

Clearfield, Inc.
Form 4
August 25, 2014

FORM 4

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

OMB APPROVAL

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STATEMENT OF CHANGES IN BENEFICIAL OWNERSHIP OF SECURITIES

Filed pursuant to Section 16(a) of the Securities Exchange Act of 1934, Section 17(a) of the Public Utility Holding Company Act of 1935 or Section 30(h) of the Investment Company Act of 1940

(Print or Type Responses)

1. Name and Address of Reporting Person *
HERZOG DANIEL R

(Last) (First) (Middle)
**CLEARFIELD, INC., 5480
NATHAN LANE**

(Street)

PLYMOUTH, MN 55442

(City) (State) (Zip)

2. Issuer Name and Ticker or Trading Symbol
Clearfield, Inc. [CLFD]

3. Date of Earliest Transaction (Month/Day/Year)
08/21/2014

4. If Amendment, Date Original Filed(Month/Day/Year)

5. Relationship of Reporting Person(s) to Issuer

(Check all applicable)

___ Director ___ 10% Owner
 Officer (give title below) ___ Other (specify below)
Chief Financial Officer

6. Individual or Joint/Group Filing(Check Applicable Line)
 Form filed by One Reporting Person
 Form filed by More than One Reporting Person

Table I - Non-Derivative Securities Acquired, Disposed of, or Beneficially Owned

1. Title of Security (Instr. 3)	2. Transaction Date (Month/Day/Year)	2A. Deemed Execution Date, if any (Month/Day/Year)	3. Transaction Code (Instr. 8)	4. Securities Acquired (A) or Disposed of (D) (Instr. 3, 4 and 5)	5. Amount of Securities Beneficially Owned Following Reported Transaction(s) (Instr. 3 and 4)	6. Ownership Form: Direct (D) or Indirect (I) (Instr. 4)	7. Nature of Ownership (Instr. 4)
				(A) or (D) Price			
Restricted Stock ⁽¹⁾	08/21/2014		A	V Amount (D) Price 15,000 A \$ 0	51,060	D	

Reminder: Report on a separate line for each class of securities beneficially owned directly or indirectly.

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SEC 1474 (9-02)

Table II - Derivative Securities Acquired, Disposed of, or Beneficially Owned (e.g., puts, calls, warrants, options, convertible securities)

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1. Title of Derivative Security (Instr. 3)	2. Conversion or Exercise Price of Derivative Security	3. Transaction Date (Month/Day/Year)	3A. Deemed Execution Date, if any (Month/Day/Year)	4. Transaction Code (Instr. 8)	5. Number of Derivative Securities Acquired (A) or Disposed of (D) (Instr. 3, 4, and 5)	6. Date Exercisable and Expiration Date (Month/Day/Year)	7. Title and Amount of Underlying Securities (Instr. 3 and 4)	8. Price of Derivative Security (Instr. 5)	9. Number of Derivative Securities Owned Following Reporting Transaction (Instr. 6)
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Reporting Owners

Reporting Owner Name / Address	Relationships			
	Director	10% Owner	Officer	Other
HERZOG DANIEL R CLEARFIELD, INC. 5480 NATHAN LANE PLYMOUTH, MN 55442			Chief Financial Officer	

Signatures

Randy Dehmer by Power of Attorney for Daniel R. Herzog 08/25/2014

**Signature of Reporting Person Date

Explanation of Responses:

- * If the form is filed by more than one reporting person, see Instruction 4(b)(v).
- ** Intentional misstatements or omissions of facts constitute Federal Criminal Violations. See 18 U.S.C. 1001 and 15 U.S.C. 78ff(a).
- (1) The restricted stock vests as to one-tenth of the shares on the first ten anniversaries of the date of grant subject to the reporting person's continued employment through each such date.

Note: File three copies of this Form, one of which must be manually signed. If space is insufficient, see Instruction 6 for procedure. Potential persons who are to respond to the collection of information contained in this form are not required to respond unless the form displays a currently valid OMB number. er=0>

Item 1.

