

CHARLOTTE RUSSE HOLDING INC

Form 10-Q

July 22, 2009

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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 JUNE 27, 2009

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

COMMISSION FILE NUMBER 000-27677

CHARLOTTE RUSSE HOLDING, INC.

(Exact Name of Registrant as Specified in Its Charter)

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DELAWARE
(State or Other Jurisdiction of Incorporation)

33-0724325
(I.R.S. Employer Identification No.)

4645 MORENA BOULEVARD

SAN DIEGO, CA
(Address of Principal Executive Offices)

92117
(Zip Code)

(858) 587-1500

(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," "non-accelerated filer" and "smaller reporting company" in Rule 12b-2 of the Exchange Act.

Large accelerated filer

Accelerated filer

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

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

Indicate the number of shares outstanding of each of the issuer's classes of common stock, as of the latest practicable date:

The number of shares of common stock outstanding as of July 21, 2009 was 21,044,791.

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	June 27, 2009 (Unaudited)	September 27, 2008 (Audited)
ASSETS		
Current assets:		
Cash and cash equivalents	\$ 59,991,613	\$ 45,462,083
Inventories	53,486,272	62,986,139
Landlord allowances receivable	440,848	6,920,100
Deferred tax assets	7,479,012	7,479,012
Other current assets	10,581,595	7,727,668
Total current assets	131,979,340	130,575,002
Fixed assets, net	205,879,013	224,346,059
Goodwill	28,790,000	28,790,000
Long-term deferred taxes	3,189,763	3,958,197
Other long-term assets	887,179	1,006,203
Total assets	\$ 370,725,295	\$ 388,675,461
LIABILITIES AND STOCKHOLDERS EQUITY		
Current liabilities:		
Accounts payable, trade	\$ 35,908,481	\$ 39,753,574
Accounts payable, other	6,109,348	14,974,051
Accrued payroll and related expense	4,663,433	8,049,185
Sales taxes payable	2,558,652	2,654,624
Other current liabilities	9,873,571	9,289,175
Total current liabilities	59,113,485	74,720,609
Deferred rent	113,295,232	118,604,954
Other liabilities	1,400,052	2,099,878
Total liabilities	173,808,769	195,425,441
Commitments and contingencies		
Stockholders' equity:		
Preferred stock, \$0.01 par value; 3,000,000 shares authorized; none issued and outstanding		
Common stock, \$0.01 par value; 100,000,000 shares authorized; 21,025,870 and 20,871,389 shares issued and outstanding at June 27, 2009 and September 27, 2008, respectively	210,259	208,714
Additional paid-in capital	65,661,022	64,520,843
Retained earnings	131,045,245	128,520,463
Total stockholders' equity	196,916,526	193,250,020
Total liabilities and stockholders' equity	\$ 370,725,295	\$ 388,675,461

See accompanying notes.

Table of Contents**CHARLOTTE RUSSE HOLDING, INC.****CONSOLIDATED STATEMENTS OF INCOME****(Unaudited)**

	Three Months Ended		Nine Months Ended	
	June 27, 2009 (13 weeks)	June 28, 2008 (13 weeks)	June 27, 2009 (39 weeks)	June 28, 2008 (39 weeks)
Net sales	\$ 202,711,091	\$ 193,232,962	\$ 634,617,025	\$ 616,527,615
Cost of goods sold, including buying, distribution and occupancy costs	146,754,550	141,599,061	483,284,954	451,309,927
Gross profit	55,956,541	51,633,901	151,332,071	165,217,688
Selling, general and administrative expenses	45,080,512	41,272,866	145,408,977	127,412,775
Impairment of long-lived assets			1,550,137	839,806
Operating income	10,876,029	10,361,035	4,372,957	36,965,107
Other income:				
Interest income, net	22,266	297,876	261,409	2,311,359
Total other income	22,266	297,876	261,409	2,311,359
Income before income taxes	10,898,295	10,658,911	4,634,366	39,276,466
Income tax expense	4,642,674	4,082,364	2,109,584	14,465,887
Net income	\$ 6,255,621	\$ 6,576,547	\$ 2,524,782	\$ 24,810,579
Earnings per share				
Basic	\$ 0.30	\$ 0.31	\$ 0.12	\$ 1.05
Diluted	\$ 0.29	\$ 0.31	\$ 0.12	\$ 1.04
Weighted average shares outstanding:				
Basic	20,935,758	20,989,953	20,917,099	23,609,819
Diluted	21,295,552	21,167,994	21,135,791	23,771,641

See accompanying notes.

