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GRILL CONCEPTS INC
Form 10-Q
August 10, 2005

SECURITIES AND EXCHANGE COMMISSION
Washington, D.C. 20549

FORM 10-Q

(Mark One)

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

For the quarterly period ended June 26, 2005

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 No. 0-23226

GRILL CONCEPTS, INC.

(Exact name of registrant as specified in its charter)

| | |
|--|---|
| Delaware ----- (State or other jurisdiction of incorporation or organization) | 13-3319172 ----- (IRS Employer Identification No.) |
|--|---|

11661 San Vicente Blvd., Suite 404, Los Angeles, California 90049

(Address of principal executive offices) (Zip code)

(310) 820-5559

(Registrant's telephone number, including area code)

(Former name, former address and former fiscal year, if changed since last
report)

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 No

Indicate by check mark whether the registrant is an accelerated filer (as
defined in Rule 12b-2 of the Exchange Act). Yes No

As of August 10, 2005, 5,660,546 shares of Common Stock of the issuer were
outstanding.

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GRILL CONCEPTS, INC.

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PART I - FINANCIAL INFORMATION

ITEM 1. FINANCIAL STATEMENTS

GRILL CONCEPTS, INC. AND SUBSIDIARIES
CONDENSED CONSOLIDATED BALANCE SHEETS

(UNAUDITED)
ASSETS

June 26, December 26,
2005 2004

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| | | |
|---|--------------|--------------|
| Current assets: | | |
| Cash and cash equivalents | \$ 1,537,000 | \$ 1,407,000 |
| Inventories | 675,000 | 620,000 |
| Receivables, net of reserve (\$182,000 in 2005 and \$143,000 in 2004) | 860,000 | 836,000 |
| Reimbursement receivables from managed outlets | 806,000 | 928,000 |
| Prepaid expenses | 675,000 | 2,372,000 |
| | ----- | ----- |
| Total current assets | 4,553,000 | 6,163,000 |
| Furniture, equipment, & improvements, net | 14,179,000 | 11,864,000 |
| Goodwill, net | 205,000 | 205,000 |
| Restricted cash | 1,042,000 | 882,000 |
| Note receivable | 88,000 | 101,000 |
| Liquor licenses | 411,000 | 350,000 |
| Other assets | 178,000 | 184,000 |
| | ----- | ----- |
| Total assets | \$20,656,000 | \$19,749,000 |
| | ===== | ===== |

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

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GRILL CONCEPTS, INC. AND SUBSIDIARIES
CONDENSED CONSOLIDATED BALANCE SHEETS
(UNAUDITED)
(Continued)

LIABILITIES, MINORITY INTEREST AND STOCKHOLDERS' EQUITY

| | June 26, 2005 | December 26, 2004 |
|---|------------------|----------------------|
| | ----- | ----- |
| Current liabilities: | | |
| Accounts payable | \$ 1,659,000 | \$ 1,988,000 |
| Accrued expenses | 2,983,000 | 2,548,000 |
| Accrued managed outlet operating expenses | 806,000 | 928,000 |
| Current portion of long term debt | 111,000 | 196,000 |
| Current portion notes payable - related parties | 303,000 | 294,000 |
| | ----- | ----- |
| Total current liabilities | 5,862,000 | 5,954,000 |
| Long-term debt | 227,000 | 148,000 |
| Notes payable - related parties | 752,000 | 829,000 |
| Other long-term liabilities | 7,725,000 | 8,054,000 |
| | ----- | ----- |
| Total liabilities | 14,566,000 | 14,985,000 |
| Minority interest | 1,429,000 | 934,000 |