Business

Overview

Kona Grill, Inc. (referred to herein as the “Company” or “we,” “us,” and “our”) currently owns and operates 30 polished casual restaurants in 19 states. Our restaurants offer freshly prepared food, attentive service, and an upscale contemporary ambiance that create an exceptional, yet affordable dining experience that we believe exceeds many traditional casual dining restaurants with whom we compete. Our high-volume polished casual restaurants feature a diverse selection of flavorful American food, internationally influenced appetizers and entrees and an extensive selection of award-winning sushi. Our menu items are prepared from scratch at each restaurant location and incorporate over 40 signature sauces and dressings, creating memorable flavor profiles that appeal to a diverse group of customers. Our diverse menu is complemented by a full service bar offering a broad assortment of wines, specialty cocktails, and beers. We believe that our innovative high-quality recipes, generous portions, and flexible price points provide customers with an excellent value proposition and allow us to attract a diverse customer base.

Our restaurants seat an average of 294 customers and are comprised of multiple dining areas that incorporate modern design elements to create an upscale ambiance that reinforces our high standards of food and service. Our main dining area, full-service bar, indoor/outdoor patio, and sushi bar provide a choice of atmospheres and a variety of environments designed to attract new customers and encourage repeat visits from regular customers. We locate our restaurants in high-activity areas such as retail centers, shopping malls, urban entertainment districts, and lifestyle centers that are situated near commercial office space and residential housing to attract customers throughout the day.

We believe that the portability of our concept has been successfully demonstrated in a variety of markets across the United States (U.S.). We plan to grow organically through unit expansion, with a target of 20% unit growth annually over the next several years by strategically expanding the Kona Grill concept in both new and existing markets. Furthermore, given the broad appeal of our concept across the U.S. and the increased demand for polished casual dining concepts overseas, we believe there is a significant opportunity to expand our concept in Latin America, the Middle East and beyond over the long term.

Competitive Strengths

The restaurant business is intensely competitive with respect to food quality, price-value relationships, ambiance, service and location. We believe that the key strengths of our business include the following:

Innovative Menu Selections with Mainstream Appeal. We offer a menu of freshly prepared, high quality food that includes a diverse selection of flavorful American favorites with an international influence and award-winning sushi items to appeal to a wide range of tastes, preferences, and price points. We prepare our dishes from scratch at each restaurant location using original recipes with generous portions and creative and appealing presentations that adhere to standards that we believe are much closer to fine dining than typical casual dining. Our more than 40 signature sauces and dressings create memorable flavor profiles and further differentiate our menu items. With an average check during 2014 of approximately \$25 per customer, we believe we provide an exceptional price-value proposition that helps create a lasting relationship between Kona Grill and our customers.

Distinctive Polished Casual Dining Experience. Our polished casual dining concept captures some of the best elements of fine dining including a variety of exceptional food options, attentive service, and an extensive wine and cocktail list, and combines them with the traditional casual dining attributes, like a broad menu with attractive price points and a choice of environments suitable for any dining occasion. Our creative menu, personalized service, and contemporary restaurant design blend together to create an inviting polished casual dining experience. We design our restaurants with a unique layout and utilize modern, eye-catching design elements to enhance the customer experience. Our multiple dining areas provide customers with a number of distinct dining environments and atmospheres to suit a range of dining occasions. Our open exhibition-style kitchen and sushi bar further emphasize the quality and freshness of our food that are the cornerstones of our concept.

Significant Bar and Happy Hour Business. Our high-energy bar and patio offer a distinctive atmosphere where customers can enjoy our alcoholic beverage offerings. Our patio is a popular place for customers to enjoy our high-value happy hour and reverse happy hour offerings, where full portions of select items are offered at reduced price points. Our patio, which is enclosed in colder climate locations, provides a year-round sales opportunity and is a key driver in generating business during non-traditional periods. Aggregate restaurant sales during these non-peak periods accounted for 24.7% of our total sales during 2014, which we believe provides us with a competitive advantage.

