WINMARK CORP Form 10-Q April 25, 2012 Table of Contents

UNITED STATES

SECURITIES AND EXCHANGE COMMISSION

Washington, D.C. 20549

FORM 10-Q

x QUARTERLY REPORT PURSUANT TO SECTION 13 OR 15(D) OF THE SECURITIES EXCHANGE ACT OF 1934

For the quarterly period ended March 31, 2012

or

0 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: 000-22012

WINMARK CORPORATION

(Exact name of registrant as specified in its charter)

Minnesota

(State or other jurisdiction of incorporation or organization)

41-1622691 (I.R.S. Employer Identification No.)

605 Highway 169 North, Suite 400, Minneapolis, MN 55441

(Address of principal executive offices) (Zip Code)

(763) 520-8500

(Registrant s telephone number, including area code)

Indicate by check mark whether the 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 for 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 x No o

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 x No o

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.

Large accelerated filer o

Non-accelerated filer o (Do not check if a smaller reporting company)

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

Common stock, no par value, 5,075,954 shares outstanding as of April 18, 2012.

Accelerated filer o

Smaller reporting company x

WINMARK CORPORATION AND SUBSIDIARIES

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PART I. FINANCIAL INFORMATION

ITEM 1: Financial Statements

WINMARK CORPORATION AND SUBSIDIARIES

CONSOLIDATED CONDENSED BALANCE SHEETS

(Unaudited)

	M	arch 31, 2012	Dec	cember 31, 2011
	ASSETS			
Current Assets:				
Cash and cash equivalents	\$	2,093,400	\$	9,020,100
Marketable securities				1,043,800
Receivables, less allowance for doubtful accounts of \$16,700				
and \$15,100		1,282,400		1,316,200
Net investment in leases - current		11,465,300		11,746,900
Income tax receivable				116,500
Inventories		69,100		68,500
Prepaid expenses		437,400		362,000
Total current assets		15,347,600		23,674,000
Net investment in leases - long-term		18,096,700		18,102,000
Long-term investments, less allowance for losses of \$883,100				
and \$883,100		3,780,000		3,817,400
Property and equipment, net		1,384,000		1,474,800
Other assets		677,500		677,500
	\$	39,285,800	\$	47,745,700

	LIABILITIES AND SHAREHOLDE	RS EQUITY	
Current Liabilities:			
Line of credit	\$	12,100,000	\$
Accounts payable		1,269,800	1,460,300
Income tax payable		58,200	
Accrued liabilities		1,709,900	1,346,000
Discounted lease rentals		13,900	20,800
Rents received in advance		282,000	274,700
Deferred revenue		1,376,800	1,212,400
Deferred income taxes		3,487,900	3,464,800
Total current liabilities		20,298,500	7,779,000
Long-Term Liabilities:			
Rents received in advance		194,500	269,400
Deferred revenue		847,300	844,300
Other liabilities		1,314,200	1,389,200
Deferred income taxes		2,607,100	2,355,100
Total long-term liabilities		4,963,100	4,858,000
Shareholders Equity:			
Common stock, no par, 10,000,000 shares	authorized,		
5,075,954 and 4,987,643 shares issued and	outstanding	1,565,800	629,800

Accumulated other comprehensive income		17,000
Retained earnings	12,458,400	34,461,900
Total shareholders equity	14,024,200	35,108,700
	\$ 39,285,800	\$ 47,745,700

The accompanying notes are an integral part of these financial statements.

WINMARK CORPORATION AND SUBSIDIARIES

CONSOLIDATED CONDENSED STATEMENTS OF OPERATIONS

(Unaudited)

