

LANDSTAR SYSTEM INC

Form 10-Q

July 31, 2009

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**UNITED STATES  
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 27, 2009**

**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 Number: **0-21238**

**LANDSTAR SYSTEM, INC.**

(Exact name of registrant as specified in its charter)

**Delaware** **06-1313069**  
(State or other jurisdiction (I.R.S. Employer  
of incorporation or organization) Identification No.)

**13410 Sutton Park Drive South, Jacksonville, Florida**

(Address of principal executive offices)

**32224**

(Zip Code)

**(904) 398-9400**

(Registrant's telephone number, including area code)

**N/A**

(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 has submitted electronically and posted on its corporate Website, 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. (Check one):

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

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The number of shares of the registrant's common stock, par value \$0.01 per share, outstanding as of the close of business on July 17, 2009 was 51,312,580.

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**PART I** FINANCIAL INFORMATION

Item 1. Financial Statements

The interim consolidated financial statements contained herein reflect all adjustments (all of a normal, recurring nature) which, in the opinion of management, are necessary for a fair statement of the financial condition, results of operations, cash flows and changes in shareholders' equity for the periods presented. They have been prepared in accordance with Rule 10-01 of Regulation S-X and do not include all the information and footnotes required by generally accepted accounting principles for complete financial statements. Operating results for the twenty six weeks ended June 27, 2009 are not necessarily indicative of the results that may be expected for the entire fiscal year ending

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December 26, 2009.

These interim financial statements should be read in conjunction with the audited financial statements and notes thereto included in the Company's 2008 Annual Report on Form 10-K.

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CONSOLIDATED BALANCE SHEETS

(Dollars in thousands, except per share amounts)

(Unaudited)

	<b>June 27, 2009</b>	<b>Dec. 27, 2008</b>
<b>ASSETS</b>		
Current Assets		
Cash and cash equivalents	\$ 92,091	\$ 98,904
Short-term investments	23,791	23,479
Trade accounts receivable, less allowance of \$7,092 and \$6,230	237,516	315,065
Other receivables, including advances to independent contractors, less allowance of \$5,344 and \$4,298	12,639	10,083
Deferred income taxes and other current assets	28,128	27,871
Total current assets	394,165	475,402
Operating property, less accumulated depreciation and amortization of \$115,023 and \$106,635	124,513	124,178
Goodwill	31,134	31,134
Other assets	33,512	32,816
Total assets	\$ 583,324	\$ 663,530
<b>LIABILITIES AND SHAREHOLDERS EQUITY</b>		
Current Liabilities		
Cash overdraft	\$ 20,471	\$ 32,065
Accounts payable	91,858	105,882
Current maturities of long-term debt	25,881	24,693
Insurance claims	27,410	23,545
Accrued income taxes	11,948	12,239
Other current liabilities	34,435	38,161
Total current liabilities	212,003	236,585
Long-term debt, excluding current maturities	37,778	111,752
Insurance claims	34,459	38,278
Deferred income taxes	27,825	23,779
Shareholders Equity		
Common stock, \$0.01 par value, authorized 160,000,000 shares, issued 66,181,267 and 66,109,547 shares	662	661
Additional paid-in capital	158,543	154,533
Retained earnings	731,959	704,331

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Cost of 14,868,687 and 14,424,887 shares of common stock in treasury	(619,609)	(605,828)
Accumulated other comprehensive loss	(296)	(561)
Total shareholders' equity	271,259	253,136
Total liabilities and shareholders' equity	\$ 583,324	\$ 663,530

See accompanying notes to consolidated financial statements.

