

FAMOUS DAVES OF AMERICA INC

Form 10-Q

November 13, 2018

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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 30, 2018

TRANSITION REPORT PURSUANT TO SECTION 13 OR 15(d)

OF THE SECURITIES EXCHANGE ACT OF 1934

Commission File No. 0 21625

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FAMOUS DAVE'S of AMERICA, INC.

(Exact name of registrant as specified in its charter)

Minnesota 41 1782300  
(State or other jurisdiction of (I.R.S. Employer  
incorporation or organization) Identification No.)

12701 Whitewater Drive, Suite 190

Minnetonka, MN 55343

(Address of principal executive offices) (Zip code)

Registrant's telephone number, including area code (952) 294 1300

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

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Indicate by check mark whether the registrant has submitted electronically every Interactive Data File required to be submitted 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 such files). Yes No

Indicate by check mark whether the registrant is a large accelerated filer, an accelerated filer, a non-accelerated filer, a smaller reporting company, or an emerging growth company. See definition of “large accelerated filer,” “accelerated filer,” “smaller reporting company,” and “emerging growth company” in Rule 12b-2 of the Exchange Act. (Check one):

Large Accelerated Filer

Accelerated Filer

Non-Accelerated Filer

Smaller Reporting Company

Emerging Growth Company

If an emerging growth company, indicate by check mark if the registrant has elected not to use the extended transition period for complying with any new or revised financial accounting standards provided pursuant to Section 13(a) of the Exchange Act.

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 November 9, 2018, 9,091,926 shares of the registrant’s Common Stock were outstanding.

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FAMOUS DAVE'S OF AMERICA, INC.

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## PART I. FINANCIAL INFORMATION

## Item 1. Financial Statements

## FAMOUS DAVE'S OF AMERICA, INC. AND SUBSIDIARIES

## CONSOLIDATED BALANCE SHEETS

SEPTEMBER 30, 2018 AND DECEMBER 31, 2017

(in thousands, except per share data)

(Unaudited)

## ASSETS

	September 30, 2018	December 31, 2017
Current assets:		
Cash and cash equivalents	\$ 4,941	\$ 8,836
Restricted cash	1,132	1,590
Accounts receivable, net of allowance for doubtful accounts of \$234,000 and \$592,000, respectively	3,835	3,768
Held-to-maturity securities	7,012	—
Inventories	657	633
Prepaid income taxes and income taxes receivable	—	689
Prepaid expenses and other current assets	712	793
Assets held for sale	—	475
Total current assets	18,289	16,784
Property, equipment and leasehold improvements, net	10,307	11,442
Other assets:		
Intangible assets, net	1,419	1,840
Deferred tax asset, net	6,587	5,823
Other assets	1,596	1,018
	\$ 38,198	\$ 36,907

## LIABILITIES AND SHAREHOLDERS' EQUITY

Current liabilities:		
Current portion of long-term debt and financing lease obligations	\$ 1,460	\$ 1,307
Accounts payable	4,182	4,365
Accrued compensation and benefits	1,221	1,545
Other current liabilities	2,607	3,118
Total current liabilities	9,470	10,335
Long-term liabilities:		
Long-term debt, less current portion	2,448	7,932
Financing lease obligation, less current portion	—	1,196
Other liabilities	4,847	3,963

Total liabilities	16,765	23,426
Shareholders' equity:		
Common stock, \$.01 par value, 100,000 shares authorized, 9,092 and 7,376 shares issued and outstanding at September 30, 2018 and December 31, 2017, respectively	91	70
Additional paid-in capital	7,321	1,460
Retained earnings	14,021	11,951
Total shareholders' equity	21,433	13,481
	\$ 38,198	\$ 36,907

See accompanying notes to consolidated financial statements.