Table of Contents**CHARLOTTE RUSSE HOLDING, INC.****CONSOLIDATED STATEMENTS OF CASH FLOWS****(Unaudited)**

	Nine Months Ended	
	June 27, 2009 (39 weeks)	June 28, 2008 (39 weeks)
Operating Activities		
Net income	\$ 2,524,782	\$ 24,810,579
Adjustments to reconcile net income to net cash provided by operating activities		
Depreciation and amortization	34,068,280	32,494,883
Amortization of construction allowances	(10,860,908)	(10,645,739)
Stock-based compensation	1,758,375	2,315,924
Deferred rent	1,100,854	2,529,189
Impairment of long-lived assets	1,550,137	839,806
Loss on disposal of assets	115,983	732,145
Deferred income taxes		(241,200)
Changes in operating assets and liabilities:		
Inventories	9,499,867	9,610,680
Prepaid rent		10,789,305
Landlord allowance receivable	6,479,252	(1,619,895)
Other current assets	(2,853,927)	(928,706)
Accounts payable, trade	(3,845,093)	347,694
Accounts payable, other	(8,864,703)	(117,284)
Accrued payroll and related expense	(3,385,752)	(741,758)
Sales taxes payable	(95,973)	(76,941)
Long term contracts	98,872	89,915
Landlord construction allowances	4,450,331	17,370,339
Other current liabilities	584,397	2,832,934
Other liabilities	(699,825)	860,959
Net cash provided by operating activities	31,624,949	91,252,829
Investing Activities		
Purchases of fixed assets	(17,230,953)	(38,723,770)
Purchases of other assets	(16,249)	(175,420)
Net cash used in investing activities	(17,247,202)	(38,899,190)
Financing Activities		
Proceeds from issuance of common stock	151,783	672,499
Excess tax benefits from option exercises		53,709
Repurchases of Common Stock		(75,390,000)
Net cash provided by (used in) financing activities	151,783	(74,663,792)
Net increase (decrease) in cash and cash equivalents	14,529,530	(22,310,153)
Cash and cash equivalents at beginning of the period	45,462,083	68,212,148

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Cash and cash equivalents at end of the period

\$ 59,991,613

\$ 45,901,995

See accompanying notes.

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CHARLOTTE RUSSE HOLDING, INC.

Notes to Consolidated Financial Statements (Unaudited)

1. Summary of Significant Accounting Policies

Basis of Presentation

The accompanying unaudited consolidated financial statements of Charlotte Russe Holding, Inc. (the Company) have been prepared in accordance with generally accepted accounting principles (GAAP) in the United States for interim financial information and with the instructions to Form 10-Q and Article 10 of Regulation S-X. Certain information and footnote disclosures required by GAAP in the United States for complete financial statements have been condensed or omitted pursuant to the rules and regulations of the Securities and Exchange Commission. In the opinion of management, the accompanying unaudited financial statements contain all material adjustments, including normal recurring accruals, necessary to present fairly the Company's financial position, results of operations and cash flows for the periods indicated, and have been prepared in a manner consistent with the audited financial statements for the fiscal year ended September 27, 2008. Certain amounts have been reclassified in prior periods to conform to the current period presentation. The Company has evaluated all subsequent events through July 22, 2009, the date the financial statements were issued.

The results of operations for the three and nine month periods ended June 27, 2009 are not necessarily indicative of the results of a full fiscal year.

These financial statements should be read in conjunction with the audited financial statements and the footnotes for the fiscal year ended September 27, 2008 included in the Company's Annual Report on Form 10-K, filed with the Securities and Exchange Commission on December 9, 2008, and the Company's amended Annual Report on Form 10-K/A, filed with the Securities and Exchange Commission on January 26, 2009.

Use of Estimates

The preparation of financial statements in conformity with GAAP requires management to make estimates and assumptions that affect the amounts reported in the consolidated financial statements. These estimates include assessing the valuation of stock-based compensation, recognition of revenues, sales allowances, the valuation of inventories and long-lived assets, including goodwill, income tax and liabilities associated with employee benefit costs, among others. Actual results could differ from those estimates.

Goodwill

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Goodwill represents the excess of the cost over the fair value of net assets acquired. In accordance with Statement of Financial Accounting Standards (SFAS) No. 142, *Goodwill and Other Intangible Assets*, the Company is required to test goodwill annually for impairment or more frequently if events and circumstances warrant, utilizing a test that begins with an estimate of the fair value of the reporting unit. The Company tests goodwill annually and whenever events or circumstances occur indicating that goodwill might be impaired.