	Three Months Ended			
	March 31, 2012		March 26, 2011	
REVENUE:				
Royalties	\$ 8,288,500	\$	7,052,800	
Leasing income	2,392,100		3,235,000	
Merchandise sales	709,800		501,400	
Franchise fees	285,000		75,000	
Other	158,000		240,700	
Total revenue	11,833,400		11,104,900	
COST OF MERCHANDISE SOLD	664,300		482,900	
LEASING EXPENSE	239,800		518,700	
PROVISION FOR CREDIT LOSSES	(53,000)		45,400	
SELLING, GENERAL AND ADMINISTRATIVE EXPENSES	5,136,100		4,845,900	
Income from operations	5,846,200		5,212,000	
LOSS FROM EQUITY INVESTMENTS	(37,400)		(77,000)	
INTEREST EXPENSE	(69,800)		(31,100)	
INTEREST AND OTHER INCOME	46,300		17,200	
Income before income taxes	5,785,300		5,121,100	
PROVISION FOR INCOME TAXES	(2,269,300)		(2,094,800)	
NET INCOME	\$ 3,516,000	\$	3,026,300	
EARNINGS PER SHARE BASIC	\$.70	\$.61	
EARNINGS PER SHARE DILUTED	\$.67	\$.58	
WEIGHTED AVERAGE SHARES OUTSTANDING BASIC	5,052,952		4,989,588	
WEIGHTED AVERAGE SHARES OUTSTANDING DILUTED	5,280,202		5,215,484	

The accompanying notes are an integral part of these financial statements.

WINMARK CORPORATION AND SUBSIDIARIES

CONSOLIDATED CONDENSED STATEMENTS OF COMPREHENSIVE INCOME

(Unaudited)

	Three Months Ended				
	Μ	larch 31, 2012		March 26, 2011	
NET INCOME	\$	3,516,000	\$	3,026,300	
OTHER COMPREHENSIVE INCOME (LOSS), BEFORE TAX:					
Unrealized net gains on marketable securities:					
Reclassification adjustment for net gains included in net income		(28,000)			
OTHER COMPREHENSIVE INCOME (LOSS), BEFORE TAX		(28,000)			
INCOME TAX (EXPENSE) BENEFIT RELATED TO ITEMS OF OTHER					
COMPREHENSIVE INCOME:					
Unrealized net gains on marketable securities:					
Reclassification adjustment for net gains included in net income		11,000			
OTHER COMPREHENSIVE LOSS, NET OF TAX		(17,000)			
COMPREHENSIVE INCOME	\$	3,499,000	\$	3,026,300	

The accompanying notes are an integral part of these financial statements.

WINMARK CORPORATION AND SUBSIDIARIES

CONSOLIDATED CONDENSED STATEMENTS OF CASH FLOWS

(Unaudited)