Personalized Customer Service. Our commitment to provide prompt, friendly, and efficient service enhances our food, reinforces our upscale ambiance, and helps distinguish us from other traditional casual dining restaurants. We train our service personnel to be cordial, friendly, and knowledgeable about all aspects of the restaurant, especially the menu and the wine list, which helps us provide personalized customer service that is designed to ensure an enjoyable dining experience and exceed our customers' expectations. Our kitchen staff completes extensive training to ensure that menu items are precisely prepared to provide a consistent quality of taste. We believe our focus on high service standards underscores our customer-centric philosophy.

Multiple Daypart Model. Our appetizers, flatbreads, entrees, and sushi offerings provide a flexible selection of items that can be ordered individually or shared allowing customers to dine with us during traditional lunch and dinner meal periods as well as between customary dining periods such as in the late afternoon and late night. The lively ambiance of our patio and bar areas provides an energetic social forum that attracts a young professional clientele during non-peak periods, as well as provides a unique atmosphere for all of our customers to enjoy before or after they dine with us. Our sushi bar provides another dining venue for customers while offering a wide selection of creative and flavorful menu items for our health conscious customers. We believe that our ability to attract customers throughout the day distinguishes us from many other casual dining chains and helps us maximize sales and leverage our fixed operating costs.

Attractive Unit Economics. During 2014, the average unit volume of our comparable base restaurants was \$4.4 million. We believe our average unit volume helps us attract high-quality employees, leverage fixed costs, and makes us a desirable tenant for landlords. We expect the average cash investment for new restaurants to be approximately \$2.5 million, net of landlord tenant improvement allowances and excluding preopening expenses. Based on historical experience, restaurants that are subject to ground leases and do not receive landlord tenant improvement allowances may require a significantly higher cash investment, but typically have lower average rental costs over the duration of the lease.

Growth Strategy

We believe that there are significant opportunities to grow our sales and increase our brand awareness throughout the United States and internationally. The following sets forth the key elements of our growth strategy.

Pursue Disciplined Restaurant Growth

Explanation of Responses:

We review potential sites in both new and existing markets that meet our target customer demographics, real estate, and investment return criteria. We believe the location of our restaurants plays a pivotal role in determining the long-term profitability of each restaurant and, accordingly, we spend significant time and resources to evaluate each prospective site. We utilize a disciplined site selection process involving our management team and Board of Directors. Our site selection criteria for new restaurants include locating our restaurants near high activity areas such as retail centers, shopping malls, and lifestyle and entertainment centers. In addition, we focus on areas that have above-average density and income populations, have high customer traffic throughout the day from thriving businesses or retail markets, and are convenient for and appealing to business and leisure travelers. We also focus on sites that have great visibility and ample parking to support high volumes of traffic.

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We plan to grow organically through unit expansion, with a target of 20% unit growth annually over the next several years. We achieved a unit growth rate of 20% for 2014, with five openings during the year, including the Fort Worth, Texas restaurant in the first quarter, the El Paso, Texas location in the second quarter and the Sarasota, Florida; Alpharetta, Georgia and Columbus, Ohio restaurants in the fourth quarter. We plan to open seven restaurants during 2015, which equates to 23% unit growth. We currently have twelve signed leases for new restaurant openings in 2015 and beyond and continue working diligently to build our pipeline for future growth.

With the acceleration of unit growth in 2014, we have incurred significant preopening expense in 2014 and expect to continue to incur such expenses in 2015 as we increase the number of new restaurant openings in 2015. We expect the opening of new units to place downward pressure on our profitability as significant preopening expenses are incurred while operating profit from the new restaurants will likely not be significant in the first few months of each new restaurant's operation as a result of start-up inefficiencies typically associated with opening new restaurants. Although the actual preopening expenses for a particular location depend upon numerous factors, we expect to incur cash preopening expenses of approximately \$425,000 per location, and non-cash preopening rent expense ranging from \$50,000 to \$100,000 per location.

Our growth strategy for developing new restaurants also includes expansion in existing markets that have the appropriate demographics to support multiple restaurants. Operating multiple restaurants in existing markets enables us to leverage our brand equity as well as gain operating efficiencies associated with regional supervision, marketing, purchasing, and hiring. In addition, our ability to hire qualified employees is enhanced in markets where we enjoy greater brand awareness and we are able to utilize existing employees in new restaurants. Our expansion plans currently do not involve any franchised restaurant operations in the U.S.

