common stock on the date of grant. The Company's outstanding stock options are exercisable into shares of the Company's common stock. The Company measures the cost of employee services received in exchange for an award of equity instruments, including grants of employee stock options and restricted stock awards, based on the fair value of the award at the date of grant in accordance with the modified prospective method. The Company uses the Black-Scholes model for purposes of determining the fair value of stock options granted and recognizes compensation costs ratably over the requisite service period, net of estimated forfeitures. For restricted stock awards, the grant-date fair value is the quoted market price of the stock.

As of September 30, 2015, all 1,702,578 options outstanding were excluded from the calculation of dilutive earnings per share as their effect would have been anti-dilutive as the exercise price of these grants are above the average market price.

For the three months ended September 30, 2015 and 2014, the Company recognized $162,850 and $159,385, respectively, and for the nine months ended September 30, 2015 and 2014, the Company recognized $506,853 and $326,753 of non-cash stock-based compensation expense related to options, respectively, in general and administrative expense in the consolidated statements of operations.

As of September 30, 2015, there was approximately $3,733,014 of total unrecognized compensation cost related to unvested share-based compensation grants, which is expected to be amortized over a weighted-average period of 4.6 years.

A summary of the status of stock option awards and changes during the nine months ended September 30, 2015 are presented below:

	Shares	Weighted Average Exercise Price	Weighted Average Remaining Contractual Life (Years)