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Stockholders' equity:

| | | |
|---|---------------|--------------|
| Series I, Convertible Preferred Stock, \$.001 par value; 1,000,000 shares authorized, none issued and outstanding in 2005 and 2004 | - | - |
| Series II, 10% Convertible Preferred Stock, \$.001 par value; 1,000,000 shares, authorized, 500 shares issued and outstanding in 2005 and 2004 | - | - |
| Common stock, \$.00004 par value; 12,000,000 shares authorized in 2005 and 2004, 5,660,546 shares issued and outstanding in 2005, 5,650,146 shares issued and outstanding in 2004 | - | - |
| Additional paid-in capital | 13,673,000 | 13,649,000 |
| Accumulated deficit | (9,012,000) | (9,819,000) |
| | ----- | ----- |
| Total stockholders' equity | 4,661,000 | 3,830,000 |
| | ----- | ----- |
| Total liabilities, minority interest and stockholders' equity | \$ 20,656,000 | \$19,749,000 |
| | ===== | ===== |

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

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GRILL CONCEPTS, INC. AND SUBSIDIARIES
CONDENSED CONSOLIDATED STATEMENTS OF OPERATIONS
(Unaudited)

| | Three Months Ended | | Six Months |
|---|--------------------|---------------|---------------|
| | June 26, 2005 | June 27, 2004 | June 26, 2005 |
| | ----- | ----- | ----- |
| Revenues: | | (restated) | |
| Sales | \$13,417,000 | \$12,181,000 | \$26,804,000 |
| Cost reimbursements | 5,085,000 | 2,903,000 | 8,554,000 |
| Management and license fees | 369,000 | 306,000 | 725,000 |
| | ----- | ----- | ----- |
| Total revenues | 18,871,000 | 15,390,000 | 36,083,000 |
| | ----- | ----- | ----- |
| Operating expenses: | | | |
| Cost of sales | 3,814,000 | 3,607,000 | 7,552,000 |
| Restaurant operating expenses | 8,047,000 | 7,627,000 | 15,748,000 |
| Reimbursed costs | 5,085,000 | 2,903,000 | 8,554,000 |
| General and administrative | 1,224,000 | 1,041,000 | 2,270,000 |
| Depreciation and amortization | 482,000 | 485,000 | 943,000 |
| Pre-opening costs | 153,000 | 1,000 | 244,000 |
| | ----- | ----- | ----- |
| Total operating expenses | 18,805,000 | 15,664,000 | 35,311,000 |
| | ----- | ----- | ----- |
| Income (loss) from operations | 66,000 | (274,000) | 772,000 |
| Interest expense, net | (43,000) | (66,000) | (80,000) |
| | ----- | ----- | ----- |
| Income (loss) before provision for income taxes and minority interest | 23,000 | (340,000) | 692,000 |

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| | | | |
|---|------------|--------------|------------|
| Provision for income taxes | (131,000) | (5,000) | (209,000) |
| Minority interest in loss of subsidiaries | 233,000 | 214,000 | 324,000 |
| | ----- | ----- | ----- |
| Net income (loss) | 125,000 | (131,000) | 807,000 |
| Preferred dividends accrued | (12,000) | (12,000) | (25,000) |
| | ----- | ----- | ----- |
| Net income (loss) applicable to common stock | \$ 113,000 | \$ (143,000) | \$ 782,000 |
| | ===== | ===== | ===== |
| Net income (loss) per share applicable to common stock: | | | |
| Basic net income (loss) | \$ 0.02 | \$ (0.03) | \$ 0.14 |
| | ===== | ===== | ===== |
| Diluted net income (loss) | \$ 0.02 | \$ (0.03) | \$ 0.13 |
| | ===== | ===== | ===== |
| Weighted average shares outstanding: | | | |
| Basic | 5,652,230 | 5,590,445 | 5,651,188 |
| | ===== | ===== | ===== |
| Diluted | 6,064,781 | 5,590,445 | 6,018,508 |
| | ===== | ===== | ===== |