In addition, we have started to explore our potential expansion into international markets. Given the strength our concept has enjoyed thus far in the U.S. and the increased demand for polished casual dining concepts overseas, we believe there is a significant opportunity to expand our concept in Latin America, the Middle East and beyond. Similar to other brands with international expansion, we plan to utilize a franchise model for development outside the U.S. Under this model, we will provide training and operational support to our partners without committing, or putting at risk, capital for restaurant construction in these international markets. Our international strategy is still in its early stages as it will take time for us to identify franchise partners and negotiate franchise agreements and for our partners to find quality real estate and construct the restaurants. We will then need to train the local team on our food and hospitality standards to ensure a successful execution of our strategy. We expect to make several investments in the coming year, including developing marketing materials, obtaining trademarks in the requisite markets and incurring incremental travel and networking expenses in order to build the right foundation for our growth.

Grow Existing Restaurant Sales

Our goal for existing restaurants is to increase unit volumes through the execution of our differentiated business model and complimented with ongoing social marketing efforts as well as local market advertising and other initiatives designed to generate awareness and trial of our concept and increase the frequency of customer visits. While many segments within the restaurant industry experienced a decline in same-store sales and customer traffic during 2014, our restaurant sales for comparable base restaurants, which include those units open for more than 18 months, increased 3.8% compared to 2013. The increase reflects a 2.9% increase in customer traffic and a 0.9% increase in average check per person. Our same-store sales for 2014 successfully lapped a 1.4% same-store sales increase during 2013. We believe the strength of our differentiated concept and the appeal of our new design enables us to gain market share, as evidenced by the positive same-store sales growth in the last seven quarters and in the past 17 out of 18 quarters.

We also continue to focus on our four wall execution with key initiatives designed to drive traffic, increase sales and enhance the customer experience while building our business for long-term growth. Our food-based promotions, which include innovative seasonal menu items, are offered four times during the year. These initiatives are highly successful in keeping our menu fresh and exciting while also providing a great venue to test the popularity of new menu items and the opportunity to place top-selling items on our regular menu. We continue to enhance our wine list and utilize our Wine Down Wednesday offering to drive customer traffic by offering a 50% discount on bottle wines each Wednesday. Our value-driven happy hour price-points help drive incremental sales and customer traffic during non-peak hours. Our To Go program and catering services continued to gain traction and increased in absolute dollars year over year. We had record gift card sales during the holiday season, with a 38% increase year over year, driven by targeted marketing initiatives. Furthermore, we continue to focus on the quality of our service and hospitality and improve our customer satisfaction with extensive training for our service staff on our wine list, drink and menu offerings. We continue to grow our customer loyalty program, Konavore, which has grown to over 225,000 members since its inception in 2010. We utilize this e-mail based program to communicate new menu offerings, restaurant specific events, and other marketing messages to keep Kona Grill top of mind for consumers. We have also increased our presence in social marketing and interactive advertising. Furthermore, we utilize a customer satisfaction survey across the entire brand to provide valuable feedback that our management team can respond to immediately. We believe we can generate additional sales through these programs at a reasonable cost per restaurant.

Continue Strategic Investments in Personnel and Systems

We believe that successful execution of our growth strategies will enable Kona Grill to be a leading polished casual dining restaurant operator in the United States. During the past two years, we have made strategic personnel investments in order to re-ignite the expansion of our concept and continue making additional investments in both operations and development personnel to support our accelerated new unit expansion and international business development initiatives. Additionally, we continue to implement information systems and tools to enhance our business while ensuring that strong financial controls are in place to minimize risks associated with our current growth strategy.