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## CONSOLIDATED STATEMENTS OF OPERATIONS

SEPTEMBER 30, 2018 AND OCTOBER 1, 2017

(in thousands, except per share data)

(Unaudited)

	Three Months Ended		Nine Months Ended	
	September 30, 2018	October 1, 2017	September 30, 2018	October 1, 2017
<b>Revenue:</b>				
Restaurant sales, net	\$ 9,903	\$ 12,292	\$ 28,571	\$ 39,955
Franchise royalty and fee revenue	3,462	3,591	10,623	11,412
Franchisee national advertising fund contributions	497	—	1,495	—
Licensing and other revenue	211	183	766	696
Total revenue	14,073	16,066	41,455	52,063
<b>Costs and expenses:</b>				
Food and beverage costs	3,091	3,679	8,907	12,017
Labor and benefits costs	3,601	4,441	10,158	14,426
Operating expenses	3,011	3,484	8,746	11,845
Depreciation and amortization	281	1,207	983	2,311
General and administrative expenses	1,937	3,753	5,922	11,796
National advertising fund expenses	497	—	1,495	—
Asset impairment, estimated lease termination charges and other closing costs, net	31	2,405	143	7,011
Net loss on disposal of property	—	45	29	61
Total costs and expenses	12,449	19,014	36,383	59,467
Income (loss) from operations	1,624	(2,948)	5,072	(7,404)
<b>Other income (expense):</b>				
Interest expense	(80)	(153)	(422)	(510)
Interest income	54	20	79	20
Total other expense	(26)	(133)	(343)	(490)
Income (loss) before income taxes	1,598	(3,081)	4,729	(7,894)
Income tax (expense) benefit	(196)	1,167	(937)	2,910
Net income (loss) from continuing operations	1,402	(1,914)	3,792	(4,984)
Net income from discontinued operations, net of tax	—	100	—	661
Net income (loss)	\$ 1,402	\$ (1,814)	\$ 3,792	\$ (4,323)
<b>Income (loss) per common share:</b>				
Basic net income (loss) per share - continuing operations	\$ 0.15	\$ (0.28)	\$ 0.45	\$ (0.72)
Basic net income per share - discontinued operations	—	0.01	—	0.10

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Basic net income (loss) per share	\$ 0.15	\$ (0.26)	\$ 0.45	\$ (0.62)
Diluted net income (loss) per share - continuing operations	\$ 0.15	\$ (0.28)	\$ 0.45	\$ (0.72)
Diluted net income per share - discontinued operations	—	0.01	—	0.10
Diluted net income (loss) per share	\$ 0.15	\$ (0.26)	\$ 0.45	\$ (0.62)
Weighted average shares outstanding - basic	9,090	6,955	8,435	6,955
Weighted average shares outstanding - diluted	9,111	6,955	8,459	6,955

See accompanying notes to consolidated financial statements.

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## FAMOUS DAVE'S OF AMERICA, INC. AND SUBSIDIARIES

## CONSOLIDATED STATEMENTS OF CHANGES IN SHAREHOLDERS' EQUITY

SEPTEMBER 30, 2018

(in thousands)

(Unaudited)

	Common Stock		Additional	Retained	Total
	Shares	Amount	Paid-in Capital	Earnings	
Balance - December 31, 2017	7,376	\$ 70	\$ 1,460	\$ 11,951	\$ 13,481
Cumulative effect of change in accounting principle	—	—	—	(1,722)	(1,722)
Common stock issued pursuant to rights offering	1,582	18	5,119	—	5,137
Exercise of stock options	109	2	432	—	434
Stock-based compensation	25	1	310	—	311
Net income	—	—	—	3,792	3,792
Balance - September 30, 2018	9,092	\$ 91	\$ 7,321	\$ 14,021	\$ 21,433

See accompanying notes to consolidated financial statements

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## FAMOUS DAVE'S OF AMERICA, INC. AND SUBSIDIARIES

## CONSOLIDATED STATEMENTS OF CASH FLOWS

SEPTEMBER 30, 2018 AND OCTOBER 1, 2017

(in thousands)

(Unaudited)

	Nine Months Ended	
	September 30, 2018	October 1, 2017
Cash flows from operating activities:		
Net income (loss) from continuing operations	\$ 3,792	\$ (4,984)
Adjustments to reconcile net income (loss) to cash flows provided by operations:		
Depreciation and amortization	983	2,311
(Gain) loss from asset impairment and estimated lease termination and other closing costs	(257)	4,976
Net loss on disposal of property	29	61
Amortization of deferred financing costs	96	26
Amortization of lease interest assets	27	27
Deferred income taxes	(185)	351
Deferred rent	(514)	285
Bad debts (recovery) expense	(35)	921
Stock-based compensation	225	183
Changes in operating assets and liabilities:		
Accounts receivable, net	(49)	(441)
Inventories	(24)	432
Prepaid income taxes and income taxes receivable	689	(1,068)
Prepaid expenses and other current assets	81	(18)
Other assets	172	(23)
Accounts payable	(183)	349
Accrued compensation and benefits	(411)	1,013
Other current liabilities	(203)	(179)
Other liabilities	(409)	(789)
Cash flows provided by continuing operating activities	3,824	3,433
Cash flows provided by discontinued operating activities	—	1,058
Cash flows provided by operating activities	3,824	4,491
Cash flows from investing activities:		
Proceeds from the sale of assets	1,187	—
Payments for acquired restaurants	(37)	—
Advances on notes receivable	(750)	—
Purchases of held to maturity securities	(6,995)	—
Purchases of property, equipment and leasehold improvements	(597)	(252)
Cash flows used for continuing investing activities	(7,192)	(252)