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

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GRILL CONCEPTS, INC. AND SUBSIDIARIES
CONDENSED CONSOLIDATED STATEMENTS OF CASH FLOWS
(Unaudited)

| | Six Months Ended | |
|---|------------------|------------------|
| | June 26, 2005 | June 27, 2004 |
| | ----- | ----- |
| Cash flows from operating activities: | | (restated) |
| Net income (loss) | \$ 807,000 | \$ (14,000) |
| Adjustments to reconcile net income to net cash provided by operating activities: | | |
| Depreciation and amortization | 943,000 | 964,000 |
| Stock based compensation expense | - | 71,000 |
| Allowance for doubtful accounts | 39,000 | 6,000 |
| Amortized deferred rent and lease incentives | (329,000) | (174,000) |
| Gain on sale of assets | - | (1,000) |
| Minority interest in loss of subsidiaries | (324,000) | (361,000) |
| Changes in operating assets and liabilities: | | |
| Inventories | (55,000) | (1,000) |
| Receivables | (63,000) | 45,000 |
| Reimbursable costs receivable | 122,000 | 41,000 |
| Prepaid expenses and other current assets | (75,000) | (151,000) |

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| | | |
|---|--------------|--------------|
| Tenant improvement allowances | 1,772,000 | 1,002,000 |
| Other assets | (4,000) | 28,000 |
| Accounts payable | (329,000) | 736,000 |
| Accrued expenses | 419,000 | (181,000) |
| Reimbursable costs payable | (122,000) | (41,000) |
| | ----- | ----- |
| Net cash provided by operating activities | 2,801,000 | 1,969,000 |
| | ----- | ----- |
| Cash flows from investing activities: | | |
| Proceeds from disposal of assets | - | 1,000 |
| Restricted cash | (160,000) | - |
| Purchase of liquor license | (61,000) | (5,000) |
| Purchase of furniture, equipment and improvements | (3,248,000) | (1,431,000) |
| | ----- | ----- |
| Net cash used in investing activities | (3,469,000) | (1,435,000) |
| | ----- | ----- |
| Cash flows from financing activities: | | |
| Proceeds from minority interest in LLC | 976,000 | 35,000 |
| Return of capital and profits to minority shareholder | (143,000) | (135,000) |
| Collections on note receivable | 15,000 | - |
| Proceeds from equipment financing | 118,000 | - |
| Proceeds from exercise of stock options | 24,000 | - |
| Payments to related parties | (68,000) | (116,000) |
| Payments on long-term debt | (124,000) | (182,000) |
| | ----- | ----- |
| Net cash provided by (used in) financing activities | 798,000 | (398,000) |
| | ----- | ----- |
| Net increase in cash and cash equivalents | 130,000 | 136,000 |
| Cash and cash equivalents, beginning of period | 1,407,000 | 1,496,000 |
| | ----- | ----- |
| Cash and cash equivalents, end of period | \$ 1,537,000 | \$ 1,632,000 |
| | ===== | ===== |
| Supplemental cash flow information: | | |
| Cash paid during the period for: | | |
| Interest | \$ 81,000 | \$ 100,000 |
| Income taxes | 129,000 | 93,000 |

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

GRILL CONCEPTS, INC. AND SUBSIDIARIES
NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS
(Unaudited)

1. INTERIM FINANCIAL PRESENTATION

The interim condensed consolidated financial statements are prepared pursuant to the requirements for reporting on Form 10-Q. These financial statements have not been audited by our independent registered public accounting firm. The December 26, 2004 balance sheet data was derived from audited financial statements but does not include all disclosures required by generally accepted accounting principles. The interim financial statements and notes thereto should be read in conjunction with the financial statements and notes included in the Company's Form 10-K for the year ended December 26, 2004. In the opinion of management,

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these interim financial statements reflect all adjustments of a normal recurring nature necessary for a fair presentation of the results for the interim periods presented. The current period results of operations are not necessarily indicative of results, which ultimately will be reported for the full year ending December 25, 2005.

2004 RESTATEMENT OF FINANCIAL STATEMENTS

The Company began a review of its lease accounting policies following announcements in February 2005 that the Chief Accountant of the Securities and Exchange Commission ("SEC") issued a letter to the American Institute of Certified Public Accountants expressing the SEC staff's views relating to certain lease accounting issues. As a result of this review, the Company revised its accounting for leases in 2004 and restated its historical financial statements as of June 27, 2004 to correct for these errors in its lease accounting.