Expansion Strategy and Site Selection

We believe the location of our restaurants is critical to our long-term success and, accordingly, we devote significant time and resources to analyzing each prospective site. Our restaurant expansion strategy focuses primarily on penetrating new markets in major metropolitan areas throughout the United States and existing markets where demographic information supports the building of additional restaurants. In general, we prefer to open restaurants in high-profile sites within specific trade areas with the following considerations:

suitable demographic characteristics, including residential and commercial population density and above-average household incomes;

great visibility;

high traffic patterns;

general accessibility;

availability of suitable parking;

proximity of shopping areas and office parks;

degree of competition and the operating performance of those competitors within the trade area; and

general availability of restaurant-level employees.

These sites generally include high-volume retail centers, shopping malls, and lifestyle and entertainment centers.

We thoroughly analyze each prospective location before presenting the site to our Real Estate Committee, comprised of members of the Board of Directors, for review. Prior to committing to a restaurant site and signing a lease, our Chief Executive Officer, Vice President of Development and a member of the Real Estate Committee visit the prospective site and evaluate the proposed economics of the restaurant based on demographic data and other relevant criteria to assure that the site will meet our return on investment criteria.

We lease all of our restaurant sites under lease terms that vary by restaurant; however, we generally lease space (freestanding or in-line) for 10 to 20 years and negotiate at least two five-year renewal options. Our rent structures vary from lease to lease, but generally provide for the payment of both minimum base rent and contingent rent based on restaurant sales. We are also generally responsible for a proportionate share of common area maintenance, property tax, insurance, and other occupancy-related expenses.

We believe our average unit volumes, differentiated menu and multi-daypart model make us an attractive tenant and provide us with multiple opportunities to obtain suitable leasing terms from landlords. As a result of the locations we select, which are often in new retail center or shopping mall developments, our restaurant development timeframes vary according to the landlord's construction schedule and other factors that are beyond our control. Once the site has been turned over to us, the typical lead-time from commencement of construction to opening is approximately six months.

Unit Economics

We target a 31% to 33% net cash-on-cash return for our restaurants once they reach their mature level of operations. Maturation periods vary from restaurant to restaurant, but generally range from two to four years. During 2014, the average unit volume of our comparable base restaurants was \$4.4 million, a 4.3% increase from 2013 demonstrating the strength and broad appeal of our concept. We generated restaurant-level operating profit of \$21.4 million during 2014, an increase of 18.3% from prior year. Our restaurant operating margin for comparable base restaurants was 18.7% in 2014 which was at the high end of our targeted range of 18% to 19%. The cash-based performance target for our restaurant operations does not include field supervision, corporate support expenses, preopening expenses, or non-cash items such as depreciation and amortization; and does not represent a targeted return on investment in our common stock.

Our investment cost for new restaurants varies significantly depending upon the location of the restaurant, the type of lease entered into and the amount of tenant improvement allowance we receive from landlords. We expect the cash investment cost of our prototype restaurant on average to be approximately \$2.5 million, net of landlord tenant improvement allowances averaging between \$0.7 million and \$1.2 million, and excluding cash preopening expenses of approximately \$425,000.

Our ability to generate sales throughout the day is a key strength of our concept. The following table depicts the amount and percentage of contribution for each daypart of overall restaurant sales during 2014.

2014 Sales by Daypart

Explanation of Responses:

	Sales	Percent	
	(Dollars in thousands)		
Lunch (Open to 3 p.m.)	\$29,025	24.4	%
Dinner (5 p.m. to 9 p.m.)	60,622	50.9	%
Non-Peak (3 p.m. to 5 p.m. and 9 p.m. to Close)	29,450	24.7	%
Total All Day	\$119,097	100.0	%

Menu

Our menu offers customers a diverse selection of flavorful American favorites with an international influence and award-winning sushi items. This diverse menu is an important factor in differentiating ourselves from other polished casual dining competitors. We offer over 40 freshly prepared signature sauces and dressings, which distinguish and complement our dishes and create delicious flavor profiles that appeal to our customers. Our menu items are prepared from scratch at each restaurant location using fresh high quality ingredients and adhere to food standards that we believe are much closer to fine dining than typical casual dining.

