

DENNYS CORP
Form 10-Q
November 03, 2010

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

FORM 10-Q

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

For the Quarterly Period Ended September 29, 2010

Commission File Number 0-18051
DENNY'S CORPORATION
(Exact name of registrant as specified in its charter)

Delaware
(State or other jurisdiction of
incorporation or organization)

13-3487402
(I.R.S. Employer
Identification No.)

203 East Main Street
Spartanburg, South Carolina 29319-0001
(Address of principal executive offices)
(Zip Code)

(864) 597-8000
(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 No

Indicate by check mark whether the registrant has submitted electronically and posted on its corporate Web site, if any, every Interactive Data File required to be submitted and posted pursuant to Rule 405 of Regulation S-T during the preceding 12 months (or for such shorter period that the registrant was required to submit and post such files).

Yes No

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

Large accelerated filer Accelerated filer Non-accelerated filer Smaller reporting company

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(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 No

As of October 28, 2010, 99,697,084 shares of the registrant's common stock, par value \$.01 per share, were outstanding.

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PART I - FINANCIAL INFORMATION

Item 1. Financial Statements

Denny's Corporation and Subsidiaries
Condensed Consolidated Statements of Operations
(Unaudited)

	Quarter Ended		Three Quarters Ended	
	September 29, 2010	September 30, 2009	September 29, 2010	September 30, 2009
	(In thousands, except per share amounts)			
Revenue:				
Company restaurant sales	\$ 107,171	\$ 116,579	\$ 320,255	\$ 377,655
Franchise and license revenue	32,761	29,485	92,326	89,982
Total operating revenue	139,932	146,064	412,581	467,637
Costs of company restaurant sales:				
Product costs	25,405	26,924	75,597	88,513
Payroll and benefits	41,533	44,712	129,072	154,623
Occupancy	7,097	7,808	21,406	24,908
Other operating expenses	17,158	18,147	49,016	56,739
Total costs of company restaurant sales	91,193	97,591	275,091	324,783
Costs of franchise and license revenue	12,009	10,308	35,498	32,295
General and administrative expenses	14,375	14,313	40,560	44,067
Depreciation and amortization	7,320	7,865	21,984	24,592
Operating (gains), losses and other charges, net	(1,900)	(2,648)	(1,594)	(6,101)
Total operating costs and expenses	122,997	127,429	371,539	419,636
Operating income	16,935	18,635	41,042	48,001
Other expenses:				
Interest expense, net	6,394	8,117	19,306	24,847
Other nonoperating expense (income), net	188	(363)	746	(1,594)
Total other expenses, net	6,582	7,754	20,052	23,253
Net income before income taxes	10,353	10,881	20,990	24,748
Provision for income taxes	419	848	1,010	1,072
Net income	\$ 9,934	\$ 10,033	\$ 19,980	\$ 23,676
Net income per share:				
Basic	\$ 0.10	\$ 0.10	\$ 0.20	\$ 0.25
Diluted	\$ 0.10	\$ 0.10	\$ 0.20	\$ 0.24

Weighted average shares
outstanding:

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Basic	99,579	96,506	98,646	96,221
Diluted	101,305	99,158	101,264	98,295

See accompanying notes

Denny's Corporation and Subsidiaries
Condensed Consolidated Balance Sheets
(Unaudited)

	September 29, 2010	December 30, 2009
(In thousands)		
Assets		
Current assets:		
Cash and cash equivalents	\$ 40,638	\$ 26,525
Receivables, less allowance for doubtful accounts of \$177 and \$171, respectively	13,718	18,106
Inventories	3,743	4,165
Assets held for sale	6,541	—
Prepaid and other current assets	11,260	9,549
Total current assets	75,900	58,345
Property, net of accumulated depreciation of \$247,975 and \$258,695, respectively	118,090	131,484
Other assets:		
Goodwill	31,892	32,440
Intangible assets, net	52,888	55,110
Deferred financing costs, net	2,773	2,676
Other noncurrent assets	31,135	32,572
Total assets	\$ 312,678	\$ 312,627
Liabilities and shareholders' deficit		
Current liabilities:		
Current maturities of notes and debentures	\$ 754	\$ 900
Current maturities of capital lease obligations	3,899	3,725
Accounts payable	19,248	22,842
Other current liabilities	62,738	64,641
Total current liabilities	86,639	92,108
Long-term liabilities:		
Notes and debentures, less current maturities	239,446	254,357
Capital lease obligations, less current maturities	18,960	19,684
Liability for insurance claims, less current portion	19,082	21,687
Deferred income taxes	13,121	13,016
Other noncurrent liabilities and deferred credits	37,854	39,273
Total long-term liabilities	328,463	348,017
Total liabilities	415,102	440,125
Commitments and contingencies		
Shareholders' deficit:		
Common stock \$0.01 par value; authorized - 135,000; issued - 99,627 and 96,613, respectively	996	966

