

LUBYS INC
Form 10-Q
December 19, 2008
Table of Contents

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 November 19, 2008

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 001-08308

Luby s, Inc.

(Exact name of registrant as specified in its charter)

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Delaware
*(State or other jurisdiction of
incorporation or organization)*

74-1335253
*(IRS Employer
Identification Number)*

13111 Northwest Freeway, Suite 600

Houston, Texas 77040

(Address of principal executive offices, including zip code)

(713) 329-6800

(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 is a large accelerated filer, an accelerated filer, or a non-accelerated filer. See definition of accelerated filer and large accelerated filer in Rule 12b-2 of the Exchange Act (check one):

Large accelerated filer Accelerated filer
Non-accelerated filer 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 December 10, 2008, there were 27,959,618 shares of the registrant's common stock outstanding.

Table of Contents

Lubys, Inc.

Form 10-Q

Quarter ended November 19, 2008

Table of Contents

	Page
<u>Part I - Financial Information</u>	
Item 1 <u>Financial Statements</u>	3
Item 2 <u>Management's Discussion and Analysis of Financial Condition and Results of Operations</u>	17
Item 3 <u>Quantitative and Qualitative Disclosures about Market Risk</u>	25
Item 4 <u>Controls and Procedures</u>	25
<u>Part II - Other Information</u>	
Item 6 <u>Exhibits</u>	26
<u>Signatures</u>	27
<u>Additional Information</u>	

We file reports with the Securities and Exchange Commission, including annual reports on Form 10-K, quarterly reports on Form 10-Q and current reports on Form 8-K. The public may read and copy any materials we file with the SEC's Public Reference Room at 100 F Street, N.E., Washington, D.C. 20549. The public may obtain information on the operation of the Public Reference Room by calling the SEC at 1-800-SEC-0330. We are an electronic filer, and the SEC maintains an Internet site at <http://www.sec.gov> that contains the reports, proxy and information statements, and other information that we file electronically. Our website address is <http://www.lubys.com>. Please note that our website address is provided as an inactive textual reference only. We make available free of charge through our website the annual report on Form 10-K, quarterly reports on Form 10-Q, current reports on Form 8-K, and all amendments to those reports as soon as reasonably practicable after such material is electronically filed with or furnished to the SEC. The information provided on our website is not part of this report, and is therefore not incorporated by reference unless such information is specifically referenced elsewhere in this report.

Table of Contents**Part I - FINANCIAL INFORMATION****Item 1. Financial Statements****Lubys, Inc.****Consolidated Balance Sheets***(In thousands, except share data)*

	November 19, 2008 (Unaudited)	August 27, 2008
ASSETS		
Current Assets:		
Cash and cash equivalents	\$ 2,353	\$ 4,566
Trade accounts and other receivables, net	3,940	3,368
Food and supply inventories	3,993	3,048
Prepaid expenses	2,677	1,627
Deferred income taxes	1,690	1,580
Total current assets	14,653	14,189
Property and equipment, net	197,413	198,118
Long-term investments	8,025	8,525
Property held for sale	6,334	5,282
Other assets	383	407
Total assets	\$ 226,808	\$ 226,521
LIABILITIES AND SHAREHOLDERS' EQUITY		
Current Liabilities:		
Accounts payable	\$ 16,814	\$ 14,268
Accrued expenses and other liabilities	18,594	17,712
Total current liabilities	35,408	31,980
Other liabilities	5,292	6,592
Total liabilities	40,700	38,572
Commitments and Contingencies		
SHAREHOLDERS' EQUITY		
Common stock, \$0.32 par value; 100,000,000 shares authorized; Shares issued were 28,446,443 and 28,439,214, respectively; Shares outstanding were 27,946,443 and 27,939,214, respectively	9,105	9,101
Paid-in capital	20,752	20,405
Retained earnings	161,026	163,218
Less cost of treasury stock, 500,000 shares	(4,775)	(4,775)
Total shareholders' equity	186,108	187,949
Total liabilities and shareholders' equity	\$ 226,808	\$ 226,521

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

Table of Contents**Luby's, Inc.****Consolidated Statements of Operations (unaudited)***(In thousands except per share data)*

	Quarter Ended	
	November 19, 2008 <i>(84 days)</i>	November 21, 2007 <i>(84 days)</i>
SALES:		
Restaurant sales	\$ 65,945	\$ 71,634
Culinary contract services	3,002	1,728
TOTAL SALES	68,947	73,362
COSTS AND EXPENSES:		
Cost of food	18,245	19,657
Payroll and related costs	24,643	24,438
Other operating expenses	16,522	15,744
Opening costs	153	
Cost of culinary contract services	2,660	1,578
Depreciation and amortization	4,365	3,956
General and administrative expenses	6,110	5,968
Provision for asset impairments, net		717
Net (gain) loss on disposition of property and equipment	(210)	316
Total costs and expenses	72,488	72,374
INCOME (LOSS) FROM OPERATIONS	(3,541)	988
Interest income	119	298
Interest expense	(86)	(51)
Interest related to income taxes		1,897
Other income, net	258	182
Income (loss) before income taxes and discontinued operations	(3,250)	3,314
Provision (benefit) for income taxes	(1,107)	(1,494)
Income (loss) from continuing operations	(2,143)	4,808
Discontinued operations, net of income taxes	(49)	(37)
NET INCOME (LOSS)	\$ (2,192)	\$ 4,771
Income (loss) per share from continuing operations:		
Basic	\$ (0.08)	\$ 0.18
Assuming dilution	\$ (0.08)	\$ 0.17
Loss per share from discontinued operations:		
Basic	\$	\$
Assuming dilution	\$	\$
Net income (loss) per share		
Basic	\$ (0.08)	\$ 0.18
Assuming dilution	\$ (0.08)	\$ 0.17
Weighted average shares outstanding:		
Basic	27,944	26,883
Assuming dilution	27,944	27,597

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

Table of Contents**Luby s, Inc.****Consolidated Statement of Shareholders Equity (unaudited)***(In thousands)*

	Common Stock Issued		Common Stock Treasury		Paid-In Capital	Retained Earnings	Total Shareholders Equity
	Shares	Amount	Shares	Amount			
BALANCE AT AUGUST 27, 2008	28,439	\$ 9,101	(500)	\$ (4,775)	\$ 20,405	\$ 163,218	\$ 187,949
Net loss						(2,192)	(2,192)
Common stock issued under nonemployee director benefit plans	7	2			66		68
Share-based compensation expense		2			281		283
BALANCE AT NOVEMBER 19, 2008	28,446	\$ 9,105	(500)	\$ (4,775)	\$ 20,752	\$ 161,026	\$ 186,108

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

Table of Contents**Luby's, Inc.****Consolidated Statements of Cash Flows (unaudited)***(In thousands)*