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LANDSTAR SYSTEM, INC. AND SUBSIDIARY  
CONSOLIDATED STATEMENTS OF INCOME  
(Dollars in thousands, except per share amounts)  
(Unaudited)

	<b>Twenty Six Weeks Ended</b>		<b>Thirteen Weeks Ended</b>	
	<b>June 27, 2009</b>	<b>June 28, 2008</b>	<b>June 27, 2009</b>	<b>June 28, 2008</b>
Revenue	\$ 960,411	\$ 1,306,479	\$ 491,164	\$ 697,651
Investment income	675	1,869	250	773
Costs and expenses:				
Purchased transportation	717,891	1,003,345	366,567	538,316
Commissions to agents	78,251	99,590	39,927	52,776
Other operating costs	14,838	13,940	7,388	7,356
Insurance and claims	18,799	19,034	9,797	9,513
Selling, general and administrative	66,612	70,958	32,243	35,101
Depreciation and amortization	11,201	10,307	5,716	5,177
Total costs and expenses	907,592	1,217,174	461,638	648,239
Operating income	53,494	91,174	29,776	50,185
Interest and debt expense	2,136	3,878	973	1,736
Income before income taxes	51,358	87,296	28,803	48,449
Income taxes	19,607	33,788	10,946	18,684
Net income	\$ 31,751	\$ 53,508	\$ 17,857	\$ 29,765
Earnings per common share	\$ 0.62	\$ 1.01	\$ 0.35	\$ 0.56
Diluted earnings per share	\$ 0.61	\$ 1.01	\$ 0.35	\$ 0.56
Average number of shares outstanding:				
Earnings per common share	51,453,000	52,726,000	51,330,000	52,851,000
Diluted earnings per share	51,636,000	53,198,000	51,487,000	53,373,000
Dividends paid per common share	\$ 0.0800	\$ 0.0750	\$ 0.0400	\$ 0.0375

See accompanying notes to consolidated financial statements.



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LANDSTAR SYSTEM, INC. AND SUBSIDIARY  
CONSOLIDATED STATEMENTS OF CASH FLOWS  
(Dollars in thousands)  
(Unaudited)

	<b>Twenty Six Weeks Ended</b>	
	<b>June 27, 2009</b>	<b>June 28, 2008</b>
<b>OPERATING ACTIVITIES</b>		
Net income	\$ 31,751	\$ 53,508
Adjustments to reconcile net income to net cash provided by operating activities:		
Depreciation and amortization of operating property	11,201	10,307
Non-cash interest charges	109	87
Provisions for losses on trade and other accounts receivable	4,868	3,156
Losses (gains) on sales/disposals of operating property	(80)	7
Director compensation paid in common stock		634
Deferred income taxes, net	3,542	4,183
Stock-based compensation	2,570	3,352
Changes in operating assets and liabilities:		
Decrease (increase) in trade and other accounts receivable	70,125	(47,409)
Decrease (increase) in other assets	388	(7,056)
Increase (decrease) in accounts payable	(14,024)	15,664
Decrease in other liabilities	(4,149)	(1,405)
Increase (decrease) in insurance claims	46	(440)
<b>NET CASH PROVIDED BY OPERATING ACTIVITIES</b>	<b>106,347</b>	<b>34,588</b>
<b>INVESTING ACTIVITIES</b>		
Net change in other short-term investments	4,553	(2,783)
Sales and maturities of investments	5,612	7,529
Purchases of investments	(11,049)	(6,881)
Purchases of operating property	(2,047)	(3,997)
Proceeds from sales of operating property	384	23
<b>NET CASH USED BY INVESTING ACTIVITIES</b>	<b>(2,547)</b>	<b>(6,109)</b>
<b>FINANCING ACTIVITIES</b>		
Increase (decrease) in cash overdraft	(11,594)	4,368
Dividends paid	(4,123)	(3,955)
Proceeds from exercises of stock options	1,116	11,993
Excess tax benefit on stock option exercises	325	1,630
Borrowings on revolving credit facility		67,000
Purchases of common stock	(13,781)	
Principal payments on long-term debt and capital lease obligations	(82,579)	(91,473)

NET CASH USED BY FINANCING ACTIVITIES	(110,636)	(10,437)
Effect of exchange rate changes on cash and cash equivalents	23	
Increase (decrease) in cash and cash equivalents	(6,813)	18,042
Cash and cash equivalents at beginning of period	98,904	60,750
Cash and cash equivalents at end of period	\$ 92,091	\$ 78,792

See accompanying notes to consolidated financial statements.