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Paid-in capital	547,473	542,576
Deficit	(632,847)	(652,827)
Accumulated other comprehensive loss, net of tax	(18,046)	(18,213)
Total shareholders' deficit	(102,424)	(127,498)
Total liabilities and shareholders' deficit	\$ 312,678	\$ 312,627

See accompanying notes

Denny's Corporation and Subsidiaries
Condensed Consolidated Statement of Shareholders' Deficit and Comprehensive Income
(Unaudited)

	Common Stock		Paid-in	Deficit	Accumulated	Total
	Shares	Amount	Capital		Other	Shareholders'
					Comprehensive	Deficit
	(In thousands)					
Balance, December 30, 2009	96,613	\$ 966	\$ 542,576	\$ (652,827)	\$ (18,213)	\$ (127,498)
Comprehensive income:						
Net income	—	—	—	19,980	—	19,980
Amortization of unrealized loss on hedged transactions, net of tax	—	—	—	—	167	167
Comprehensive income	—	—	—	19,980	167	20,147
Share-based compensation on equity classified awards	—	—	1,588	—	—	1,588
Issuance of common stock for share-based compensation	459	4	(4)	—	—	—
Exercise of common stock options	2,555	26	3,313	—	—	3,339
Balance, September 29, 2010	99,627	\$ 996	\$ 547,473	\$ (632,847)	\$ (18,046)	\$ (102,424)

See accompanying notes

Denny's Corporation and Subsidiaries
Condensed Consolidated Statements of Cash Flows
(Unaudited)

	Three Quarters Ended	
	September 29, 2010	September 30, 2009
	(In thousands)	
Cash flows from operating activities:		
Net income	\$ 19,980	\$ 23,676
Adjustments to reconcile net income to cash flows provided by operating activities:		
Depreciation and amortization	21,984	24,592
Operating (gains), losses and other charges, net	(1,594)	(6,101)
Amortization of deferred financing costs	771	811
Loss on early extinguishment of debt	221	40
(Gain) loss on interest rate swap	167	(1,486)
Deferred income tax expense	105	650
Share-based compensation	2,010	3,899
Changes in assets and liabilities, net of effects of acquisitions and dispositions:		
Decrease (increase) in assets:		
Receivables	1,704	3,313
Inventories	422	1,314
Other current assets	(1,716)	(4,691)
Other assets	(2,117)	(2,175)
Increase (decrease) in liabilities:		
Accounts payable	(977)	(2,949)
Accrued salaries and vacations	(5,600)	(3,009)
Accrued taxes	1,932	1,105
Other accrued liabilities	(1,496)	(7,107)
Other noncurrent liabilities and deferred credits	(4,203)	(4,482)
Net cash flows provided by operating activities	31,593	27,400
Cash flows from investing activities:		
Purchase of property	(13,202)	(12,484)
Proceeds from disposition of property	9,917	20,730
Collections on notes receivable	3,151	—
Net cash flows (used in) provided by investing activities	(134)	8,246
Cash flows from financing activities:		
Long-term debt payments	(17,747)	(22,906)
Proceeds from exercise of stock options	3,339	102
Tax withholding on share-based payments	(154)	(253)
Net bank overdrafts	(2,716)	(3,745)
Deferred financing costs	(58)	—
Debt transaction costs	(10)	—
Net cash flows used in financing activities	(17,346)	(26,802)

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Increase in cash and cash equivalents	14,113	8,844
Cash and cash equivalents at:		
Beginning of period	26,525	21,042
End of period	\$ 40,638	\$ 29,886

See accompanying notes

Denny's Corporation and Subsidiaries
Notes to Condensed Consolidated Financial Statements
(Unaudited)

Note 1. Introduction and Basis of Presentation

Denny's Corporation, or Denny's, is one of America's largest family-style restaurant chains. At September 29, 2010, the Denny's brand consisted of 1,612 restaurants, 1,380 (86%) of which were franchised/licensed restaurants and 232 (14%) of which were company-owned and operated.