	Quarter Ended	
	November 19, 2008 (84 days)	November 21, 2007 (84 days)
CASH FLOWS FROM OPERATING ACTIVITIES:		
Net income (loss)	\$ (2,192)	\$ 4,771
Adjustments to reconcile net income (loss) to net cash provided by operating activities:		
Provision for asset impairments, net of gains and losses on property sales	(210)	1,033
Depreciation and amortization	4,365	3,956
Amortization of debt issuance cost	20	21
Non-cash compensation expense	68	57
Share-based compensation expense	283	259
Interest related to income taxes		(1,897)
Deferred tax provision	1,264	2,359
Cash provided by operating activities before changes in operating assets and liabilities	3,598	10,559
Changes in operating assets and liabilities:		
Increase in trade accounts and other receivables, net	(572)	(1,524)
Increase in food and supply inventories	(945)	(1,568)
Increase in prepaid expenses and other assets	(1,070)	(1,460)
Increase in accounts payable, accrued expenses and other liabilities	642	837
Net cash provided by operating activities	1,653	6,844
CASH FLOWS FROM INVESTING ACTIVITIES:		
Proceeds from redemption or maturity of short-term investments		(23,800)
Purchases of short-term investments		2,000
Proceeds from redemption or maturity of long-term investments	500	
Proceeds from disposal of assets and property held for sale	1,111	15
Purchases of property and equipment	(5,477)	(7,888)
Net cash used in investing activities	(3,866)	(29,673)
CASH FLOWS FROM FINANCING ACTIVITIES:		
Proceeds from revolving credit facility	5,000	
Repayments	(5,000)	
Proceeds received on the exercise of stock options		11,200
Net cash provided by financing activities		11,200
Net decrease in cash and cash equivalents	(2,213)	(11,629)
Cash and cash equivalents at beginning of period	4,566	17,514
Cash and cash equivalents at end of period	\$ 2,353	\$ 5,885
Cash paid for:		
Income taxes	\$	\$ 172

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

Table of Contents

Luby s, Inc.

Notes to Consolidated Financial Statements (unaudited)

November 19, 2008

Note 1. Basis of Presentation

The accompanying unaudited consolidated financial statements of Luby s, Inc. (the Company or Luby s) have been prepared in accordance with U.S. generally accepted accounting principles (GAAP) for interim financial information and with the instructions to Form 10-Q and Article 10 of Regulation S-X. Accordingly, they do not include all of the information and footnotes required by GAAP for complete financial statements as they are prepared for the Company s Annual Report on Form 10-K. In the opinion of management, all adjustments (consisting of normal recurring accruals) considered necessary for a fair presentation have been included. Operating results for the period ended November 19, 2008 are not necessarily indicative of the results that may be expected for the fiscal year ending August 26, 2009.

The balance sheet dated August 27, 2008, included in this Form 10-Q, has been derived from the audited financial statements at that date. However, this Form 10-Q does not include all of the information and footnotes required by GAAP for an annual filing of complete financial statements. Therefore, these financial statements should be read in conjunction with the consolidated financial statements and footnotes included in Luby s Annual Report on Form 10-K for the fiscal year ended August 27, 2008.

Certain accounts and prior period results have been reclassified to provide more meaningful comparability to the Company s current presentation.

Note 2. Hurricane Ike

Hurricane Ike struck southeast Texas in September 2008 causing massive power outages and inflicting wide-spread damage in the greater Houston area. Over 40 Luby s locations in the Houston area were closed over varying lengths of time due to the storm. Restaurant sales were negatively impacted by approximately 273 days in the aggregate when some of our locations were unable to open due to storm damage or loss of power. We estimate approximately \$1.5 million in lost sales from these store closures partially offset by post hurricane sales. During the quarter, we incurred direct costs of \$0.9 million for damages, auxiliary power, food loss and other miscellaneous costs. We are seeking to recover a portion of lost profits, property damages, and some expenses incurred through insurance claims.

Note 3. Fair Value Measurement

In September 2006, the Financial Accounting Standards Board (FASB) issued Statement No. 157, *Fair Value Measurements*, which defines fair value, establishes a framework for using fair value to measure assets and liabilities, and expands disclosure about fair value measurements. FAS 157 applies whenever other statements require or permit asset or liabilities to be measured at fair value. The Company adopted the provisions of FAS 157 at the beginning of the first quarter of fiscal year 2009.

FAS 157 establishes a three-tier fair value hierarchy, which prioritizes the inputs used to measure fair value. These tiers include:

Level 1: Defined as observable inputs such as quoted prices in active markets for identical assets or liabilities as of the reporting date. Active markets are those in which transactions for the asset or liability occur in sufficient frequency and volume to provide pricing information on an ongoing basis.

Level 2: Defined as pricing inputs other than quoted prices in active markets included in Level 1, which are either directly or indirectly observable as of the reporting date. Level 2 includes those financial instruments that are valued using models or other valuation methodologies. These models are primarily industry-standard models that consider various assumptions, including quoted forward prices for commodities, time value, volatility factors, and current market and contractual prices for the underlying instruments, as well as other relevant economic measures.

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Level 3: Defined as pricing inputs that are unobservable from objective sources. These inputs may be used with internally developed methodologies that result in management's best estimate of fair value.

Table of Contents

As of November 19, 2008, the Company held auction rate securities which are classified as available-for-sale investments in long-term investments on the balance sheet and are required to be measured at fair value on a recurring basis. As discussed in Note 5 below, the continued illiquidity in the auction rate market has affected the fair market value of the Company's auction rate securities because the auctions continue to fail. Therefore, in absence of an active market, the Company estimated the fair value of these investments using price submissions from traders specializing in the securities. These traders considered, among other items, the collateralization underlying the security, the creditworthiness of the counterparty, the timing of the expected future cash flows, the investments interest rate compared to like investments and the current illiquidity of the investments, and the expectation of the next time the security is expected to have a successful auction.

Although management currently has the intent and believes it has the ability to hold the Company's auction rate securities until maturity or until the securities can be sold for par value, there is no certainty in the long-term. The market for the Company auction rate securities has not been liquid for an extended time and the credit risk of the security issuers and related insurers is uncertain. Therefore, the Company considers the impairment of its auction rate securities to be other-than-temporary.

As a result of the other-than-temporary decline in fair value of the Company's auction rate securities investments, which the Company attributes to liquidity issues rather than credit issues, the Company recorded a realized holding loss of approximately \$0.8 million charge to earnings during the fourth quarter of fiscal year 2008. The securities increased in value during the first quarter of fiscal year 2009. However, any recoveries of previous realized losses will not be recorded until the security is sold. Any future decrease in fair value related to these investments will increase our realized loss.

The assets measured at fair value on a recurring basis subject to the disclosure requirements of FAS 157 at November 19, 2008 were as follows (in thousands):

	Fair Value Measurement at Reporting Date Using		
	Quoted Prices in Active Markets for Identical Assets (Level 1)	Significant Other Observable Inputs (Level 2)	Significant Unobservable Inputs (Level 3)
	<i>(In thousands)</i>		
Auction rate securities investments, par value	\$	\$	\$ 8,850
Total gains or losses (realized and unrealized):			
Included in net income (loss)			(825)
Balance at November 19, 2008	\$	\$	\$ 8,025

Note 4. Accounting Periods

The Company's fiscal year ends on the last Wednesday in August. As such, each fiscal year normally consists of 13 four-week periods, accounting for 364 days. Each of the first three quarters of each fiscal year consists of three four-week periods (12 weeks), while the fourth quarter normally consists of four four-week periods (16 weeks). Comparability between accounting periods will be affected by varying lengths of the periods, as well as the seasonality associated with the restaurant business.

Table of Contents

Note 5. Investments

Short-term Investments

Short-term investments include securities of two types; securities held-to-maturity are reported at amortized cost and available-for-sale securities reported at fair value with unrealized gains and losses excluded from earnings and reported in shareholders' equity unless such losses are considered other than temporary. No realized or unrealized gains or losses were recognized on these investments during the fiscal years ended August 29, 2007 and August 27, 2008. As of November 19, 2008 and August 27, 2008, the Company held no securities as short-term investments.