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Cash flows used for discontinued investing activities	—	(49)
Cash flows used for investing activities	(7,192)	(301)
Cash flows from financing activities:		
Payments for debt issuance costs	—	(15)
Payments on long-term debt and financing lease obligations	(6,625)	(1,206)
Proceeds from sale of common stock, net of offering costs	5,120	—
Proceeds from exercise of stock options	520	—
Cash flows used for financing activities	(985)	(1,221)
Increase (decrease) in cash, cash equivalents and restricted cash	(4,353)	2,969
Cash, cash equivalents and restricted cash, beginning of period	10,426	6,164
Cash, cash equivalents and restricted cash, end of period	\$ 6,073	\$ 9,133

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	Nine Months Ended	
	September 30, 2017	October 31, 2017
<b>Supplemental Disclosures</b>		
Cash paid for interest	\$ 271	\$ 479
Cash paid (refunds received) for income taxes, net	6	(1,613)
<b>Non-cash investing and financing activities:</b>		
Change in deferred taxes, recognized in additional paid-in capital	\$ —	\$ 55
Increase (decrease) in accrued property and equipment purchases	23	3

See accompanying notes to consolidated financial statements.

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FAMOUS DAVE'S OF AMERICA, INC. AND SUBSIDIARIES

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

(1) Basis of Presentation

Basis of Presentation

Famous Dave's of America, Inc. ("Famous Dave's" or the "Company") was incorporated in Minnesota on March 14, 1994. The Company develops, owns, operates and franchises restaurants under the name "Famous Dave's." As of September 30, 2018, there were 147 Famous Dave's restaurants operating in 33 states, the Commonwealth of Puerto Rico, Canada, and the United Arab Emirates, including 16 Company-owned restaurants and 131 franchise-operated restaurants. An additional 63 franchise-operated restaurants were committed to be developed through signed area development agreements as of September 30, 2018.

These consolidated financial statements were prepared in accordance with accounting principles generally accepted in the United States of America ("GAAP") and Securities and Exchange Commission ("SEC") Rules and Regulations. These unaudited consolidated financial statements represent the consolidated financial statements of the Company and its subsidiaries as of September 30, 2018 and December 31, 2017, and for the three and nine months ended September 30, 2018 and October 1, 2017. The information furnished in these consolidated financial statements includes normal recurring adjustments and reflects all adjustments, which are, in the opinion of management, necessary for a fair presentation. Certain information and footnote disclosures normally included in financial statements prepared in accordance with GAAP have been condensed or omitted. These consolidated financial statements should be read in conjunction with the audited consolidated financial statements and notes thereto included in the Company's Annual Report on Form 10 K for the fiscal year ended December 31, 2017 as filed with the SEC on March 5, 2018.

Due to the seasonality of the Company's business, revenue and operating results for the three and nine months ended September 30, 2018 are not necessarily indicative of the results to be expected for the full fiscal year or any other interim period.

Reclassifications

Certain prior period amounts have been reclassified to conform to the current period's presentation. These reclassifications did not have an impact on the reported net income (loss) for any of the periods presented.

Income Taxes

The Company maintains a federal deferred tax asset ("DTA") in the amount of \$6.6 million and \$5.8 million as of September 30, 2018 and December 31, 2017, respectively. The Company evaluates the DTA on a quarterly basis to determine whether current facts and circumstances indicate that the DTA may not be fully realizable. As of September 30, 2018, the Company concluded that the DTA is fully realizable and that a valuation allowance was not considered necessary; however, the Company will continue to evaluate the asset on a quarterly basis until the DTA has been fully utilized.