The following table shows the unit activity for the quarter and three quarters ended September 29, 2010 and September 30, 2009:

	Quarter Ended		Three Quarters Ended	
	September 29, 2010	September 30, 2009	September 29, 2010	September 30, 2009
Company-owned restaurants, beginning of period	228	263	233	315
Units opened	6	—	10	1
Units sold to franchisees	(2)	(7)	(11)	(59)
Units closed	—	—	—	(1)
End of period	232	256	232	256
Franchised and licensed restaurants, beginning of period	1,328	1,281	1,318	1,226
Units opened	55	9	68	29
Units purchased from Company	2	7	11	59
Units closed	(5)	(8)	(17)	(25)
End of period	1,380	1,289	1,380	1,289
Total restaurants, end of period	1,612	1,545	1,612	1,545

Our unaudited Condensed Consolidated Financial Statements have been prepared pursuant to the rules and regulations of the Securities and Exchange Commission. Therefore, certain information and notes normally included in financial statements prepared in accordance with U.S. generally accepted accounting principles have been condensed or omitted. In our opinion, all adjustments considered necessary for a fair presentation of the interim periods presented have been included. Such adjustments are of a normal and recurring nature. The preparation of these financial statements requires us to make estimates and judgments that affect the reported amounts of assets, liabilities, revenues and expenses, and related disclosure of contingent assets and liabilities. Actual results may differ from these estimates under different assumptions or conditions; however, we believe that our estimates, including those for the above-described items, are reasonable.

These interim Condensed Consolidated Financial Statements should be read in conjunction with our Consolidated Financial Statements and notes thereto for the year ended December 30, 2009 and the related Management's Discussion and Analysis of Financial Condition and Results of Operations, both of which are contained in our Annual Report on Form 10-K for the fiscal year ended December 30, 2009. The results of operations for the interim periods

presented are not necessarily indicative of the results for the entire fiscal year ending December 29, 2010.

Note 2. Summary of Significant Accounting Policies

Newly Adopted Accounting Standards

Fair Value

Accounting Standards Update (“ASU”) No. 2010-06, “Fair Value Measurements and Disclosures (Topic 820): Improving Disclosures about Fair Value Measurements”

Effective March 31, 2010, we adopted ASU No. 2010-06, which improves disclosure requirements related to fair value measurements under the Codification. The new disclosure requirements relate to transfers in and out of Levels 1 and 2. ASU No. 2010-06 also includes separate disclosure requirements about purchases, sales, issuances and settlements relating to Level 3 measurements, which we are required to adopt in the first quarter of 2011. The adoption did not have a material impact on the disclosures included in our Condensed Consolidated Financial Statements.

Subsequent Events

ASU No. 2010-09, “Subsequent Events (Topic 855): Amendments to Certain Recognition and Disclosure Requirements”

Effective December 31, 2009, the first day of fiscal 2010, we adopted ASC No. 2010-09, which removes the requirement to disclose the date through which subsequent events have been evaluated. The adoption did not have a material impact on the disclosures included in our Condensed Consolidated Financial Statements. See Note 18.

Variable Interest Entities

Financial Accounting Standards Board (“FASB”) Accounting Standards Codification (“ASC”) 810 “Consolidation”

Effective December 31, 2009, the first day of fiscal 2010, we adopted FASB ASC 810, which amends the guidance on the consolidation of variable interest entities for determining whether an entity is a variable interest entity and modifies the methods allowed for determining the primary beneficiary of a variable interest entity. In addition, it requires ongoing reassessments of whether an enterprise is the primary beneficiary of a variable interest entity and enhanced disclosures related to an enterprise’s involvement in a variable interest entity. The adoption did not have a material impact on our Condensed Consolidated Financial Statements.

There have been no other material changes to our significant accounting policies and estimates from the information provided in Note 2 of our Consolidated Financial Statements included in our Form 10-K for the fiscal year ended December 30, 2009.