Long-term Investments

During the first quarter of fiscal year 2009, \$0.5 million of auction rate municipal bonds were called at their par value by the issuer. No gain or loss was recognized. At November 19, 2008, the Company held \$8.85 million, par value (\$8.03 million, net book value) in auction rate municipal bonds as long-term investments. Although the value of the auction rate securities increased during the first quarter of fiscal year 2009, no realized or unrealized gains or losses were recorded.

As of August 27, 2008, the Company recorded \$9.35 million, par value (\$8.53 million, fair value) in auction rate municipal bonds as long-term investments. The adjustment to fair value was recorded in fiscal year 2008 based on the continued illiquidity of the auction rate securities market and a valuation of the securities. The realized \$0.82 million loss is considered other-than-temporary and was recorded as a charge to earnings.

Currently, there are no active markets for the Company's auction rate securities. Therefore, the Company estimated the fair value using price submissions from traders specializing in the securities. Based on price submissions and on the possible long-term illiquidity of the markets, the Company recognized an other than temporary impairment in the fourth quarter of fiscal year 2008.

The auction rate municipal securities are long-term debt obligations that are secured by certain revenue streams (airport, sewer, hospital, etc.). These auction rate securities have insurance policies guaranteeing each of the bonds payment of principal and accrued interest, as scheduled, if the issuer is unable to service the debt and has been issued ratings ranging from A2 Aaa (Moody's) and A AAA (Standard and Poor's). The bonds have experienced this disparity in credit ratings because of the insurance company's revised credit ratings issued by Moody's and Standard and Poor's. If these securities continue to fail at auction, interest income will continue to accrue at a designated benchmark rate plus a premium; otherwise, they will be sold. At each of the resets between February 12, 2008 and November 19, 2008, the Company received all accrued interest due.

When the market stopped normal trading on February 12, 2008 and auctions began overwhelmingly to fail, the Company had sale orders on all of its holdings and all but three of the auctions failed. Of the bonds that were successfully sold, the Company received par value of \$8.3 million plus accrued interest on the bonds.

These municipal bonds have underlying maturity dates ranging from June 1, 2019 through February 1, 2042 and taxable equivalent yield rates ranging from 3.07% to 4.01%. Historically, the auction process allowed investors to obtain immediate liquidity by selling the securities at their face amounts. Liquidity for these securities was historically provided by entering sales orders through a Dutch-auction process that resets interest rates on these investments every 7, 28 or 35 days. However, the disruptions in the credit markets have continued to adversely affect the auction market for these types of securities.

Although the Company intends to hold the investments until liquidity returns to the auction rate securities market or the bonds are called or refunded by the issuer or other types of remedy, the Company has recorded these available-for-sale securities as long-term investments and recorded a realized loss as other-than-temporary impairment in the consolidated statement of operations because auction sell orders have predominantly failed. The length of time required for liquidity to return to the market by normal or other means is uncertain.

Table of Contents**Note 6. Income Taxes**

For the quarter ended November 19, 2008, including both continuing and discontinued operations, the Company generated a gross taxable loss of approximately \$1.5 million. No cash payments of estimated income taxes were made during the first quarter of fiscal year 2009.

Deferred tax assets and liabilities are recorded based on differences between the financial reporting basis and the tax basis of assets and liabilities using currently enacted rates and laws that will be in effect when the differences are expected to reverse. Deferred tax assets are recognized to the extent future taxable income is expected to be sufficient to utilize those assets prior to their expiration. If current available information raises doubt about the realization of the deferred tax assets, a valuation allowance would be necessary. A valuation allowance for deferred tax assets may be required if recovery of prior taxes by carrying back current losses to prior years is not available, if the Company projects lower levels of future taxable income, or if the Company recently experienced consecutive pretax losses. Such a valuation allowance would be established through a charge to income tax expense which would adversely affect the Company's reported operating results. During the first quarter of fiscal year 2009, the Company did not record a charge to establish a valuation allowance against its deferred tax assets.

Management believes that adequate provisions for income taxes have been reflected in the financial statements and is not aware of any significant exposure items that have not been reflected in the financial statements. Amounts considered probable of settlement within one year have been included in the accrued expenses and other liabilities in the accompanying consolidated balance sheet.

Note 7. Property and Equipment

The cost and accumulated depreciation of property and equipment at November 19, 2008 and August 27, 2008, together with the related estimated useful lives used in computing depreciation and amortization, were as follows:

	November 19, 2008	August 27, 2008	Estimated Useful Lives
	<i>(In thousands)</i>		
Land	\$ 53,270	\$ 53,904	
Restaurant equipment and furnishings	122,088	120,426	3 to 15 years
Buildings	182,924	183,385	20 to 33 years
Leasehold and leasehold improvements	20,950	20,923	Lesser of lease term or estimated
			useful life
Office furniture and equipment	6,047	6,029	3 to 10 years
Construction in progress	2,208	880	
	387,487	385,547	
Less accumulated depreciation and amortization	(190,074)	(187,429)	
Property and equipment, net	\$ 197,413	\$ 198,118	

Table of Contents

Note 8. Impairment of Long-Lived Assets and Property Held for Sale

Impairment of Long-Lived Assets and Store Closings

The Company periodically evaluates long-lived assets whenever events or changes in circumstances indicate that the carrying amount of an asset may not be recoverable. The Company estimates future cash flows expected to result from the use and possible disposition of the asset and will recognize an impairment loss when the sum of the undiscounted estimated future cash flows is less than the carrying amounts of such assets. The estimates of future cash flows, based on reasonable and supportable assumptions and projections, require management's subjective judgments. The span of time for which future cash flows are estimated is often lengthy, which increases the sensitivity to assumptions made. Depending on the assumptions and estimates used, the estimated future cash flows projected in the evaluation of long-lived assets can vary within a wide range of outcomes. The Company considers the likelihood of possible outcomes in determining the best estimate of future cash flows. The measurement for such an impairment loss is then based on the fair value of the asset as determined by either discounted cash flows, appraisals or the estimated net proceeds upon sale. With respect to continuing operations, writedowns associated with these impairment analyses, as well as actual exit costs incurred for store closings are reflected in the Provision for Asset Impairments.

Property Held for Sale

At November 19, 2008, the Company had a total of six owned properties and four ground leases recorded at approximately \$6.3 million in property held for sale. The Company is actively marketing the locations currently classified as property held for sale.

In the first quarter of fiscal year 2009, one owned property was sold and removed from property held for sale. Also, in the first quarter of fiscal year 2009, one owned property and one ground lease property were closed and classified as property held for sale.

At August 27, 2008, the Company had a total of six owned properties and three ground leases recorded at approximately \$5.3 million in property held for sale.

Property held for sale consists of already-closed restaurant properties and are valued at the lower of net depreciable value or net realizable value.

The Company's results of discontinued operations will be affected by the disposal of two of the ten properties held for sale to the extent proceeds from the sales exceed or are less than net book value.

Note 9. Commitments and Contingencies

Off-Balance Sheet Arrangements

The Company has no off-balance sheet arrangements.

Pending Claims

Certain current and former hourly restaurant employees filed a lawsuit against us in Texas Federal Court alleging violations of the Fair Labor Standards Act with respect to the inclusion of certain employees in a tip pool. The lawsuit seeks penalties and attorney's fees and was conditionally certified as a collective action in October 2008. We intend to vigorously defend our position. It is not possible at this time to reasonably estimate the possible loss or range of loss, if any.

From time to time, we are subject to various other private lawsuits, administrative proceedings and claims that arise in the ordinary course of our business. A number of these lawsuits, proceedings and claims may exist at any given time. These matters typically involve claims from guests, employees and others related to issues common to the restaurant industry. At this time, management believes that the ultimate resolution of pending legal proceedings will not have a material adverse effect on our results of operations, financial position or cash flows.