Historically, the Company recognized straight-line rents and amortized tenant improvement allowances using the initial non-cancelable term of the lease commencing on the date rent payments began. Under generally accepted accounting principles, as highlighted in the SEC guidance, the Company should have recognized rent expense (net of the related tenant improvement allowance amortization) on a straight-line basis over the initial non-cancelable term of the lease, beginning on the later of when the Company had access to the site or the lease was executed. The impact of correctly calculating rent expense was to decrease restaurant operating expenses and decrease general and administrative expenses by \$2,000 and \$1,000, respectively, for the three months and by \$4,000 and \$2,000 for the six months ended June 27, 2004.

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In closing the 2004 books and records, the Company reviewed the estimated useful lives that it was using to amortize its leasehold improvements. In the case of six restaurants, it was found that the incorrect lives had been used. The Company has revised the amortization period to reflect the shorter of their estimated useful lives or the initial lease term. The impact of the change is to increase depreciation and amortization expense by \$30,000 and \$61,000 for the three and six months ended June 27, 2004.

A portion of the above adjustments was recorded on the books of the LLC's in which we have a majority ownership or we consolidate under FIN 46. As discussed in the footnotes to Form 10K dated December 26, 2004, the Company allocates results to the minority interests based on the underlying economics of the investment. The impact of the above adjustments increased the amount of loss allocated to the minority interests by \$48,000 and \$95,000, respectively for the three and six months ended June 27, 2004.

During fourth quarter of 2004, the Company eliminated amounts that had previously been recorded as restaurant sales revenue arising from complimentary meals and promotional activities. The Company's previous method of recording these activities as restaurant sales revenue with a corresponding increase in operating expense is not in accordance with generally accepted accounting principles. Historically the amounts associated with complimentary meals and promotional activities have been recorded as restaurant revenues, with an offsetting amount in restaurant operations and corporate general and administrative expenses. As revised, the Company has eliminated all amounts for complimentary meals and promotional activities. As a result of these adjustments, revenues were decreased by \$465,000 in the second quarter 2004, restaurant operating expenses decreased by \$424,000 and general and administrative expenses decreased by \$41,000. The adjustments for the full six month period ended June 27, 2004 was a decrease in revenues of \$962,000, a

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decrease in restaurant operating expenses of \$875,000 and a decrease in general and administrative expenses of \$87,000. These adjustments have no impact on previously reported income and are non-cash.

The effects of our revisions to previously reported Consolidated Financial Statements as of and for the quarter ended June 27, 2004 are summarized as follows.

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The following table reflects the effects of the restatement on the Consolidated Statement of Operations:

| | JUNE 27, 2004 | | | |
|--|---------------------------|------------|---------------------------|------------|
| | THREE MONTHS | | SIX MONTHS | |
| | AS PREVIOUSLY REPORTED | RESTATED | AS PREVIOUSLY REPORTED | RESTATED |
| Sales | 12,646,000 | 12,181,000 | 26,156,000 | 25,194,000 |
| Total Revenue | 15,855,000 | 15,390,000 | 32,851,000 | 31,889,000 |
| Restaurant operating expenses | 8,054,000 | 7,628,000 | 16,179,000 | 15,300,000 |
| General & administrative | 1,083,000 | 1,041,000 | 2,310,000 | 2,221,000 |
| Depreciation & amortization | 454,000 | 485,000 | 903,000 | 964,000 |
| Total operating expenses | 12,494,000 (1) | 15,664,000 | 25,632,000 | 32,104,000 |
| Loss from operations | (246,000) | (274,000) | (160,000) | (215,000) |
| Loss before taxes | (312,000) | (340,000) | (292,000) | (347,000) |
| Loss before minority interest | (317,000) | (345,000) | (320,000) | (375,000) |
| Minority interest | 166,000 | 214,000 | 266,000 | 361,000 |
| Net loss | (151,000) | (131,000) | (54,000) | (14,000) |
| Net loss applicable to common stock | (163,000) | (143,000) | (79,000) | (39,000) |
| Net loss per share applicable to common stock: | | | | |
| Basic | (\$0.03) | (\$0.03) | (\$0.01) | (\$0.01) |
| Diluted | (\$0.03) | (\$0.03) | (\$0.01) | (\$0.01) |