March 31, 2012 March 26, 2011 OPERATIVITIES: S 3,516,000 \$ 3,026,300 Adjustments to reconcile net income to net cash provided by operating activities: 114,500 120,500 Provision for credit losses (63,000) 45,400 70,000 Compensation expense related to stock options 205,400 770,000 600 Defered income taxes 275,100 770,000 669,800 669,800 669,800 669,800 669,800 669,800 669,800 160,900 669,800 160,900 150,700 70,000 769,800 160,900 180,900 160,900 180,900 160,900 180,900 160,900 160,900 160,900 160,900 161,700 268,800 160,900 161,700 268,800 16,900,90 161,700 268,800 16,900,90 161,700 268,800 16,900,90 161,600,90 16,600,90 38,100 162,900 16,900,90 161,600,90 16,600,90 16,600,90 16,600,90 16,600,90 16,800,90 16,800,90 16,800,90 16,800,90		Three Months Ended		
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Accounts payable (190,500) 1,161,700 Accounts payable (190,500) 1,690,400 Rents received in advance and security deposits 107,600 76,200 Other assets 3,000 Deferred revenue 167,400 216,800 Net cash provided by operating activities 4,532,600 7,704,800 INVESTING ACTIVITIES: 700 (25,800) Purchase of marketable securities (265,800) 167,400 Purchase of quipment (23,700) (32,400) Purchase of equipment for lease contracts (4,338,000) (4,720,000) Principal collections on lease receivables 1,229,600 (186,300) FINANCING ACTIVITIES: 700 (23,000) (5,300,000) Proceeds from borrowings on line of credit 14,600,000 146,300 FINANCING ACTIVITIES: (2,499,300) (2,499,300) Proceeds from borrowings on line of credit 14,600,000 169,300 Repurchases of common stock (2,499,300) 69,800 Repurchases of common stock (2,499,300) 10/3,000 Proceeds from exercises of stock options 327,400 69,800 <tr< td=""><td>Inventories</td><td>(600)</td><td></td><td>38,100</td></tr<>	Inventories	(600)		38,100
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Rents received in advance and security deposits 107,600 76,200 Other assets 3,000 Deferred revenue 167,400 216,800 Net cash provided by operating activities 4,532,600 7,704,800 INVESTING ACTIVITIES: 1,311,600 160,400 Purchase of marketable securities (265,800) 100,400 Purchase of property and equipment (23,700) (32,400) Purchase of requipment for lease contracts (4,338,000) (4,720,000) Proceeds from sale of on investing activities 1,229,600 (186,300) FINANCING ACTIVITIES: 1 14,600,000 100,000 Proceeds from borrowings on line of credit (2,500,000) (5,300,000) 100,000 FINANCING ACTIVITIES: 1229,600 (186,300) 14,200,000 14,200,000 14,200,000 10,200,000 10,200,000 10,200,000 10,200,000 10,200,000 12,499,300 12,499,300 12,499,300 12,499,300 12,499,300 12,499,300 12,499,300 12,499,300 12,499,300 12,499,300 12,499,300 12,499,300 12,499,300<	Accounts payable	(190,500)		1,161,700
Other assets3,000Deferred revenue167,400216,800Net cash provided by operating activities4,532,6007,704,800INVESTING ACTIVITIES:1,311,600160,400Purchase of marketable securities(265,800)100,400Purchase of equipment for lease contracts(4,338,000)(4,720,000)Purchase of equipment for lease contracts(4,338,000)(4,720,000)Principal collections on lease receivables1,229,600(186,300)FINANCING ACTIVITIES:111Proceeds from borrowings on line of credit14,600,000163,000)Payments on line of credit14,600,0002,499,300)Proceeds from exercises of stock options403,200421,300Proceeds from exercises of stock options327,40069,800Net cash used for financing activities(12,688,900)(7,408,000)Net cash used for financing activities(12,688,900)110,500Cash and cash equivalents, beginning of period9,020,1002,257,100Net cash used for financing activities(2,257,100)110,500Cash and cash equivalents, end of period\$ 2,093,400\$ 2,367,600	Accrued and other liabilities	288,900		1,690,400
Deferred revenue 167,400 216,800 Net cash provided by operating activities 4,532,600 7,704,800 INVESTING ACTIVITIES:	Rents received in advance and security deposits	107,600		76,200