Table of Contents

Construction Activity

From time to time, the Company enters into non-cancelable contracts for the construction of its new restaurants. This construction activity exposes the Company to the risks inherent in new construction including but not limited to rising material prices, labor shortages, delays in getting required permits and inspections, adverse weather conditions and injuries sustained by workers.

Note 10. Related Parties

Affiliate Services

The Company's Chief Executive Officer, Christopher J. Pappas, and Chief Operating Officer, Harris J. Pappas, own two restaurant entities (the Pappas entities) that may provide services to the Company and its subsidiaries, as detailed in the Master Sales Agreement dated December 9, 2005 among the Company and the Pappas entities.

Under the terms of the Master Sales Agreement, the Pappas entities may provide specialized (customized) equipment fabrication and basic equipment maintenance, including stainless steel stoves, shelving, rolling carts, and chef tables. The total costs under the Master Sales Agreement of custom-fabricated and refurbished equipment in the first quarter of each of fiscal year 2009 and 2008 were \$150,154 and \$132,117, respectively. The increase in the first quarter of fiscal year 2009 was primarily due to new restaurant openings. Services provided under this agreement are subject to review and approval by the Finance and Audit Committee.

Operating Leases

The Company previously leased property from the Pappas entities, used to accommodate the Company's in-house repair and fabrication center, and was referred to as the Houston Service Center. The Company terminated this lease in August 2008. The Company paid zero and \$13,600, in the first quarter of each of fiscal years 2009 and 2008, respectively, pursuant to the terms of this lease. The Company leases a new property that combines both the offices of the Company's Facility Services and Warehouse Operations, from an unrelated third party. The property is approximately 60,000 square feet.

The Company also previously leased approximately 27,000 square feet of warehouse space from the Pappas entities to complement the Houston Service Center, at a monthly rate of approximately \$0.21 per square foot. The Company paid zero and \$11,118 in the first quarter of each of fiscal years 2009 and 2008, respectively, pursuant to the terms of this lease. On February 29, 2008, the Company terminated this lease with the Pappas entities.

In the third quarter of fiscal 2004, Messrs. Pappas became partners in a limited partnership which purchased a retail strip center in Houston, Texas. Messrs. Pappas collectively own a 50% limited partnership interest and a 50% general partnership interest in the limited partnership. A third party company manages the center. One of the Company's restaurants has rented approximately 7% of the space in that center since July 1969. No changes were made to the Company's lease terms as a result of the transfer of ownership of the center to the new partnership. The Company made payments of \$46,300 and \$43,896 in the first quarter of each of fiscal years 2009 and 2008, respectively, under the lease agreement which currently includes an annual base rate of \$14.64 per square foot.

On November 22, 2006, the Company executed a new lease agreement with respect to this shopping center. Effective upon the Company's relocation and occupancy into the new space in July 2008, the new lease agreement provides for a primary term of approximately 12 years with two subsequent five-year options and gives the landlord an option to buy out the tenant on or after the calendar year 2015 by paying the then unamortized cost of improvements to the tenant. The Company will owe, under the lease, \$16.65 per square foot plus maintenance, taxes, and insurance for the calendar year 2008. Thereafter, the lease provides for reasonable increases in rent at set intervals. The new lease agreement was approved by the Finance and Audit Committee.

Table of Contents

Affiliated rents paid for the Houston Service Center, the separate storage facility and the Houston property leases combined represented 4.0% and 7.5% of total rents for continuing operations for the first quarter of each of fiscal years 2009 and 2008, respectively.

	Quarter Ended	
	November 19, 2008 (84 days)	November 21, 2007 (84 days)
<i>(In thousands, except percentages)</i>		
AFFILIATED COSTS INCURRED:		
General and administrative expenses – professional and other costs	\$ 50	\$ 38
Capital expenditures – custom-fabricated and refurbished equipment and furnishings	150	132
Other operating expenses and opening costs, including property leases	50	77
Total	\$ 250	\$ 247
RELATIVE TOTAL COMPANY COSTS:		
General and administrative expenses	\$ 6,110	\$ 5,968
Capital expenditures	5,477	7,888
Other operating expenses and opening costs	16,675	15,744
Total	\$ 28,262	\$ 29,600
AFFILIATED COSTS INCURRED AS A PERCENTAGE OF		
RELATIVE TOTAL COMPANY COSTS		
Fiscal year to date	0.88%	0.83%

Board of Directors

Pursuant to the terms of a separate Purchase Agreement dated March 9, 2001, entered into by and among the Company, Christopher J. Pappas and Harris J. Pappas, the Company agreed to submit three persons designated by Christopher J. Pappas and Harris J. Pappas as nominees for election at the 2002 Annual Meeting of Shareholders. Messrs. Pappas designated themselves and Frank Markantonis as their nominees for directors, all of whom were subsequently elected. Christopher J. Pappas and Harris J. Pappas are brothers, Frank Markantonis is an attorney whose principal client is Pappas Restaurants, Inc., an entity owned by Harris J. Pappas and Christopher J. Pappas.

As amended in June 2004, the Purchase Agreement allows Messrs. Pappas to continue to nominate persons for election to the board, which, if such nominees are elected, would result in Messrs. Pappas having nominated three of the then-serving directors of the Company. Messrs. Pappas retain their right for so long as they both are executive officers of the Company.

Christopher J. Pappas is a member of the advisory board of Amegy Bank, National Association, which is a lender and syndication agent under the Company's 2007 Revolving Credit Facility.

Table of Contents**Key Management Personnel**

In November 2005, Christopher and Harris Pappas entered into new employment agreements that were subsequently amended in November 2008 to extend the termination date thereof to August 2010. Both continue to devote their primary time and business efforts to the Company while maintaining their roles at Pappas Restaurants, Inc.

Ernest Pekmezaris, the former Chief Financial Officer of the Company, became a consultant to the Company on April 20, 2007. Mr. Pekmezaris is also the Treasurer of Pappas Restaurants, Inc. Compensation for the services provided by Mr. Pekmezaris to Pappas Restaurants, Inc. is paid entirely by that entity.

Peter Tropoli, Senior Vice President, Administration, General Counsel and Secretary of the Company, is an attorney who, in the past, has provided litigation services to entities controlled by Christopher J. Pappas and Harris J. Pappas. Mr. Tropoli is the stepson of Frank Markantonis, who is a director of the Company.

Paulette Gerukos, Vice President of Human Resources of the Company, is the sister-in-law of Harris J. Pappas, the Chief Operating Officer.

Note 11. Share-Based Compensation**Stock Options**

The Company has an Incentive Stock Plan for officers and employees together (Employee Stock Plans) and a Non-employee Director Stock Option Plan for non-employee directors. These plans authorize the granting of stock options, restricted stock and other types of awards consistent with the purpose of the plans. The number of shares authorized for issuance under the Company's plans as of November 19, 2008 totals approximately 2.9 million, of which approximately 1.7 million shares are available for future issuance. Stock options granted under the Incentive Stock Plan and the Non-employee Director Stock Option Plan have an exercise price equal to the market price of the Company's common stock at the date of grant. Option awards under the Employee Stock Plans generally vest 25% each year on the anniversary of the grant date and expire six to ten years from the grant date. Option awards under the Non-employee Director Stock Option Plan generally vest 100% on the first anniversary of the grant date and expire ten years from the grant date.