Our menu features a selection of appetizers, salads, soups, flatbreads, sandwiches, noodles, seafood, signature entrees, and desserts. We round out our menu with over 60 hand-made award-winning sushi choices. Our appetizers include socially interactive items that can be eaten individually or easily shared among customers. Our signature entrees feature various sauces and offer customers generous portions that are impressive in presentation and in taste. For example, our most popular entrée is the Macadamia Nut Chicken served with shoyu-cream sauce and accompanied by parmesan garlic mashed potatoes and seasonal vegetables. Other favorites include Miso-Sake Sea Bass served with shrimp and pork fried rice and a seasonal vegetable and Pan-Seared Ahi served with steamed white rice, baby bok choy and a sweet chili sauce.

We are also known for our extensive assortment of sushi that includes traditional favorites as well as distinctive specialty sushi and sashimi items such as our Voodoo Roll made with spicy crawfish mix and avocado rolled inside of seaweed and topped with a habanero tuna mix and chili masago, or the Bama Roll made with crab mix, cream cheese and jalapeno in soy paper topped with tuna, avocado, fish roe and spicy mayo. Our menu, coupled with an expansive selection of sushi, offers ample choices for health conscious customers. We take great pride in providing our customers the full Kona Grill experience without compromising their dietary needs and restrictions. We offer extensive gluten-free, vegetarian and vegan menus. We also feature a bento box with a variety of selections of protein and side dishes for the enjoyment of our young customers.

Each of our restaurants has a dedicated kitchen staff member, whom we refer to as our saucier, to oversee the preparation of more than 40 signature sauces and dressings that are made from scratch using only high-quality ingredients and fresh products. Each sauce is designed according to a proprietary recipe for specific menu items and includes unique flavors and combinations such as our honey cilantro, shoyu-cream, and spicy aioli dipping sauces, and our sesame-soy and honey dijon dressings. We believe that these distinctive sauces and dressings provide a unique flavor profile, which further distinguishes Kona Grill from its competitors. Our flavorful sauces and dressings also enhance the overall dining experience for our customers by allowing them to not only experience new tastes but to also share their favorite sauces with others, helping to foster customer loyalty and a socially interactive dining experience.

The versatility of our menu enables us to provide customers with dishes that can be enjoyed outside of the traditional lunch and dinner meal periods, as well as to serve our customers' requirements for a variety of dining occasions, including everyday dining, business lunches, social gatherings and special occasions. We also offer group dining menus and sushi platters to provide additional opportunities to service our customers. In general, our menu is consistent from location to location. We typically update our menu in the spring and the fall and make enhancements to existing items or introduce new items based on customer feedback, which helps ensure that we are meeting the needs of our customers.

Our restaurants also offer an extensive selection of domestic and imported bottled and draft beers, over 50 selections of wines by the glass or bottle, and an extensive selection of liquors and specialty cocktail drinks. During our weekday happy hour (3 p.m. to 7 p.m.), reverse happy hour (9 p.m. to 11 p.m.) and Sunday happy hour in select markets, we offer discounts on selected food and alcoholic beverage items. Happy hour times may vary by location due to local liquor laws. Alcoholic beverage sales represented approximately 30% of our total restaurant sales during 2014.

Decor and Atmosphere

We design our restaurants to offer our customers a unique dining experience in a setting that is relevant for today and tomorrow. Each of our restaurants is individually designed with a contemporary look that is adaptable to varying real estate opportunities while incorporating signature elements such as our saltwater aquarium, multiple dining areas and

open floor plan. Our customers can expect to find a warm and inviting atmosphere that aligns with our innovative food and drink offerings and high quality service. Our design incorporates exotic veneers, various tiles and textures, vertical beveled stone, raised fabric panels, and fire and water elements. The layout of our restaurants focuses on creating multiple dining areas for our customers while maintaining an open atmosphere that allows customers to have a panoramic view of the entire restaurant and exhibition kitchen and sushi bar. Each restaurant features varying water elements, including our signature aquarium with bright and colorful exotic fish, plants, and unique under water decor. We also utilize a variety of directional lighting styles and custom design elements to add warmth to all dining spaces throughout our restaurants.