Net cash provided by operating activities4,532,6007,704,800INVESTING ACTIVITIES:1,311,600160,400Purchase of marketable securities(265,800)Purchase of property and equipment(23,700)(32,400)Purchase of equipment for lease contracts(4,338,000)(4,720,000)Purchase of equipment for lease contracts(4,338,000)(4,720,000)Principal collections on lease receivables4,545,5004,405,700Net cash provided by (used for) investing activities1,229,600(186,300)FINANCING ACTIVITIES:14,600,000249,300Proceeds from borrowings on line of credit14,600,000249,300Payments on line of credit(2,500,000)(5,300,000)Represent of common stock(24,99,300)249,300Proceeds from exercises of stock options327,40069,800Net cash used for financing activities(12,688,900)(7,408,000)Net cash used for financing activities(12,688,900)(7,408,000)Net cash used for financing activities9,020,1002,257,100Cash and cash equivalents, beginning of period9,020,1002,257,100Cash and cash equivalents, end of period\$ 2,093,400\$ 2,367,600	Other assets			3,000
INVESTING ACTIVITIES:Proceeds from sale of marketable securities1,311,600160,400Purchase of marketable securities(265,800)Purchase of property and equipment(23,700)(32,400)Purchase of equipment for lease contracts(4,338,000)(4,720,000)Principal collections on lease receivables4,545,5004,405,700Net cash provided by (used for) investing activities1,229,600(186,300)FINANCING ACTIVITIES:Proceeds from borrowings on line of credit14,600,000Payments on line of credit(2,500,000)(5,300,000)Repurchases of common stock(2,499,300)(2,499,300)Proceeds from exercises of stock options403,200421,300Dividends paid(25,519,500)(99,800)Tax benefits on exercised stock options327,40069,800Net cash used for financing activities(12,688,900)(7,408,000)Net cash used for financing activities(22,519,500)110,500Cash and cash equivalents, beginning of period9,020,1002,257,100Cash and cash equivalents, end of period\$2,093,400\$Start Cash activationsS2,093,400\$Proceeds from cash equivalents, end of period\$2,093,400\$Proceeds from exercised stock options9,020,1002,257,100Cash and cash equivalents, end of period\$2,093,400\$Proceeds from exercised stock options\$2,367,600	Deferred revenue	167,400		216,800
INVESTING ACTIVITIES:Proceeds from sale of marketable securities1,311,600160,400Purchase of marketable securities(265,800)Purchase of property and equipment(23,700)(32,400)Purchase of equipment for lease contracts(4,338,000)(4,720,000)Principal collections on lease receivables4,545,5004,405,700Net cash provided by (used for) investing activities1,229,600(186,300)FINANCING ACTIVITIES:Proceeds from borrowings on line of credit14,600,000Payments on line of credit(2,500,000)(5,300,000)Repurchases of common stock(2,499,300)(2,499,300)Proceeds from exercises of stock options403,200421,300Dividends paid(25,519,500)(99,800)Tax benefits on exercised stock options327,40069,800Net cash used for financing activities(12,688,900)(7,408,000)Net cash used for financing activities(22,519,500)110,500Cash and cash equivalents, beginning of period9,020,1002,257,100Cash and cash equivalents, end of period\$2,093,400\$Start Cash activationsS2,093,400\$Proceeds from cash equivalents, end of period\$2,093,400\$Proceeds from exercised stock options9,020,1002,257,100Cash and cash equivalents, end of period\$2,093,400\$Proceeds from exercised stock options\$2,367,600				
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Purchase of marketable securities(265,800)Purchase of property and equipment(23,700)(32,400)Purchase of equipment for lease contracts(4,338,000)(4,720,000)Principal collections on lease receivables4,545,5004,405,700Net cash provided by (used for) investing activities1,229,600(186,300)FINANCING ACTIVITIES:Proceeds from borrowings on line of credit14,600,000Payments on line of credit(2,500,000)(5,300,000)Repurchases of common stock(2,499,300)(25,300,000)Proceeds from exercises of stock options403,200421,300Dividends paid(25,519,500)(99,800)Tract cash used for financing activities(12,688,900)Net cash used for financing activities(12,688,900)(7,408,000)Net cash used for financing activities(12,688,900)(7,408,000)NET INCREASE (DECREASE) IN CASH AND CASH EQUIVALENTS(6,926,700)110,500Cash and cash equivalents, beginning of period9,020,1002,257,100Cash and cash equivalents, end of period\$2,093,400\$2,093,400\$	INVESTING ACTIVITIES:			