In connection with their entry into employment agreements effective March 9, 2001, Messrs. Pappas together were granted an aggregate of approximately 2.2 million stock options at an exercise price of \$5.00 per share, which was below the quoted market price on the date of grant. Messrs. Pappas exercised all of these options on October 26, 2007. On March 9, 2001, the Company's Board of Directors unanimously approved the employment agreements and related stock option grants.

A summary of the Company's stock option activity for the quarter ended November 19, 2008 is presented below:

	Shares Under Fixed Options	Weighted-Average Exercise Price	Weighted-Average Remaining Contractual Term (Years)	Aggregate Intrinsic Value (In thousands)
Outstanding at August 27, 2008	689,254	\$ 10.73	3.90	\$ 145
Granted				
Exercised				
Forfeited or Expired				
Outstanding at November 19, 2008	689,254	10.73	3.67	28
Exercisable at November 19, 2008	421,429	\$ 10.60	3.48	\$ 28

Table of Contents**Restricted Stock**

Restricted stock grants consist of the Company's common stock and generally vest after three years, with the exception of grants under the Nonemployee Director Stock Option Plan, which vest when granted due to the fact that they are granted in lieu of a cash payment. All restricted stock grants are cliff-vested. Restricted stock awards are valued at the average market price of the Company's common stock at the date of grant.

A summary of the Company's restricted stock activity during the first quarter of fiscal year 2008 is presented in the following table:

	Restricted Stock Units	Fair Value (Per share)	Weighted-Average Remaining Contractual Term (Years)	Weighted-Average Grant Date
Unvested at August 27, 2008	95,190	\$ 10.04	1.79	6/11/07
Granted	7,229	7.78		10/1/08
Vested	(9,050)	12.30		11/15/05
Unvested at November 19, 2008	93,369	\$ 9.64	1.59	9/11/07

Note 12. Earnings Per Share

Basic net income per share is computed by dividing net income available to common shareholders by the weighted average number of common shares outstanding for the reporting period. Diluted net income per share reflects the potential dilution that could occur if securities or other contracts to issue common stock were exercised or converted into common stock. For the calculation of diluted net income per share, the basic weighted average number of shares is increased by the dilutive effect of restricted stock, phantom stock, and stock options determined using the treasury stock method. Stock options with exercise prices exceeding current market prices that were excluded from the computation of net income per share amounted to approximately 653,000 shares and 249,000 shares for the quarters ended November 19, 2008 and November 21, 2007, respectively.

The components of basic and diluted net income per share are as follows:

	Quarter Ended	
	November 19, 2008 (84 days)	November 21, 2007 (84 days)
	(In thousands, except per share data)	
Numerator:		
Income (loss) from continuing operations	\$ (2,143)	\$ 4,808
Net income (loss)	\$ (2,192)	\$ 4,771
Denominator:		
Denominator for basic earnings per share - weighted-average shares	27,944	26,883
Effect of potentially dilutive securities:		
Employee and non-employee stock options		640
Phantom stock		30
Restricted stock		44
Denominator for earnings per share assuming dilution	27,944	27,597
Income (loss) from continuing operations:		
Basic	\$ (0.08)	\$ 0.18

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Assuming dilution	\$	(0.08)	\$	0.17
Net income (loss) per share:				
Basic	\$	(0.08)	\$	0.18
Assuming dilution	\$	(0.08)	\$	0.17

Table of Contents

Note 13. New Accounting Pronouncements

On August 28, 2008, we adopted SFAS No. 157, Fair Value Measurements, which defines fair value, and SFAS No. 159, the Fair Value Option for Financial Assets and Financial Liabilities including an Amendment of SFAS No. 115, which permits entities to choose to measure many financial instruments and certain other items at fair value. The impact of these statements is reflected on our consolidated financial statements for the first quarter of fiscal year 2009.

In February 2008, the FASB issued FASB Staff Position FAS 157-2, Effective Date of SFAS No. 157, which delayed the effective date of SFAS No. 157 for all non-financial assets and liabilities, except those that are recognized or disclosed at fair value in the financial statements on a recurring basis, until August 27, 2009. We have not yet determined the impact, if any, that the implementation of SFAS 157-2, for non-financial assets and liabilities, will have on our consolidated financial statements.

In December 2007, the FASB issued SFAS No. 141(R), Business Combinations (SFAS 141(R)), which replaces SFAS 141. SFAS 141(R) requires assets and liabilities acquired in a business combination, contingent consideration, and certain acquired contingencies to be measured at their fair values as of the date of acquisition. SFAS 141(R) also requires that acquisition-related costs and restructuring costs be recognized separately from the business combination. SFAS 141(R) is effective for fiscal years beginning after December 15, 2008 and will be effective for business combinations entered into during fiscal year 2010.

In December 2007, the FASB issued SFAS No. 160, Noncontrolling Interests in Consolidated Financial Statements, an Amendment of ARB No. 51 (SFAS 160). SFAS 160 clarifies the accounting for noncontrolling interests and establishes accounting and reporting standards for the noncontrolling interest in a subsidiary, including classification as a component of equity. SFAS 160 is effective for fiscal years beginning after December 15, 2008. The Company does not currently have any minority interests.

In March 2008, the FASB issued SFAS No. 161, Disclosures about Derivative Instruments and Hedging Activities (SFAS 161). SFAS 161 requires entities to provide enhanced disclosures about derivative instruments and hedging activities. SFAS 161 is effective for financial statements issued for fiscal years and interim periods beginning after November 15, 2008. The Company does not currently have any derivative instruments or hedging activities.

In June 2008, the FASB issued FASB Staff Position (FSP) EITF 03-6-1, *Determining Whether Instruments Granted in Share-Based Payment Transactions Are Participating Securities* (FSP EITF 03-6-1). FSP EITF 03-6-1 addresses whether instruments granted in share-based payment transactions are participating securities prior to vesting, and therefore need to be included in the earnings allocation in computing earnings per share under the two-class method as described in SFAS No. 128, *Earnings per Share*. Under the guidance of FSP EITF 03-6-1, unvested share-based payment awards that contain nonforfeitable rights to dividends or dividend equivalents (whether paid or unpaid) are participating securities and shall be included in the computation of earnings-per-share pursuant to the two-class method. FSP EITF 03-6-1 is effective for financial statements issued for fiscal years beginning after December 15, 2008 and all prior-period earnings per share data presented shall be adjusted retrospectively. Early application is not permitted. The Company is assessing the potential impact of this FSP on its earnings per share calculation.

Table of Contents

Item 2. Management's Discussion and Analysis of Financial Condition and Results of Operations

Management's discussion and analysis of financial condition and results of operations should be read in conjunction with the consolidated financial statements and footnotes for the period ended November 19, 2008 included in Item 1 of Part I of this Quarterly Report on Form 10-Q, and the audited financial statements included in our Annual Report on Form 10-K for the fiscal year ended August 27, 2008.

Overview

As of November 19, 2008, we operated 120 restaurants, of which 119 are traditional cafeterias and one primarily serves seafood. These establishments are located in close proximity to retail centers, business developments and residential areas in four states. Of the 120 restaurants, 89 are located on property that we own and 31 are on leased premises.

Accounting Periods

Our fiscal year ends on the last Wednesday in August. As such, each fiscal year normally consists of 13 four-week periods, or accounting periods, accounting for 364 days in the aggregate. Each of the first three quarters of each fiscal year consists of three four-week periods, while the fourth quarter normally consists of four four-week periods. Comparability between quarters may be affected by varying lengths of the quarters, as well as the seasonality associated with the restaurant business.