Regardless of the experience customers are looking for, our restaurant design offers a variety of dining experiences to fit every mood and occasion. Our indoor/outdoor patio with a full service bar incorporates a high-energy, socially interactive atmosphere for customers to enjoy appetizers or sushi while they wait to dine with us, and serves as a destination for many of our frequent customers during the late afternoon and late night periods. Our restaurant in Fort Worth, Texas features a rooftop patio with a retractable roof. We also have enclosed patios in colder climates to maximize utilization of the patio throughout the year. Alternatively, our dining room provides a warm and intimate ambience for special occasions or dinner with friends and family. For sushi enthusiasts, we showcase our highly trained sushi chefs creating their masterpieces at our expansive sushi bar.

Food Preparation, Quality Control, and Purchasing

We believe that we have some of the highest food quality standards in the industry. Our standards are designed to protect food products throughout the preparation process. We provide detailed specifications to suppliers for food ingredients, products, and supplies. We strive to maintain quality and consistency in our restaurants through careful hiring, training and supervision of personnel. Our restaurant general managers and executive chefs generally receive nine weeks of training while our other restaurant managers and sous chefs receive seven weeks of training. We require annual recertification training for all employees, and each employee receives an operations manual relating to food and beverage preparation and restaurant operations. We also instruct kitchen managers and staff on safety, sanitation, housekeeping, repair and maintenance, product and service specifications, ordering and receiving products, and quality assurance. All of our restaurant managers are compliant with Hazard Analysis and Critical Control Point, or HACCP. We monitor minimum cook temperature requirements and conduct twice-a-day kitchen and food quality inspections to further assure the safety and quality of all of the items we use in our restaurants. We have a ServSafe alcohol certification program, where every front of house employee is trained and tested to ensure we are providing responsible alcohol service. Additionally, we engage a third party service provider to perform quarterly inspections at all of our restaurants to monitor and ensure compliance with required guidelines.

We are committed to purchasing high-quality ingredients for our restaurants at reasonable prices. We use only the freshest ingredients and, as a result, we maintain only modest inventories. We have arrangements with local produce distributors and specialty food suppliers who provide high-quality ingredients and perishable food products. We believe that competitively priced alternative distribution sources are available should those channels be necessary. We source all of our products and supplies with reputable and high-quality providers that are capable of providing consistent, reliable distribution to all of our restaurants.

Our goal is to maximize purchasing efficiencies and obtain the lowest possible prices for ingredients, products, and supplies, while maintaining the highest quality. Our corporate office coordinates national supply contracts, negotiates prices for food supply throughout all of our restaurants, monitors quality control and consistency of the food supplied to restaurants, and oversees delivery of food on a nationwide basis. In order to provide the freshest ingredients and products, and to maximize operating efficiencies between purchase and usage, we utilize an automated food cost and inventory system to assist each restaurant's management team in determining daily order requirements for food ingredients, products, and supplies. The management team orders accordingly from approved suppliers, and all deliveries are inspected to assure that the items received meet our quality specifications and negotiated prices.

Restaurant Operations

Executive and Restaurant Management

Our executive management team continually monitors restaurant operations to assure the quality of products and services and the maintenance of facilities. Restaurant management and our corporate office institute procedures to enhance efficiency, reduce costs and provide centralized and individual restaurant support systems. Our corporate operations team and district managers have primary responsibility for oversight of our restaurants and participate in analyzing restaurant-level performance and strategic planning. We currently employ five district managers who are each responsible for overseeing the restaurants in a specific region. The district managers' responsibilities include supporting the general managers and helping each general manager achieve the sales and cash flow targets for their restaurant as well as providing insight for decision making in such areas as food and beverage, people development, and systems to enhance the efficiency of operations and the dining experience for our customers. In addition, our corporate food and beverage team includes a vice president, a corporate chef, a corporate sushi chef, three regional culinary partners and an operations support manager who are responsible for educating, coaching, and developing kitchen personnel, implementing systems to improve the efficiency of kitchen operations, and developing new menu offerings.