Purchase of property and equipment(23,700)(32,400)Purchase of equipment for lease contracts(4,338,000)(4,720,000)Principal collections on lease receivables4,545,5004,405,700Net cash provided by (used for) investing activities1,229,600(186,300)FINANCING ACTIVITIES:14,600,000Proceeds from borrowings on line of credit14,600,000Payments on line of credit(2,500,000)Repurchases of common stock(2,499,300)Proceeds from exercises of stock options403,200403,200421,300Dividends paid(25,519,500)Cash used for financing activities(12,688,900)Net cash used for financing activities(2,519,500)Net cash used for financing activities(12,688,900)Net cash used for financing activities(2,519,500)Net cash used for financing activities(2,257,100)Cash and cash equivalents, beginning of period9,020,1002,257,100\$Cash and cash equivalents, end of period\$2,093,400\$2,367,600	Proceeds from sale of marketable securities	1,311,600		160,400
Purchase of equipment for lease contracts(4,338,00)(4,720,000)Principal collections on lease receivables4,545,5004,405,700Net cash provided by (used for) investing activities1,229,600(186,300)FINANCING ACTIVITIES:14,600,0009Proceeds from borrowings on line of credit14,600,000Payments on line of credit(2,500,000)(5,300,000)Repurchases of common stock(2,499,300)Proceeds from exercises of stock options403,200421,300Dividends paid(25,519,500)(99,800)Tax benefits on exercised stock options327,40069,800Net cash used for financing activities(12,688,900)(7,408,000)NET INCREASE (DECREASE) IN CASH AND CASH EQUIVALENTS(6,926,700)110,500Cash and cash equivalents, beginning of period9,020,1002,257,100Cash and cash equivalents, end of period\$2,093,400\$Statement\$2,093,400\$2,367,600	Purchase of marketable securities	(265,800)		
Principal collections on lease receivables4,545,5004,405,700Net cash provided by (used for) investing activities1,229,600(186,300)FINANCING ACTIVITIES:Proceeds from borrowings on line of credit14,600,000Payments on line of credit(2,500,000)(5,300,000)Repurchases of common stock(2,499,300)Proceeds from exercises of stock options403,200421,300Dividends paid(25,519,500)(99,800)Tax benefits on exercised stock options327,40069,800Net cash used for financing activities(12,688,900)(7,408,000)NET INCREASE (DECREASE) IN CASH AND CASH EQUIVALENTS(6,926,700)110,500Cash and cash equivalents, beginning of period9,020,1002,257,100Cash and cash equivalents, end of period\$ 2,093,400\$ 2,367,600	Purchase of property and equipment	(23,700)		(32,400)
Net cash provided by (used for) investing activities1,229,600(186,300)FINANCING ACTIVITIES:14,600,000Proceeds from borrowings on line of credit14,600,000Payments on line of credit(2,500,000)Repurchases of common stock(2,499,300)Proceeds from exercises of stock options403,200Addaga and the exercise of stock options403,200Dividends paid(25,519,500)Tax benefits on exercised stock options327,400Net cash used for financing activities(12,688,900)Net cash used for financing activities(12,688,900)NET INCREASE (DECREASE) IN CASH AND CASH EQUIVALENTS(6,926,700)Cash and cash equivalents, beginning of period9,020,100Qash and cash equivalents, end of period\$2,093,400\$ <td>Purchase of equipment for lease contracts</td> <td>(4,338,000)</td> <td></td> <td>(4,720,000)</td>	Purchase of equipment for lease contracts	(4,338,000)		(4,720,000)
FINANCING ACTIVITIES:Proceeds from borrowings on line of credit14,600,000Payments on line of credit(2,500,000)Repurchases of common stock(2,499,300)Proceeds from exercises of stock options403,200Proceeds from exercises of stock options403,200Dividends paid(25,519,500)Tax benefits on exercised stock options327,400Net cash used for financing activities(12,688,900)NET INCREASE (DECREASE) IN CASH AND CASH EQUIVALENTS(6,926,700)Cash and cash equivalents, beginning of period9,020,100Cash and cash equivalents, end of period\$2,093,400\$	Principal collections on lease receivables	4,545,500		4,405,700
FINANCING ACTIVITIES:Proceeds from borrowings on line of credit14,600,000Payments on line of credit(2,500,000)Repurchases of common stock(2,499,300)Proceeds from exercises of stock options403,200Proceeds from exercises of stock options403,200Dividends paid(25,519,500)Tax benefits on exercised stock options327,400Net cash used for financing activities(12,688,900)NET INCREASE (DECREASE) IN CASH AND CASH EQUIVALENTS(6,926,700)Cash and cash equivalents, beginning of period9,020,100Cash and cash equivalents, end of period\$2,093,400\$				