Same-Store Sales

The restaurant business is highly competitive with respect to food quality, concept, location, price, and service, all of which may have an effect on same-store sales. Our same-store sales calculation measures the relative performance of a certain group of restaurants. To qualify for inclusion in this group, a store must have been in operation for 18 consecutive accounting periods. Stores that close on a permanent basis are removed from the group in the fiscal quarter when operations cease at the restaurant, but remain in the same-store group for previously reported fiscal quarters. Although management believes this approach leads to more effective year-over-year comparisons, neither the time frame nor the exact practice may be similar to those used by other restaurant companies.

Hurricane Ike

Hurricane Ike struck southeast Texas in September 2008 causing massive power outages and inflicting wide-spread damage in the greater Houston area. Over 40 Luby's locations in the Houston area were closed over varying lengths of time due to the storm. Restaurant sales were negatively impacted by approximately 273 days in the aggregate when some of our locations were unable to open due to storm damage or loss of power. We estimate approximately \$1.5 million in lost sales from these store closures which were partially offset by post-hurricane sales. During the quarter, we incurred direct costs of \$0.9 million for damages, auxiliary power, food loss and other miscellaneous costs. We are seeking to recover a portion of lost profits, property damages, and some expenses incurred through insurance claims.

RESULTS OF OPERATIONS

First Quarter Fiscal Year 2009 compared to First Quarter Fiscal Year 2008

Sales

Total sales decreased approximately \$4.4 million, or 6.0%, in the first quarter of fiscal year 2009 compared to the first quarter of fiscal year 2008, consisting of a \$5.7 million decrease in restaurant sales and a \$1.3 million increase in culinary contract services revenue. The \$5.7 million decline in restaurant sales included a \$2.6 million reduction in sales related to closed operations. On a same-store basis, sales decreased approximately \$4.5 million, or 6.7%, due primarily to declines in guest traffic partially offset by higher menu prices. Excluding the lost sales from Hurricane Ike and the estimated unfavorable calendar shift, same-store sales were down 3.8%.

Table of Contents

Cost of Food

Food costs decreased approximately \$1.4 million, or 7.2%, in the first quarter of fiscal year 2009 compared to fiscal year 2008 due to lower sales volumes. As a percentage of restaurant sales, food costs increased 0.3%, to 27.7% in the first quarter of fiscal year 2009 compared to 27.4% in the first quarter of fiscal year 2008, primarily due to increased commodity costs in oils, shortenings, beef, fresh produce and seafood partially offset by higher menu prices.

Payroll and Related Costs

Payroll and related costs increased approximately \$0.2 million in the first quarter of fiscal year 2009 compared to fiscal year 2008 due primarily to higher wage rates. As a percentage of restaurant sales, these costs increased 3.3%, to 37.4% in the first quarter of fiscal year 2009 compared to 34.1% in the first quarter of fiscal year 2008, due to significantly reduced restaurant sales. Payroll and related expenses included higher average wages paid to our crew employees and an increase in staffing among the management teams at the restaurants as well as higher training related costs. First quarter of prior year's payroll and related costs, as a percentage of restaurant sales, benefited by 1.2% from a reduction in workers compensation expense.

Other Operating Expenses

Other operating expenses primarily include restaurant-related expenses for utilities, repairs and maintenance, advertising, insurance, services, supplies and occupancy costs. Other operating expenses increased by approximately \$0.8 million, or 4.9%, in the first quarter of fiscal year 2009 compared to the first quarter of fiscal year 2008. As a percentage of restaurant sales, these costs increased 3.1% to 25.1% in the first quarter of fiscal year 2009 compared to 22.0% in the first quarter of fiscal year 2008. Other operating expenses increased primarily due to Hurricane Ike related expenses.

Opening Costs

Opening costs include labor, supplies, occupancy, and other costs necessary to support the restaurant through its opening period. Opening costs were approximately \$153,000 in the first quarter of fiscal year 2009 compared to the first quarter of fiscal year 2008 and consisted of occupancy costs incurred during the period.

Cost of Culinary Contract Services

Cost of culinary contract services increased by approximately \$1.1 million in the first quarter of fiscal year 2009 compared to the first quarter of fiscal year 2008. This increase was related to the food, labor and other operating expenses associated with the increase in revenue for this business activity.

Depreciation and Amortization

Depreciation and amortization expense increased by approximately \$0.4 million, or 10.4%, in the first quarter of fiscal year 2009 compared to the first quarter of fiscal year 2008 due to the higher depreciable asset base generated by increased capital expenditures in fiscal year 2008, including the opening of three restaurants in fiscal year 2008 as well as upgrades and remodels to existing units.

General and Administrative Expenses

General and administrative expenses include corporate salaries and benefits-related costs, including restaurant area leaders, share-based compensation, professional fees, travel and recruiting expenses and other office expenses. General and administrative expenses increased by approximately \$0.1 million, or 2.4%, in the first quarter of fiscal year 2009 compared to the first quarter of fiscal year 2008. As a percentage of total sales, general and administrative expenses increased to 8.9% in the first quarter of fiscal year 2009 compared to 8.1% in the first quarter of fiscal year 2008. The increase was primarily due to a \$0.4 million increase in corporate salary expense related to staffing costs including severances partially offset by lower professional fees.

Table of Contents

Asset Charges

The provision for asset impairments, net decreased by approximately \$0.7 million in the first quarter of fiscal year 2009 compared with fiscal year 2008. There were no impairments taken in the first quarter of fiscal year 2009. However, in the first quarter of fiscal year 2008, there were write-downs of selected underperforming units to net realizable value based on an estimate of net sales proceeds, partially offset by a reversal of a previously recognized impairment related to one ground lease unit which will be reopened.

The net loss (gain) on disposition of property and equipment increased by approximately \$0.5 million in the first quarter of fiscal year 2009 compared with the first quarter of fiscal year 2008. The loss in the first quarter of fiscal year 2008 included significant retirements of assets that were replaced due to increased remodel activity. The net gain in the first quarter of fiscal year 2009 is the net of normal asset retirement activity offset by the gain on the sale of a closed restaurant property.

Interest Income

Interest income decreased by approximately \$0.2 million primarily related to lower cash and short term investment balances.

Interest Expense

Interest expense remained comparable to the prior quarter.

Interest Related to Income Taxes

The interest related to income taxes in the first quarter of fiscal year 2008 includes the reversal of previously recognized interest expense associated with the settled tax audit contingencies and the interest portion of an income tax refund.

Other Income, Net

Other income, net, consisted primarily of the following components: net rental property income and expenses relating to property for which we are the landlord; prepaid sales tax discounts earned through our participation in state tax prepayment programs; oil and gas royalty income; and de-recognition of gift certificate liability resulting from the expiration of state statutes of limitation on gift certificate amounts. Other income remained comparable to the prior quarter.

Taxes

The net income tax benefit for the first quarter of fiscal year 2009 primarily reflects the tax benefit recognized due to the pre-tax loss in the first quarter of fiscal year 2009 at an effective tax rate of 33.9%. The net income tax benefit for the first quarter of fiscal year 2008 included \$2.8 million in nonrecurring net tax benefit partially offset by \$1.3 million in income tax expense at an effective tax rate of 38.5%. The net income tax benefit of \$2.8 million included a reversal of tax accruals for contingencies that did not materialize following the completion of tax audits and an income tax refund receivable, partially offset by the reversal of unrealized deferred tax assets related to stock options.

Discontinued Operations

The loss from discontinued operations remained comparable to the prior quarter.