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LANDSTAR SYSTEM, INC. AND SUBSIDIARY  
CONSOLIDATED STATEMENT OF CHANGES IN SHAREHOLDERS' EQUITY  
Twenty Six Weeks Ended June 27, 2009  
(Dollars in thousands)  
(Unaudited)

	Common Stock		Additional Paid-In	Retained	Treasury Stock at Cost		Accumulated Other Comprehensive Income	Total
	Shares	Amount	Capital	Earnings	Shares	Amount	(Loss)	
Balance December 27, 2008	66,109,547	\$ 661	\$ 154,533	\$ 704,331	14,424,887	\$ (605,828)	\$ (561)	\$ 253,136
Net income				31,751				31,751
Dividends paid (\$0.08 per share)				(4,123)				(4,123)
Purchases of common stock					443,800	(13,781)		(13,781)
Stock-based compensation			2,570					2,570
Exercises of stock options, including excess tax benefit	71,720	1	1,440					1,441
Foreign currency translation							23	23
Unrealized gain on available-for-sale investments, net of income taxes							242	242
Balance June 27, 2009	66,181,267	\$ 662	\$ 158,543	\$ 731,959	14,868,687	\$ (619,609)	\$ (296)	\$ 271,259

See accompanying notes to consolidated financial statements.

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LANDSTAR SYSTEM, INC. AND SUBSIDIARY  
 NOTES TO CONSOLIDATED FINANCIAL STATEMENTS  
 (Unaudited)

The consolidated financial statements include the accounts of Landstar System, Inc. and its subsidiary, Landstar System Holdings, Inc., and reflect all adjustments (all of a normal, recurring nature) which are, in the opinion of management, necessary for a fair statement of the results for the periods presented. The preparation of the consolidated financial statements requires the use of management's estimates. Actual results could differ from those estimates. Landstar System, Inc. and its subsidiary are herein referred to as "Landstar" or the "Company".

**(1) Share-based Payments**

The Company's Board of Directors has amended and restated the 2002 Employee Stock Option Plan. As amended and restated, the 2002 Employee Stock Option Plan is now called the Amended and Restated 2002 Employee Stock Option and Stock Incentive Plan (the "ESOSIP"). The ESOSIP was approved by vote of the Company's shareholders at the Annual Meeting of Stockholders on April 30, 2009. The amendment and restatement of the ESOSIP will, among other things, provide the Compensation Committee of the Company's Board of Directors the power to grant equity and equity-based awards in addition to stock options, including restricted stock, stock appreciation rights, performance shares and other stock based awards. It also extends the term of the ESOSIP to 10 years after the date it was amended and restated by the Company's Board of Directors for all awards, except for incentive stock options which may not be granted after the tenth anniversary of the date the 2002 Employee Stock Option Plan was originally adopted by the Board.

In revising the ESOSIP, the Company has not increased the number of shares available for grant under the 2002 Employee Stock Option Plan. As originally adopted, 800,000 shares were authorized for issuance. Through the adjustment provisions of the 2002 Employee Stock Option Plan, to reflect stock splits with respect to the Company's common stock, the number of shares authorized for issuance has been adjusted to be 6,400,000 shares. Awards of restricted stock, performance shares or other stock-based awards now authorized under the ESOSIP would be made from the existing pool of shares available under the 2002 Employee Stock Option Plan. Moreover, to the extent that the awards of restricted stock, performance shares or other stock-based awards provide the recipient with the full value of the shares, and the settlement of an existing obligation is not otherwise payable in cash, each share granted would count as two shares against the share limit in the ESOSIP.

As of June 27, 2009, the Company had an employee stock option plan, the ESOSIP and one stock option plan for members of its Board of Directors (the "Plans"). No further grants can be made under the employee stock option plan as its term for granting stock options has expired. In addition, no further grants are to be made under the stock option plan for members of the Board of Directors. Amounts recognized in the financial statements with respect to these Plans are as follows (in thousands):

	<b>Twenty Six Weeks Ended</b>		<b>Thirteen Weeks Ended</b>	
	<b>June 27, 2009</b>	<b>June 28, 2008</b>	<b>June 27, 2009</b>	<b>June 28, 2008</b>
Total cost of the Plans during the period	\$ 2,570	\$ 3,352	\$ 1,181	\$ 1,659
Amount of related income tax benefit recognized during the period	650	1,060	297	530
Net cost of the Plans during the period	\$ 1,920	\$ 2,292	\$ 884	\$ 1,129