The following table presents the Company's effective tax rates for the periods presented:

Three Months Ended

Nine Months Ended

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	September 30, 2018		September 30, 2017	
	2018	2017	2018	2017
Effective tax rate	12.3 %	37.9 %	19.8 %	36.9 %

The net decrease in the Company's effective tax rate for the three and nine months ended September 30, 2018 was primarily a result of federal tax reform, signed into law on December 22, 2017, which reduced the Company's federal statutory tax rate to 21%, and adjustments recorded as a result of the finalization of the Company's 2017 tax returns. The Company provides for income taxes based on its estimate of federal and state income tax liabilities. These estimates include, among other items, effective rates for state and local income taxes, allowable tax credits for items such as taxes paid on reported tip income, estimates related to depreciation and amortization expense allowable for tax purposes, and the tax deductibility of certain other items. The Company's estimates are based on the information available at the time that the Company prepares the income tax provision. The Company generally files its annual income tax returns several months after its fiscal year-end. Income tax returns are subject to audit by federal, state, and local governments, generally years after the tax returns are filed. These returns could be subject to material adjustments or differing interpretations of the tax laws.

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FAMOUS DAVE'S OF AMERICA, INC. AND SUBSIDIARIES

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

Restricted cash and marketing fund

The Company has a system-wide marketing development fund, to which Company-owned restaurants, in addition to the majority of franchise-operated restaurants, contribute a percentage of net sales for use in public relations and marketing development efforts. The assets held by this fund are considered to be restricted. Accordingly, the Company reflects the cash related to this fund within restricted cash and reflects the liability within accounts payable on the Company's consolidated balance sheets. The Company had approximately \$1 million and \$1.3 million in this fund as of September 30, 2018 and December 31, 2017, respectively.

In conjunction with the Company's credit agreements, the Company has deposited amounts for undrawn letters of credit in cash collateral accounts. The Company had approximately \$142,000 and \$298,000 in restricted cash as of September 30, 2018 and December 31, 2017, respectively, related to these undrawn letters of credit.

Held to maturity securities

The Company maintains short-term U.S. treasury notes and has classified these investments as held-to-maturity at the time of purchase. Held-to-maturity securities are those securities which the Company has the intent and ability to hold until maturity. Held-to-maturity securities are recorded at amortized cost, adjusted for the amortization or accretion of premiums and discounts. Premiums and discounts are amortized or accreted over the life of the related held-to-maturity security using a straight-line method. As of September 30, 2018, the Company had approximately \$7.0 million of securities, which mature in November, 2018. The carrying value of these securities approximated fair value as of September 30, 2018. The Company did not have held-to-maturity securities at December 31, 2017.

Concentrations of Credit Risk

As of September 30, 2018, the Company had receivables from a franchisee of approximately \$463,000.

Statement of Cash Flows

Effective January 1, 2018, the Company adopted ASU No. 2016-18, "Statement of Cash Flows (Topic 230), Restricted Cash" ("ASU No. 2016-18"). ASU No. 2016-18 provides guidance on the presentation of restricted cash and restricted cash equivalents, which are now included with cash and cash equivalents when reconciling the beginning and ending cash amounts shown on the statements of cash flows. Using the retrospective transition method required under the standard, the Company has adjusted the presentation of its Condensed Consolidated Statements of Cash Flows for all periods presented. The adoption of ASU No. 2016-18 did not have any other impact on the Company's Consolidated Financial Statements.

The following table provides additional details by financial statement line item of the restated presentation in the Company's Condensed Consolidated Statement of Cash Flows for the period impacted:

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(in thousands)	October 1, 2017		As Restated
	As Reported	2016-18 Impact	
Cash flows provided by operating activities:			
Restricted cash	\$ (7)	\$ 7	\$ -
Net cash provided by operating activities	4,484	7	4,491
Net increase in cash, cash equivalents and restricted cash	2,962	7	2,969
Cash, cash equivalents and restricted cash as of the beginning of the period	4,450	1,714	6,164
Cash, cash equivalents and restricted cash as of the end of the period	\$ 7,412	\$ 1,721	\$ 9,133