Table of Contents**LIQUIDITY AND CAPITAL RESOURCES*****Cash and Cash Equivalents***

General. Our primary sources of short-term and long-term liquidity are cash flows from operations and our revolving credit facility.

Our cash requirements consist principally of:

capital expenditures for new store development and construction, restaurant renovations and upgrades and information technology; and

working capital.

A continued decline in our cash flow from operations could require us to utilize our credit facility. Under the current terms of our revolving credit facility, capital expenditures and the amount of borrowings are limited based on our trailing cash flows, as defined in the agreement. Based upon current levels of operations and anticipated growth, we expect that cash flows from operations, combined with other financing alternatives in place or available, will be sufficient to meet our capital expenditures and working capital requirements during the next twelve months.

As is common in the restaurant industry, we maintain relatively low levels of accounts receivable and inventories, and our vendors grant trade credit for purchases such as food and supplies. We also continually invest in our business through the addition of new units and refurbishment of existing units, which are reflected as long-term assets.

Cash and cash equivalents decreased to \$2.4 million from \$4.6 million at the beginning of the fiscal year. This decrease is primarily due to a decrease in cash provided by operating activities. We generally reinvest available cash flows from operations to develop new restaurants or enhance existing restaurants.

The following table summarizes our cash flows from operating, investing and financing activities:

	Quarter Ended	
	November 19, 2008 (84 days)	November 21, 2007 (84 days) (In thousands)
Total cash provided by (used in):		
Operating activities	\$ 1,653	\$ 6,844
Investing activities	(3,866)	(29,673)
Financing activities		11,200
Decrease in cash and cash equivalents	\$ (2,213)	\$ (11,629)

Operating Activities. In the first quarter of fiscal year 2009, operating cash flow decreased \$5.2 million to \$1.7 million compared to the first quarter of fiscal year 2008, primarily due to a decline in restaurant sales and increased restaurant expenses and general and administrative expenses.

Investing Activities. Cash flows used in investing activities were \$3.9 million in the first quarter of fiscal year 2009 compared to \$29.7 million in the first quarter of fiscal year 2008, primarily due to decreased purchases of property and equipment, which includes new restaurant construction in progress. Our capital expenditure program includes, among other things, investments in new locations, restaurant remodeling, and information technology enhancements. We used \$5.5 million for purchases of property and equipment in the first quarter of fiscal year 2009 compared to \$7.9 million in the first quarter of fiscal year 2008. We expect to spend approximately \$12.0 million to \$17.0 million on capital expenditures in fiscal year 2009.

Table of Contents

Financing Activities. Cash provided by financing activities decreased \$11.2 million to zero, compared to the first quarter of fiscal year 2008, due primarily to the nonrecurrence of proceeds from the exercise of stock options. Borrowings under the revolver during the first quarter of fiscal year 2009 were repaid prior to November 19, 2008.

Status of Long-Term Investments and Liquidity

At November 19, 2008, we held \$8.85 million, par value (\$8.03 million, net book value) in auction rate municipal bonds as long-term investments. These securities are long-term bonds with underlying maturities in years 2019 through 2042 but have historically had short-term features intended for the investor's liquidity. Prior to the collapse of the auction rate securities market in February 2008, these bonds were purchased or sold through a Dutch-auction process in short-term intervals of 7, 28 or 35 dayceeff" style="background:#CCEEFF;padding:0in 0in 0in;width:85.0%;">

Total Net Acreage

223,433

2004 Capex Budget (\$mm)

\$

35

Wells to Be Drilled

55

Piceance / Uintah Basins Geology and Opportunities

[GRAPHIC]

Development drilling

Stepout drilling

Infill drilling

Exploration drilling

Recompletions of existing zones

New zone additions

Canada - Overview

[GRAPHIC]

Average Working Interest		63%
Operator		EVG, et al
Proved Reserves 12/31/03 (Bcfe)		37
% PUD		28%
% Gas		88%
Daily Production Since Acquisition (MMcfe/d)		11
R/P (Years)		9
Net Developed Acreage		44,728
Net Undeveloped Acreage		60,106
Total Acreage		104,834
2004 Capex Budget (\$mm)	\$	34
Wells to Be Drilled		65

Canada Geology and Opportunities

[GRAPHIC]

Development drilling

Stepout drilling

Infill drilling

Exploration drilling

Recompletions of existing zones

New zone additions

Conventional & unconventional reservoirs

Kansas - Overview

Total Net Acreage: 746,000

[GRAPHIC]

Kansas Geology and Opportunities

[GRAPHIC]

Perfect fit with business strategy of acquiring and developing unconventional natural gas properties in North America

Prospective pay zones include:

12+ coals

6+ shales

3 - 6 sands

60+ wells drilled in 2004

Approximately 100 wells in production testing by 12/31/04

Alaska's Cook Inlet Basin

[GRAPHIC]

Established Conventional Gas:

Discovered 1957

Declining gas supply in this region

6.2 Tcf produced to date

Cook Inlet Basin Resource

1.5 trillion tons coal possible

200 Tcf CBM resource possible

Pioneer Unit acquired in 2001

Evergreen Expands Acreage in 2003

5 core holes drilled to test gas quality

Financial Overview

27

\$200 Million Senior Subordinated Notes

Issuer:	Evergreen Resources, Inc.
Amount:	\$200 million
Form:	Senior Subordinated Notes
Distribution:	144A / Reg S offering (with registration rights)
Maturity:	8 Years (2012)
Mandatory Redemption:	Change of control put at 101%
Optional Redemption:	Non-callable for 4 years; 3-year equity claw back: 35% of issue at a premium of par plus coupon
Use of Proceeds:	Repay existing bank debt and general corporate purposes
Ratings:	Ba3 / BB-
Interest Rate:	5 7/8%, yield 6%

Hedging Position

Remaining Contract Period	Market	Volume in Mcf/day	Weighted Average \$/Mcf
Apr 04 Oct 04	Midcontinent	65,000	4.86
Apr 04 Dec 04	Midcontinent	50,000	4.20
Apr 04 Dec 04	Northwest Pipeline	3,000	4.33
Apr 04 Dec 04	AECO Canada	4,739	4.63
Oct 04	Midcontinent	10,000	5.79
Nov 04 Dec 04	Midcontinent	50,000	5.89
Jan 05 Dec 05	Midcontinent	100,000	5.14

Corporate Performance

Consistently Ranked as an Industry Leader in:

Low Finding and Development Costs

Reserve Per Share Growth

Production Per Share Growth

Recycle Ratio (Full Cycle Economics)

Historical Financial Performance

Net Income(1)

[CHART]

Funds From Operations(2)

[CHART]

(1) **2002 net income adjusted for after-tax impairment of international properties.**

(2) **Defined as cash flow from operations before changes in working capital.**

Components of Growth

Reserve Replacement

[CHART]

Finding and Development Costs(1), (2)

[CHART]

-
- (1) **Includes capital spending on gathering and compression system.**
 - (2) **2003 costs exclude \$33.4 million deferred tax gross-up associated with Carbon acquisition.**

Low cost Structure / High Profitability

Lease Operating Expenses

[CHART]

Efficiency Ratio(1)

[CHART]

(1) **Efficiency Ratio = Netback / F&D costs from all sources.**

Proven Reserves

(In Trillion Cubic Feet Equivalent)

[CHART]

* Includes Carbon Energy

2004 Drilling Program

Gross Wells Drilled	Q1 (a)	Q2 (e)	Q3 (e)	Q4 (e)	Total (e)
Raton Basin	47	64	52	37	200
Kansas	12	10	20	19	61
Piceance/Uintah	5	15	20	15	55
Canada	2	18	32	13	65
Total Wells	66	107	124	84	381
Total Wells w/o Kansas	54	97	104	65	320