Proceeds from borrowings on line of credit14,600,000Payments on line of credit(2,500,000)(5,300,000)Repurchases of common stock(2,499,300)Proceeds from exercises of stock options403,200421,300Dividends paid(25,519,500)(99,800)Tax benefits on exercised stock options327,40069,800Net cash used for financing activities(12,688,900)(7,408,000)NET INCREASE (DECREASE) IN CASH AND CASH EQUIVALENTS(6,926,700)110,500Cash and cash equivalents, beginning of period9,020,1002,257,100Cash and cash equivalents, end of period\$2,093,400\$\$2,367,600		1,229,600		(186,300)
Payments on line of credit (2,500,000) (5,300,000) Repurchases of common stock (2,499,300) Proceeds from exercises of stock options 403,200 421,300 Dividends paid (25,519,500) (99,800) Tax benefits on exercised stock options 327,400 69,800 Net cash used for financing activities Net cash used for financing activities (12,688,900) (7,408,000) NET INCREASE (DECREASE) IN CASH AND CASH EQUIVALENTS (6,926,700) 110,500 Cash and cash equivalents, beginning of period 9,020,100 2,257,100 Cash and cash equivalents, end of period \$ 2,093,400 \$ 2,367,600	FINANCING ACTIVITIES:			
Repurchases of common stock(2,499,300)Proceeds from exercises of stock options403,200421,300Dividends paid(25,519,500)(99,800)Tax benefits on exercised stock options327,40069,800Net cash used for financing activities(12,688,900)(7,408,000)NET INCREASE (DECREASE) IN CASH AND CASH EQUIVALENTS(6,926,700)110,500Cash and cash equivalents, beginning of period9,020,1002,257,100Cash and cash equivalents, end of period\$2,093,400\$\$2,093,400	Proceeds from borrowings on line of credit	14,600,000		
Proceeds from exercises of stock options403,200421,300Dividends paid(25,519,500)(99,800)Tax benefits on exercised stock options327,40069,800Net cash used for financing activities(12,688,900)(7,408,000)NET INCREASE (DECREASE) IN CASH AND CASH EQUIVALENTS(6,926,700)110,500Cash and cash equivalents, beginning of period9,020,1002,257,100Cash and cash equivalents, end of period\$2,093,400\$State of the state	Payments on line of credit	(2,500,000)		(5,300,000)
Dividends paid(25,519,500)(99,800)Tax benefits on exercised stock options327,40069,800Net cash used for financing activities(12,688,900)(7,408,000)NET INCREASE (DECREASE) IN CASH AND CASH EQUIVALENTS(6,926,700)110,500Cash and cash equivalents, beginning of period9,020,1002,257,100Cash and cash equivalents, end of period\$2,093,400\$State of the second seco	Repurchases of common stock			(2,499,300)
Tax benefits on exercised stock options327,40069,800Net cash used for financing activities(12,688,900)(7,408,000)NET INCREASE (DECREASE) IN CASH AND CASH EQUIVALENTS(6,926,700)110,500Cash and cash equivalents, beginning of period9,020,1002,257,100Cash and cash equivalents, end of period\$2,093,400\$\$2,093,400\$2,367,600	Proceeds from exercises of stock options	403,200		421,300
Net cash used for financing activities(12,688,900)(7,408,000)NET INCREASE (DECREASE) IN CASH AND CASH EQUIVALENTS(6,926,700)110,500Cash and cash equivalents, beginning of period9,020,1002,257,100Cash and cash equivalents, end of period\$2,093,400\$\$2,093,400\$2,367,600		(25,519,500)		(99,800)
NET INCREASE (DECREASE) IN CASH AND CASH EQUIVALENTS(6,926,700)110,500Cash and cash equivalents, beginning of period9,020,1002,257,100Cash and cash equivalents, end of period\$2,093,400\$	Tax benefits on exercised stock options	327,400		69,800
Cash and cash equivalents, beginning of period 9,020,100 2,257,100 Cash and cash equivalents, end of period \$ 2,093,400 \$ 2,367,600		(12,688,900)		(7,408,000)
Cash and cash equivalents, end of period\$2,093,400\$2,367,600		(6,926,700)		110,500
i juli i juli juli juli juli juli juli j	Cash and cash equivalents, beginning of period	9,020,100		2,257,100
SUPPLEMENTAL DISCLOSURES:	Cash and cash equivalents, end of period	\$ 2,093,400	\$	2,367,600
	SUPPLEMENTAL DISCLOSURES:			