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FAMOUS DAVE'S OF AMERICA, INC. AND SUBSIDIARIES

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

Recently Adopted Accounting Pronouncements

In May 2014, the Financial Accounting Standards Board ("FASB") issued Accounting Standards Update ("ASU") No. 2014-09, Revenue from Contracts with Customers. The FASB issued ASU No. 2016-08, "Revenue from Contracts with Customers: Principal versus Agent Considerations (Reporting Revenue Gross versus Net)" in March 2016, ASU 2016-10 "Revenue from Contracts with Customers (Topic 606): Identifying Performance Obligations and Licensing" in April 2016, ASU 2016-11, "Revenue Recognition (Topic 605) and Derivatives and Hedging (Topic 815): Rescission of SEC Guidance Because of Accounting Standards Updates 2014-09 and 2014-16 Pursuant to Staff Announcements at the March 3, 2016 EITF Meeting" in May 2016 and ASU 2016-12, "Revenue from Contracts with Customers (Topic 606): Narrow-Scope Improvements and Practical Expedients" in May 2016. These new standards provide for a single, principles-based model for revenue recognition that replaces the existing revenue recognition guidance. In July 2015, the FASB deferred the effective date of ASU 2014-09 until annual and interim periods beginning on or after December 15, 2017. The new guidance permitted the use of either a full retrospective or modified retrospective transition method and early adoption was permitted. The Company has adopted this standard beginning with fiscal year 2018 utilizing the modified retrospective transition method, applied to all contracts.

The new guidance did not impact the timing of revenue recognition on franchise royalty revenues, restaurant and merchandise sales or licensing revenue. Although the recognition of contributions from franchisees to the Company's system-wide Public Relations and Marketing Development Fund (the "NAF") did not change, the Company, beginning in fiscal 2018, now reports these contributions on a gross basis within the franchisee national advertising fund contributions line item on the consolidated statements of operations.

Beginning in fiscal 2018, the Company recognizes franchise fee revenue on a straight-line basis over the life of the related franchise agreements and any exercised renewal periods. Cash payments are due upon the opening of a new restaurant or upon the execution of a renewal of the related franchise agreement. The Company's performance obligation with respect to franchise fee revenues consists of a license to utilize the Company's brand for a specified period of time, which is satisfied equally over the life of each franchise agreement.

Area development fees are deferred until a new restaurant is opened pursuant to the area development agreement, at which time revenue is recognized on a straight-line basis over the life of the franchise agreement. Cash payments for area development agreements are typically due when an area development agreement has been executed. Gift card breakage revenue is recognized proportionately as gift cards are redeemed utilizing an estimated breakage rate based on the Company's historical experience. Gift card breakage revenue is reported within the licensing and other revenue line item of the consolidated statements of operations.

The Company's revenue is generally disaggregated within the consolidated statements of operations; however, within the franchise fee revenue line item of the consolidated statements of operations, the Company recognized approximately \$72,000 and \$185,000 of franchise fee revenue related to the adoption of the new revenue standard during the three and nine months ended September 30, 2018. Gift card breakage revenue was not material to the Company's consolidated financial statements. The Company recognized revenue related to gift cards of approximately \$53,000 and \$229,000 during the three and nine months ended September 30, 2018, which is reflected in the restaurant sales, net, line item of its consolidated statements of operations. As of September 30, 2018, gift cards payable of approximately \$841,000 is expected to be recognized as revenue over the next 12 months, as they are redeemed.

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The following table summarizes the impact of the adoption of the new revenue standard on the Company's previously reported consolidated balance sheets:

(in thousands)	December 31, 2017	New revenue standard adjustments	January 1, 2018
Deferred tax asset, net	\$ 5,823	\$ 579	\$ 6,402
Other current liabilities	3,118	224	3,342
Other liabilities	3,963	2,077	6,040
Retained earnings	11,951	(1,722)	10,229

The increases to other current liabilities and other liabilities relate to deferred franchise fee revenue. The increase to deferred tax asset, net is related to the tax effects of these adjustments to deferred franchise fee revenue. These adjustments resulted in a net decrease to retained earnings as of the adoption date.

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FAMOUS DAVE'S OF AMERICA, INC. AND SUBSIDIARIES

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

Contract liabilities consist of deferred revenue resulting from franchise fees paid by franchisees. We classify these liabilities within other current liabilities and other liabilities within our consolidated balance sheets based on the expected timing of revenue recognition associated with these liabilities. The following table reflects the change in contract liabilities between the date of adoption (January 1, 2018) and September 30, 2018:

(in thousands)

Balance, January 1, 2018           \$ 2,370

Revenue recognized                 (185)

Balance, September 30, 2018   \$ 2,185

The following table illustrates estimated revenues expected to be recognized in the future related to unsatisfied performance obligations as of September 30, 2018:

(in thousands)