During the first quarter of fiscal 2009, the Company concluded that events had occurred and circumstances had changed, that may indicate the existence of potential impairment of goodwill. These indicators included a significant decline in the Company's stock price, continued deterioration in the retail marketplace, and the related impact the current retail marketplace had on management's expectations for future revenues. As a result, the Company performed an interim assessment of goodwill for impairment in the first quarter of fiscal 2009. Included in the interim testing was a review of the fair market value of the Company as compared to the carrying value of its assets using a discounted cash flow model. The significant factors and assumptions the Company used in its discounted cash flow analysis included: earnings before interest, taxes, depreciation and amortization (EBITDA), the discount rate used to calculate the present value of future cash flows and future capital expenditures. EBITDA assumptions included sales growth assumptions based on the Company's historical sales

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CHARLOTTE RUSSE HOLDING, INC.

Notes to Consolidated Financial Statements (Unaudited) (Continued)

1. Summary of Significant Accounting Policies (continued)

trends, as well as gross margin and selling, general and administrative expense growth assumptions based on the historical relationship of those measures compared to sales, adjusting for the current economic conditions. The Company also considered as an indicator of fair market value its total market capitalization based on the trading price of its common stock as of December 27, 2008. However, given the extreme volatility in the stock market during the quarter ended December 27, 2008, as well as the impact that the credit crisis and the recession had on the stock market during that period, and the fact that the carrying value of the Company's assets did not exceed its total market capitalization during any period prior to the first quarter of fiscal 2009, management concluded that it was appropriate to place more reliance on fair market value as calculated by the Company's discounted cash flow model in evaluating goodwill impairment as of December 27, 2008, rather than the total market capitalization. The Company's assessment concluded that step 2 was not required and no impairment of goodwill existed as of December 27, 2008, as the fair value exceeded carrying value.

During the second and third quarters of fiscal 2009, these indicators began to improve, and the Company determined that an interim assessment of goodwill for impairment was not warranted. On March 12, 2009, the Company announced that its Board of Directors had instructed its financial advisor to initiate a sale process. Additionally, beginning in January 2009, the Company's fair market value as indicated by its stock price began to improve, and although the retail marketplace in general has not improved significantly, the Company's results in the latter part of the second quarter were improving. These trends continued into the third quarter, and at June 27, 2009, total market capitalization based on the trading price of the Company's common stock exceeded its net book value. The Company will perform its annual impairment analysis in the fourth quarter.

Impairment of Long-Lived Assets

In accordance with SFAS No. 144, *Accounting for the Impairment or Disposal of Long-Lived Assets*, whenever events or changes in circumstances indicate that the carrying amount of its assets might not be recoverable, the Company, using its best estimates based upon reasonable and supportable assumptions and projections, reviews the carrying value of long-lived assets for impairment based on an estimate of undiscounted future cash flows resulting from the use of those assets in operation. If estimated future undiscounted cash flows are not sufficient to recover the carrying value of the assets, then the Company compares the carrying value to fair value of those assets. Impairment for long-lived assets to be held is measured by comparing the carrying amount of the asset to its fair value. Impairment is reviewed at the lowest levels for which there are identifiable cash flows that are independent of the cash flows of other groups of assets. The Company performs such analysis on an individual store basis and estimates fair values based on an analysis of discounted cash flows. The Company measures impairment for long-lived assets to be disposed of at the lower of the carrying amount or net realizable value (fair market value less cost to dispose).

During the second quarter of fiscal 2009, the Company recorded a \$1.6 million impairment charge against the carrying values of long-lived assets. The Company reviewed individual store performance by projecting forecasted sales over each store's remaining lease term, and calculating each store's discounted cash flow. This discounted cash flow was compared to the carrying value of each store's assets. For certain stores, this analysis resulted in an asset carrying value greater than the estimated discounted cash flow. The carrying value of these assets was written down to estimated fair value. In the second quarter of fiscal 2008, the Company recorded a \$0.8 million impairment charge. No impairment charges were recorded during the third quarter of fiscal 2009 or 2008.

Changes in events or circumstances used to develop assumptions relied upon in the Company's analysis, may affect the estimated discounted cash flows expected to be derived from long-lived assets. Such changes may either increase or decrease the expected cash flows and could cause additional stores to become impaired and the Company to record additional charges to income.

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CHARLOTTE RUSSE HOLDING, INC.

Notes to Consolidated Financial Statements (Unaudited) (Continued)

1. Summary of Significant Accounting Policies (continued)

Vendor Allowances

The Company receives certain allowances from its merchandise vendors primarily related to distribution center handling expenses or defective merchandise. Agreements with vendors for these allowances apply to all shipments and sale of merchandise to the Company. These allowances are reflected as a reduction of merchandise inventory in the period they are received and allocated to cost of sales during the period in which the items are sold. Vendor allowances included in cost of goods sold totaled \$2.7 million and \$2.9 million in the third quarter of fiscal 2009 and 2008, respectively, and \$10.0 million and \$10.2 million in the first nine months of fiscal 2009 and 2008, respectively.