Cash paid for interest	\$ 19,800	\$ 90,200
Cash paid for income taxes	\$ 1,481,100	\$ 1,348,200

The accompanying notes are an integral part of these financial statements.

WINMARK CORPORATION AND SUBSIDIARIES

NOTES TO CONSOLIDATED CONDENSED FINANCIAL STATEMENTS

1. Management s Interim Financial Statement Representation:

The accompanying consolidated condensed financial statements have been prepared by Winmark Corporation and subsidiaries (the Company), without audit, pursuant to the rules and regulations of the Securities and Exchange Commission. The Company has a 52/53 week year which ends on the last Saturday in December. The information in the consolidated condensed financial statements includes normal recurring adjustments and reflects all adjustments which are, in the opinion of management, necessary for a fair presentation of such financial statements. The consolidated condensed financial statements and notes are presented in accordance with accounting principles generally accepted in the United States of America for interim financial information and with the instructions for Form 10-Q, and therefore do not contain certain information included in the Company s annual consolidated financial statements and notes. This report should be read in conjunction with the audited consolidated financial statements and the notes thereto included in the Company s latest Annual Report on Form 10-K.

Revenues and operating results for the three months ended March 31, 2012 are not necessarily indicative of the results to be expected for the full year.

Reclassifications

Certain reclassifications of previously reported amounts have been made to conform to the current year presentation. Such reclassifications did not impact net income or shareholders equity as previously reported.

2. Organization and Business:

The Company offers licenses to operate franchises using the service marks Plato s Closet®, Play It Again Sports®, Once Upon A Child® and Music Go Round®. The Company also operates both middle market and small-ticket equipment leasing businesses under the Winmark Capital® and Wirth Business Credit® marks.

3. Fair Value Measurements

The Company defines fair value as the price that would be received for an asset or paid to transfer a liability (an exit price) in the principal or most advantageous market for the asset or liability in an orderly transaction between market participants on the measurement date. The Company uses three levels of inputs to measure fair value:

• Level 1 quoted prices in active markets for identical assets and liabilities.

• Level 2 observable inputs other than quoted prices in active markets for identical assets and liabilities.

• Level 3 unobservable inputs in which there is little or no market data available, which require the reporting entity to develop its own assumptions.

The Company s marketable securities were valued based on Level 1 inputs using quoted prices.

Due to their nature, the carrying value of cash equivalents, receivables, payables and debt obligations approximates fair value.

4. Investments:

Marketable Securities

The following is a summary of marketable securities classified as available-for-sale securities:



The Company s unrealized gains and losses for marketable securities classified as available-for-sale securities in accumulated other comprehensive income are as follows:

	March 31, 2012	Dec	ember 31, 2011
Unrealized gains	\$	\$	32,900
Unrealized losses			(4,900)
Net unrealized gains/(losses)	\$	\$	28,000

The Company s realized gains and losses recognized on sales of available-for-sale marketable securities are as follows:

	Three Months Ended			
	Mai	rch 31, 2012	Μ	arch 26, 2011
Realized gains	\$	42,300	\$	
Realized losses		(12,300)		(600)
Net realized gains/(losses)	\$	30,000	\$	(600)

Amounts reclassified out of accumulated other comprehensive income into earnings is determined by using the average cost of the security when sold.

Long-Term Investments

The Company has an investment in Tomsten, Inc. (Tomsten), the parent company of Archiver's retail chain. The Company has invested a total of \$8.5 million in the purchase of common stock of Tomsten. The Company's investment currently represents 22.0% of the outstanding common stock of Tomsten. As of March 31, 2012, \$0.3 million of the Company's investment, with a current carrying value of \$2.5 million, is attributable to goodwill. The amount of goodwill was determined by calculating the difference between the Company's net investment in Tomsten less its pro rata share of Tomsten's net worth.

The Company has a \$2.0 million investment in senior subordinated promissory notes with warrants in BridgeFunds Limited (BridgeFunds). BridgeFunds advances funds to claimants involved in civil litigation to cover litigation expenses. Monthly prepayment of the principal of such notes in an amount equal to Available Cash Flow (as defined within the agreements governing the notes) is required, and the maturity date of the notes is June 30, 2012. During the three months ended March 31, 2012, the Company did not receive any payments of principal or interest on the notes. The Company stopped accruing interest on this investment as of September 30, 2010. The Company has deemed this investment to be impaired, and in evaluating the investment for impairment has determined that its present value of expected future cash flows, discounted at the effective interest rate on the notes of 15%, is less than the recorded investment in the notes. In developing its estimate of expected future cash flows, the Company used certain information obtained from BridgeFunds concerning existing liabilities, claimant cases outstanding and historical default rates on claimant advances, and made certain assumptions regarding the timing of case settlements, the payment of future liabilities and future default rates. The Company

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recognized \$883,100 in impairment charges during 2011 and established a corresponding valuation allowance accordingly. Based upon the Company s estimate of expected future cash flows as of March 31, 2012, there were no additional impairment charges during the three month period then ended. As of March 31, 2012, the \$1.3 million net investment balance inclusive of \$0.2 million of related interest receivable is classified as long-term based on expected payments from Available Cash Flow.