The fair value of each option grant on its grant date was calculated using the Black-Scholes option pricing model with the following weighted average assumptions for grants made in the 2009 and 2008 twenty-six-week periods:

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	<b>2009</b>	<b>2008</b>
Expected volatility	38.0%	33.0%
Expected dividend yield	0.400%	0.375%
Risk-free interest rate	1.50%	3.00%
Expected lives (in years)	4.0	4.1

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The Company utilizes historical data, including exercise patterns and employee departure behavior, in estimating the term options will be outstanding. Expected volatility was based on historical volatility and other factors, such as expected changes in volatility arising from planned changes to the Company's business, if any. The risk-free interest rate was based on the yield of zero coupon U.S. Treasury bonds for terms that approximated the terms of the options granted. The weighted average grant date fair value of stock options granted during the twenty-six-week periods ended June 27, 2009 and June 28, 2008 was \$11.75 and \$12.60, respectively.

The following table summarizes information regarding the Company's stock options under the Plans:

		<b>Weighted Average</b>	<b>Weighted Average</b>	<b>Remaining</b>	<b>Aggregate Intrinsic Value (000s)</b>
	<b>Number of Options</b>	<b>Exercise Price per Share</b>	<b>Contractual Term (years)</b>		
Options outstanding at December 27, 2008	2,505,644	\$ 35.47			
Granted	362,000	\$ 38.24			
Exercised	(71,720)	\$ 15.57			
Forfeited	(93,000)	\$ 42.74			
Options outstanding at June 27, 2009	2,702,924	\$ 36.12	7.0		\$ 0
Options exercisable at June 27, 2009	1,333,424	\$ 31.39	5.4		\$ 6,136

As of June 27, 2009, there were 1,906,747 stock options outstanding that were out-of-the-money based on that day's per share closing market price of \$35.99 as reported on the NASDAQ Global Select Market. The remaining 796,177 stock options outstanding as of June 27, 2009 that were in-the-money had an aggregate intrinsic value of \$10,777,000. The total intrinsic value of stock options exercised during the twenty-six-week periods ended June 27, 2009 and June 28, 2008 was \$1,453,000 and \$10,046,000, respectively.

As of June 27, 2009, there were 5,300,824 shares of the Company's common stock reserved for issuance upon exercise of options granted and to be granted under the Plans.

As of June 27, 2009, there was \$13,429,000 of total unrecognized compensation cost related to non-vested stock options granted under the Plans. The compensation cost related to these non-vested options is expected to be recognized over a weighted average period of 3.5 years.

Under the Directors' Stock Compensation Plan, outside members of the Board of Directors who are elected or re-elected to the Board receive 6,000 shares of common stock of the Company, subject to certain restrictions including restrictions on transfer. The Company issued 12,000 shares of its common stock in the twenty-six-week period ended June 28, 2008 to members of the Board of Directors upon such members' re-election at the 2008 annual stockholders meeting. During the 2008 twenty-six-week period, the Company reported \$634,000 in compensation expense representing the fair market value of these share awards. There were no such shares issued in the twenty-six-week period ended June 27, 2009. As of June 27, 2009, there were 138,423 shares of the Company's common stock reserved for issuance upon the grant of stock under the Directors' Stock Compensation Plan.

**(2) Income Taxes**

The provisions for income taxes for the 2009 and 2008 twenty-six-week periods were based on estimated full year combined effective income tax rates of approximately 38.2% and 38.7%, respectively, which were higher than the statutory federal income tax rate primarily as a result of state taxes, the meals and entertainment exclusion and non-deductible stock-based compensation.

(3) Earnings Per Share

Earnings per common share amounts are based on the weighted average number of common shares outstanding and diluted earnings per share amounts are based on the weighted average number of common shares outstanding plus the incremental shares that would have been outstanding upon the assumed exercise of all dilutive stock options.

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The following table provides a reconciliation of the average number of common shares outstanding used to calculate earnings per share to the average number of common shares and common share equivalents outstanding used to calculate diluted earnings per share (in thousands):

**Twenty Six Weeks  
Ended**