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Our typical restaurant management team consists of a general manager, assistant general manager, two front-of-the-house managers, executive chef, sous chef, and head sushi chef. Our restaurants employ on average approximately 75 non-management employees, many of whom work part-time. The general manager is responsible for the day-to-day operations of the restaurant, including the hiring, training, personnel development, execution of local marketing programs, and operating results. The chefs are responsible for overseeing the preparation of menu and sushi items, maintaining product quality, and closely monitoring food costs and department labor costs. We also employ a kitchen staff member who is dedicated to the preparation of our signature sauces and dressings.

Training

In order to maintain quality and consistency in each of our restaurants, we carefully train and supervise restaurant personnel and adhere to high standards related to personnel performance, food and beverage preparation, and maintenance of our restaurants. All of our restaurant personnel participate in both initial and ongoing training programs under the direction of our director of training. Each restaurant manager completes a formal training program that is comprised of a mix of classroom and on-the-job instruction. Programs for general managers and executive chefs provide nine weeks of training. Programs for other managers provide seven weeks of training and may involve work in our other restaurants and cross training of various duties. The training covers all aspects of management philosophy and overall restaurant operations, including supervisory skills, operating and performance standards, accounting procedures, IT systems and employee selection and training necessary for top-quality restaurant operations. The training programs also involve intensive understanding and testing of our menu, learning the ingredients of various menu items, and other key service protocols. In addition, our hourly staff goes through a series of in-depth interactive training for their positions.

We implement these programs by hiring dedicated corporate personnel as well as designating high-performing existing restaurant personnel to assist in training. Our training personnel are involved in training for both new employees hired in anticipation of new restaurant openings as well as for ongoing training in existing restaurants. When we open a new restaurant, we provide training to restaurant personnel in every position for several weeks prior to and after the opening to assure the smooth and efficient operation of the restaurant from the first day it opens to the public.

Recruitment and Retention

Our future growth and success is highly dependent upon our ability to attract, develop, and retain qualified individuals who are capable of successfully managing our high-volume, upscale casual restaurants. We believe that our unit volume, the image and atmosphere of the Kona Grill concept, and career advancement and employee benefit programs enable us to attract high quality management and restaurant personnel. We offer restaurant management personnel competitive wages and benefits, including medical insurance and participation in our 401(k) plan with a company match. We motivate and prepare our restaurant personnel by providing them with opportunities for increased

responsibility and advancement through a formal management development program. Furthermore, the management team of each restaurant shares in a bonus tied to the sales and overall profitability of their restaurant. We believe that our compensation package for managers and restaurant employees is comparable to or better than those provided by other polished casual restaurants. We believe our compensation policies help us attract quality personnel.

Information Systems

We believe that our management information systems enable us to increase the speed and accuracy of order-taking and pricing, efficiently schedule labor to better serve customers, monitor labor costs, assist in product purchasing and menu mix management, promptly access financial and operating data, and improve the accuracy and efficiency of restaurant-level information and reporting.

We utilize an integrated information system to manage the flow of information within each of our restaurants and between each restaurant and our corporate office. This system includes a point-of-sale (POS) local area network that helps facilitate the operations of the restaurant by recording sales transactions and printing orders in the appropriate locations within the restaurant. Additionally, we utilize the POS system to authorize, batch, and transmit credit card transactions, record employee time clock information, and produce a variety of management reports. The POS is integrated with food cost and labor scheduling software as well as our financial reporting system and incorporates a redundancy and back-up emergency operating plan on a temporary basis if the system experiences downtime.

We transmit electronically select information that is captured from the POS system to our corporate office on a daily basis. This information flow enables senior management to monitor operating results with daily and weekly sales analysis, detailed labor and food cost information, and comparisons between actual and budgeted operating results. We anticipate continually updating both our restaurant information systems and corporate office information systems to enhance operations. We believe our information systems are secure and scalable as we continue to build our brand.

Advertising and Marketing

Our ongoing advertising and marketing strategy consists of loyalty programs, social media, grass-root local marketing, various public relations activities and word-of-mouth recommendations. We believe that these mediums are key components in driving customer trial and usage. We expect to continue to invest in marketing, branding and advertising efforts, primarily to introduce our concept in new markets and to increase comparable restaurant sales and solidify brand awareness in existing markets.