2004 Capital Budget

(In Millions of Dollars)

	Q1a	Q2e	Q3e	Q4e	2004e
Raton Basin:					
Drilling and completion	\$ 15.2	\$ 14.2	\$ 11.9	\$ 8.5	\$ 49.8
Collection and compression	7.5	10.5	7.7	6.1	31.8
Equipment	1.8	3.8	1.4	0.3	7.3
Other costs	6.1	5.7	4.8	3.0	19.6
Total Raton Basin	\$ 30.6	\$ 34.2	\$ 25.8	\$ 17.9	\$ 108.5
Piceance/Uintah	2.6	12.6	15.0	4.5	34.7
Canada	7.3	13.3	6.7	6.5	33.8
Alaska & Others	\$ 2.7	1.7	1.0	1.0	6.4
Total Kansas costs	\$ 7.3	\$ 12.5	\$ 10.9	\$ 5.9	\$ 36.6
Total Capital Budget	\$ 50.5	\$ 74.3	\$ 59.4	\$ 35.8	\$ 220.0
Total Capital Budget w/o KS	\$ 43.2	\$ 61.8	\$ 48.5	\$ 29.9	\$ 183.4

Highlights

Nearly 100% of Proven Reserves and Production are Nat. Gas

Almost 100% Operated

Fully Integrated Operations and Services

Established Track Record of Predictable Reserve Growth

Large Inventory of Highly Prospective Future Drilling Locations

Raton Basin CBM only about 50% Drilled

Excellent Well Economics with Proven Low Cost Model

Expanding to Other Areas with Extensive Upside Potential

1000 s of Prospective Locations if Other Areas Successful

Predictable Performance and Growing Net Asset Value

Announced Merger with PXD Creates Corporate and Operating Synergies

The proposed merger will be submitted to each of Pioneer's and Evergreen's stockholders for their consideration, and Pioneer will file with the SEC a registration statement containing the joint proxy statement prospectus to be used by Pioneer to solicit approval of its stockholders to issue additional stock in the merger and to be used by Evergreen to solicit the approval of its stockholders for the proposed merger. Pioneer will also file other documents concerning the proposed merger. You are urged to read the registration statement and the joint proxy statement prospectus regarding the proposed merger when they become available and any other relevant documents filed with the SEC, as well as any amendments or supplements to those documents, because they will contain important information. You will be able to obtain a free copy of the joint proxy statement prospectus including the registration statement, as well as other filings containing information about Pioneer at the SEC's Internet Site (<http://www.sec.gov>). Copies of the joint proxy statement prospectus can also be obtained without charge, by directing a request to: Susan Spratlen; 5205 N. O'Connor Blvd, Suite 900, Irving, Texas 75039; 972-969-3583

Pioneer and its directors and executive officers may be deemed to be participants in the solicitation of proxies from the stockholders of Pioneer in connection with the proposed merger. Evergreen and its directors and executive officers may be deemed to be participants in the solicitation of proxies from the stockholders of Evergreen in connection with the proposed merger. Additional information regarding the interests of those participants may be obtained by reading the joint proxy statement prospectus regarding the proposed merger when it becomes available.

[GRAPHIC]

Recognized Leader in Coal Bed Methane
Technology & Development

EVERGREEN RESOURCES, INC.

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Legal Information

This filing contains forward-looking statements within the meaning of federal securities laws, including statements regarding, among other things, Evergreen's growth strategies; anticipated trends in Evergreen's business and its future results of operations; market conditions in the oil and gas industry; the ability of the company to make and integrate acquisitions; and the impact of government regulations. These forward-looking statements are based largely on Evergreen's expectations and are subject to a number of risks and uncertainties, many of which are beyond Evergreen's control. Actual results could differ materially from those implied by these forward-looking statements as a result of, among other things, a decline in natural gas production, a decline in natural gas prices, incorrect estimations of required capital expenditures, increases in the cost of drilling, completion and gas collection, an increase in the cost of production and operations, an inability to meet projections, and/or changes in general economic conditions. In light of these and other risks and uncertainties of which Evergreen may be unaware or which Evergreen currently deems immaterial, there can be no assurance that actual results will be as projected in the forward-looking statements. These and other risks and uncertainties are described in more detail in Evergreen's most recent Annual Report on Form 10-K filed with the Securities and Exchange Commission.

This filing also contains forward looking statements regarding Evergreen's proposed merger with a wholly owned subsidiary of Pioneer Natural Resources. Forward-looking statements relating to expectations about future results or events regarding the proposed merger are based upon information available to Evergreen as of today's date, and Evergreen does not assume any obligation to update any of these statements. The forward-looking statements are not guarantees of the future performance of Pioneer, Evergreen or the combined company, and actual results may vary materially from the results and expectations discussed. For instance, although Pioneer and Evergreen have signed an agreement for a subsidiary of Pioneer to merge with Evergreen, there is no assurance that they will complete the proposed merger. The merger agreement will terminate if the companies do not receive necessary approval of each of Pioneer's and Evergreen's stockholders or government approvals or fail to satisfy conditions to closing. Additional risks and uncertainties related to the proposed merger include, but are not limited to, conditions in the financial markets relevant to the proposed merger, the successful integration of Evergreen into Pioneer's business, and each company's ability to compete in the highly competitive oil and gas exploration and production industry. The revenues, earnings and business prospects of Pioneer, Evergreen and the combined company and their ability to achieve planned business objectives will be subject to a number of risks and uncertainties. These risks and uncertainties include, among other things, volatility of oil and gas prices, product supply and demand, competition, government regulation or action, foreign currency valuation changes, foreign government tax and regulation changes, litigation, the costs and results of drilling and operations, Pioneer's and Evergreen's ability to replace reserves, implement its business plans, or complete its development projects as scheduled, access to and cost of capital, uncertainties about estimates of reserves, quality of technical data, environmental and weather risks, acts of war or terrorism. These and other risks are identified from time to time in Pioneer's and Evergreen's SEC reports and public announcements.

The proposed merger of Evergreen with a wholly owned subsidiary of Pioneer will be submitted to each of Pioneer's and Evergreen's stockholders for their consideration, and Pioneer will file with the SEC a registration statement containing the joint proxy statement prospectus to be used by Pioneer to solicit approval of its stockholders to issue additional stock in the merger and to be used by Evergreen to solicit the approval of its

stockholders for the proposed merger. Pioneer and Evergreen will also file other documents concerning the proposed merger. You are urged to read the registration statement and the joint proxy statement prospectus regarding the proposed merger when they become available and any other relevant documents filed with the SEC, as well as any amendments or supplements to those documents, because they will contain important information. You will be able to obtain a free copy of the joint proxy statement prospectus including the registration statement, as well as other filings containing information about Evergreen at the SEC's Internet Site (<http://www.sec.gov>). Copies of the joint proxy statement prospectus can also be obtained, without charge, by directing a request to Evergreen Resources, Inc., John B. Kelso, 1401 17th Street, Suite 1200, Denver, Colorado 80202, or via telephone at 303-298-8100.

Evergreen and its directors and executive officers may be deemed to be participants in the solicitation of proxies from the stockholders of Evergreen in connection with the proposed merger. Pioneer and its directors and executive officers may be deemed to be participants in the solicitation of proxies from the stockholders of Pioneer in connection with the proposed merger. Additional information regarding the interests of those participants may be obtained by reading the joint proxy statement prospectus regarding the proposed merger when it becomes available.