Accounting Standards to be Adopted

Fair Value

Accounting Standards Update (“ASU”) No. 2010-06, “Fair Value Measurements and Disclosures (Topic 820): Improving Disclosures about Fair Value Measurements”

As mentioned under the "Fair Value" section above, we are required to adopt the disclosure requirements of ASU 2010-06 about purchases, sales, issuances and settlements relating to Level 3 measurements in the first quarter of 2011. We do not anticipate that the adoption will have a material impact on the disclosures included in our Condensed Consolidated Financial Statements.

Receivables

Accounting Standards Update (“ASU”) No. 2010-20, “Disclosures about the Credit Quality of Financing Receivables and the Allowance for Credit Losses”

In July 2010, the FASB issued ASU 2010-20, which requires additional disclosures about the credit quality of financing receivables, including credit card receivables, and the allowance for doubtful accounts. We are required to adopt the provisions of this ASU in the fourth quarter of 2010. We believe the adoption will result in increased notes receivable disclosure, but will not have any impact on our Condensed Consolidated Financial Statements.

Accounting standards that have been issued or proposed by the FASB or other standards-setting bodies that do not require adoption until a future date are not expected to have a material impact on our Condensed Consolidated Financial Statements upon adoption.

Note 3. Notes Receivables

Notes receivable were comprised of the following:

September 29, 2010	December 30, 2009
(In thousands)	

Current assets (included as a component of receivables):

Receivables related to sale of restaurants to franchisees	\$	825	\$	3,504
Receivables related to sale of real estate to a third party		63		61
Total current notes receivable	\$	888	\$	3,565

Noncurrent (included as a component of other noncurrent assets):

Receivables related to sale of restaurants to franchisees	\$	1,667	\$	1,894
Receivables related to sale of real estate to a third party		64		111
Total noncurrent notes receivable	\$	1,731	\$	2,005

Note 4. Assets Held for Sale

Assets held for sale of \$6.5 million as of September 29, 2010, include restaurants and real estate to be sold to franchisees. There were no assets held for sale as of December 30, 2009. We expect to sell each of these assets within 12 months. Our Credit Facility (defined in Note 8) required us to make mandatory prepayments to reduce outstanding indebtedness with the net cash proceeds from the sale of specified real estate properties, restaurant assets and restaurant operations to franchisees, net of a voluntary \$10.0 million annual exclusion related to proceeds from the sale of restaurant operations to franchisees and a voluntary \$10.0 million annual exclusion related to proceeds from the sale of restaurant assets. As of September 29, 2010 and December 30, 2009, no reclassification of long-term debt to current liabilities was required. As a result of classifying certain assets as held for sale, we recognized impairment charges of \$0.1 million for the quarter and three quarters ended September 29, 2010 and \$0.4 million for the three quarters ended September 30, 2009. This expense is included as a component of operating (gains), losses and other charges, net in our Condensed Consolidated Statements of Operations.

Note 5. Goodwill and Other Intangible Assets

The changes in carrying amounts of goodwill for the three quarters ended September 29, 2010 are as follows:

	(In thousands)
Balance at December 30, 2009	\$ 32,440
Write-offs associated with sale of restaurants	(548)
Balance at September 29, 2010	\$ 31,892

Goodwill and intangible assets were comprised of the following:

	September 29, 2010		December 30, 2009	
	Gross Carrying Amount	Accumulated Amortization	Gross Carrying Amount	Accumulated Amortization
	(In thousands)			
Goodwill	\$ 31,892	\$ —	\$ 32,440	\$ —
Intangible assets with indefinite lives:				
Trade names	\$ 42,483	\$ —	\$ 42,454	\$ —
Liquor licenses	176	—	176	—
Intangible assets with definite lives:				
Franchise and license agreements	46,513	36,365	50,787	38,397
Foreign license agreements	241	160	241	151
Intangible assets	\$ 89,413	\$ 36,525	\$ 93,658	\$ 38,548
Other assets with definite lives:				
Software development costs	\$ 33,570	\$ 29,899	\$ 32,806	\$ 28,401

Note 6. Operating (Gains), Losses and Other Charges, Net

Operating (gains), losses and other charges, net are comprised of the following:

	Quarter Ended		Three Quarters Ended	
	September 29, 2010	September 30, 2009	September 29, 2010	September 30, 2009
	(In thousands)			
Gains on sales of assets and other, net	\$ (3,757)	\$ (3,127)	\$ (5,233)	\$ (7,159)
Restructuring charges and exit costs	1,778	479		