5.

Investment in Leasing Operations:

Investment in leasing operations consists of the following:

	Marc	h 31, 2012	l	December 31, 2011
Direct financing and sales-type leases:				
Minimum lease payments receivable	\$	27,040,200	\$	27,413,300
Estimated residual value of equipment		2,992,700		2,764,400
Unearned lease income net of initial direct costs deferred		(4,198,600)		(4,217,000)
Security deposits		(2,624,000)		(2,448,800)
Equipment installed on leases not yet commenced		6,476,800		6,489,200
Total investment in direct financing and sales-type leases		29,687,100		30,001,100
Allowance for credit losses		(759,200)		(803,800)
Net investment in direct financing and sales-type leases		28,927,900		29,197,300
Operating leases:				
Operating lease assets		1,302,500		1,218,900
Less accumulated depreciation and amortization		(668,400)		(567,300)
Net investment in operating leases		634,100		651,600
Total net investment in leasing operations	\$	29,562,000	\$	29,848,900

As of March 31, 2012, the \$29.6 million total net investment in leases consists of \$11.5 million classified as current and \$18.1 million classified as long-term. As of December 31, 2011, the \$29.8 million total net investment in leases consists of \$11.7 million classified as current and \$18.1 million classified as long-term.

As of March 31, 2012, leased assets with one customer approximated 13% of the Company s total assets.

Future minimum lease payments receivable under lease contracts and the amortization of unearned lease income, net of initial direct costs deferred, is as follows for the remainder of fiscal 2012 and the full fiscal years thereafter as of March 31, 2012:

	Di	Direct Financing and Sales-Type Leases				erating Leases
	Mini	Minimum Lease		Income		inimum Lease
	Paymer	Payments Receivable		Amortization	Payments Receivabl	
2012	\$	11,200,300	\$	2,343,800	\$	1,055,600
2013		9,312,400		1,402,400		1,517,800

2014 2015	4,776,900 1,251,700	366,900 79,300	132,400
2015	498,900	6,200	
Thereafter			
	\$ 27,040,200	\$ 4,198,600	\$ 2,705,800

The activity in the allowance for credit losses for leasing operations during the first three months of 2012 and 2011, respectively, is as follows:

	March 31, 2012			March 26, 2011		
Balance at beginning of period	\$	803,800	\$	907,800		
Provisions charged to expense		(53,000)		45,400		
Recoveries		34,100		25,100		
Deductions for amounts written-off		(25,700)		(117,800)		
Balance at end of period	\$	759,200	\$	860,500		

The Company s investment in direct financing and sales-type leases (Investment In Leases) and allowance for credit losses by loss evaluation methodology are as follows:

		March 31, 2012				December 31, 2011			
	Investment In Leases			lowance for		Investment	Allowance for Credit Losses		
			Cı	redit Losses		In Leases			
Collectively evaluated for loss potential	\$	29,687,100	\$	759,200	\$	30,001,100	\$	803,800	
Individually evaluated for loss potential									
Total	\$	29,687,100	\$	759,200	\$	30,001,100	\$	803,800	

The Company s key credit quality indicator for its investment in direct financing and sales-type leases is the status of the lease, defined as accruing or non-accruing. Leases that are accruing income are considered to have a lower risk of loss. Non-accrual leases are those that the Company believes have a higher risk of loss. The following table sets forth information regarding the Company s accruing and non-accrual leases. Delinquent balances are determined based on the contractual terms of the lease.

	1	0-60 Days Delinquent nd Accruing	61-90 Days Delinquent and Accruing	March 31, 2012 Over 90 Days Delinquent and Accruing	Noi	n-Accrual	Total
Middle-Market	\$	26,835,700	\$	\$	\$	94,300	\$ 26,930,000
Small-Ticket		2,757,100					2,757,100
Total Investment in Leases	\$	29,592,800	\$	\$	\$	94,300	\$ 29,687,100

December 31, 2011