Adoption of Recent Accounting Pronouncements

In May 2009, the Financial Accounting Standards Board (FASB) issued SFAS No. 165, *Subsequent Events* (SFAS No. 165). SFAS No. 165 establishes general standards of accounting for the disclosure of events that occur after the balance sheet date but before financial statements are issued or available to be issued. It requires the disclosure of the date through which an entity has evaluated subsequent events and whether that date represents the date the financial statements were issued or were available to be issued. SFAS No. 165 is effective for interim or annual financial periods ending after June 15, 2009 and is applied prospectively. The Company adopted this statement effective June 27, 2009. There was no material financial statement impact as a result of adoption.

In April 2009, the FASB issued FASB Staff Position (FSP) No. FAS 107-1 and APB 28-1, *Interim Disclosures about Fair Value of Financial Instruments* (FSP No. FAS 107-1 and APB 28-1). FSP No. FAS 107-1 and APB 28-1 requires a publicly traded company to include disclosures about the fair value of its financial instruments whenever it issues summarized financial information for interim reporting periods. FSP No. FAS 107-1 and APB 28-1 is effective for interim reporting periods ending after June 15, 2009. The Company adopted this statement effective June 27, 2009. There was no material financial statement impact as a result of adoption.

In May 2008, the FASB issued SFAS No. 162, *The Hierarchy of Generally Accepted Accounting Principles* (SFAS No. 162). SFAS No. 162 identifies the sources of accounting principles and the framework for selecting the principles to be used in the preparation of financial statements of nongovernmental entities that are presented in conformity with GAAP. SFAS No. 162 is effective as of November 15, 2008 for financial statements presented in conformity with GAAP. The Company adopted this statement effective November 15, 2008. There was no material financial statement impact as a result of adoption.

In September 2006, the FASB issued SFAS No. 157, *Fair Value Measurements* (SFAS No. 157). SFAS No. 157 provides guidance for using fair value to measure assets and liabilities. It also responds to investors' requests for expanded information about the extent to which companies

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measure assets and liabilities at fair value, the information used to measure fair value and the effect of fair valued measurements on earnings. SFAS No. 157 applies whenever standards require (or permit) assets or liabilities to be measured at fair value, and does not expand the use of fair value in any new circumstances. SFAS No. 157 is effective for financial assets and liabilities in financial statements issued for fiscal years beginning after November 15, 2007. The Company adopted this statement for financial assets and liabilities measured at fair value effective September 28, 2008. There was no material financial statement impact as a result of adoption. In accordance with the guidance of FSP No. 157-2, *Effective Date of FASB Statement No. 157*, the Company has postponed adoption of the standard for non-financial assets and liabilities that are measured at fair value on a non-recurring basis, until the fiscal year beginning after November 15, 2008. Non-financial assets and liabilities that are measured at fair value on a

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CHARLOTTE RUSSE HOLDING, INC.

Notes to Consolidated Financial Statements (Unaudited) (Continued)

1. Summary of Significant Accounting Policies (continued)

non-recurring basis include fixed assets and goodwill. The Company does not anticipate adoption will have a material impact on its consolidated financial position, results of operations or liquidity. See Note 4 for more information.

In October 2008, the FASB issued FSP No. 157-3, *Determining the Fair Value of a Financial Asset When the Market for That Asset Is Not Active* (FSP No. 157-3). FSP No. 157-3 clarifies the application of SFAS No. 157 in a market that is not active, and is effective as of the issue date, including application to prior periods for which financial statements have not been issued. The Company adopted this statement effective October 10, 2008. There was no material financial statement impact as a result of adoption.

In February 2007, the FASB issued SFAS No. 159, *The Fair Value Option for Financial Assets and Financial Liabilities Including an amendment of FASB Statement No. 115* (SFAS No. 159). SFAS No. 159 expands the use of fair value accounting but does not affect existing standards that require assets or liabilities to be carried at fair value. Under SFAS No. 159, a company may elect to use fair value to measure accounts and loans receivable, available-for-sale and held-to-maturity securities, equity method investments, accounts payable, guarantees and issued debt. Other eligible items include firm commitments for financial instruments that otherwise would not be recognized at inception and non-cash warranty obligations where a warrantor is permitted to pay a third party to provide the warranty goods or services. If the use of fair value is elected, any upfront costs and fees related to the item must be recognized in earnings and cannot be deferred (e.g., debt issue costs). The fair value election is irrevocable and generally made on an instrument-by-instrument basis, even if a company has similar instruments that it elects not to measure based on fair value. At the adoption date, unrealized gains and losses on existing items for which fair value has been elected are reported as a cumulative adjustment to beginning retained earnings. Subsequent to the adoption of SFAS No. 159, changes in fair value are recognized in earnings. SFAS No. 159 is effective for fiscal years beginning after November 15, 200