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Fiesta Restaurant Group, Inc.

Form 10-Q

August 06, 2018

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**UNITED STATES
SECURITIES AND EXCHANGE COMMISSION
WASHINGTON, DC 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 July 1, 2018

OR

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

Commission File Number: 001-35373

FIESTA RESTAURANT GROUP, INC.

(Exact name of Registrant as specified in its charter)

Delaware

(State or other jurisdiction of
incorporation or organization)

90-0712224

(I.R.S. Employer
Identification No.)

14800 Landmark Boulevard, Suite 500

75254

Dallas, Texas

(Address of principal executive office)

(Zip Code)

Registrant's telephone number, including area code: (972) 702-9300

Indicate by check mark whether the registrant (1) has filed all reports required to be filed by Section 13 or 15(d) of the Securities Exchange Act of 1934 during the preceding 12 months (or for such shorter period that the registrant was required to file such reports), and (2) has been subject to such filing requirements for the past 90 days. Yes No

Indicate by check mark whether the registrant has submitted electronically and posted on their Corporate Web site, if any, every Interactive Data File required to be submitted and posted pursuant to Rule 405 of Regulation S-T during the preceding 12 months (or for such shorter period that the registrant was required to submit and post such files). Yes No

Indicate by check mark whether the registrant is a large accelerated filer, an accelerated filer, a non-accelerated filer, a smaller reporting company, or an emerging growth company. See the definitions 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 (Do not check if smaller reporting company)

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.

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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 August 1, 2018, Fiesta Restaurant Group, Inc. had 27,266,023 shares of its common stock, \$.01 par value, outstanding.

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CONDENSED CONSOLIDATED FINANCIAL STATEMENTS
QUARTER ENDED JULY 1, 2018**

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	July 1, 2018	December 31, 2017
ASSETS		
Current assets:		
Cash	\$4,698	\$ 3,599
Accounts receivable	13,517	9,830
Inventories	2,602	2,880
Prepaid rent	3,315	3,300
Income tax receivable	4,662	11,334
Prepaid expenses and other current assets	8,292	10,105
Total current assets	37,086	41,048
Property and equipment, net	239,647	234,561
Goodwill	123,484	123,484
Deferred income taxes	15,091	17,232
Other assets	7,511	6,988
Total assets	\$422,819	\$ 423,313
LIABILITIES AND STOCKHOLDERS' EQUITY		
Current liabilities:		
Current portion of long-term debt	\$ 103	\$ 98
Accounts payable	18,198	20,293
Accrued payroll, related taxes and benefits	11,729	11,776
Accrued real estate taxes	4,581	5,860
Other liabilities	15,666	21,817
Total current liabilities	50,277	59,844
Long-term debt, net of current portion	74,691	76,425
Deferred income—sale-leaseback of real estate	21,664	23,466
Other liabilities	29,983	32,062
Total liabilities	176,615	191,797
Commitments and contingencies		
Stockholders' equity:		
Common stock, par value \$.01; authorized 100,000,000 shares, issued 27,267,752 and 27,086,958 shares, respectively, and outstanding 26,919,479 and 26,847,458 shares, respectively.	270	268
Additional paid-in capital	168,727	166,823
Retained earnings	78,159	64,425
Treasury stock, at cost; 42,905 shares	(952)	—
Total stockholders' equity	246,204	231,516
Total liabilities and stockholders' equity	\$422,819	\$ 423,313

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

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FIESTA RESTAURANT GROUP, INC.
CONDENSED CONSOLIDATED STATEMENTS OF OPERATIONS
THREE AND SIX MONTHS ENDED JULY 1, 2018 AND JULY 2, 2017
(In thousands of dollars, except share and per share amounts)
(Unaudited)

	Three Months Ended		Six Months Ended	
	July 1, 2018	July 2, 2017	July 1, 2018	July 2, 2017
Revenues:				
Restaurant sales	\$ 176,152	\$ 172,005	\$ 344,985	\$ 346,982
Franchise royalty revenues and fees	675	619	1,326	1,249
Total revenues	176,827	172,624	346,311	348,231
Costs and expenses:				
Cost of sales	56,689	50,728	110,254	101,676
Restaurant wages and related expenses (including stock-based compensation expense of \$33, (\$74), \$50 and \$35, respectively)	47,677	46,269	94,160	94,401
Restaurant rent expense	8,840	8,915	17,732	18,777
Other restaurant operating expenses	24,654	24,636	48,104	48,704
Advertising expense	5,361	4,292	11,574	11,831
General and administrative (including stock-based compensation expense of \$984, \$1,248, \$1,856 and \$1,785, respectively)	12,820	18,996	27,739	34,694
Depreciation and amortization	9,170	8,596	18,169	17,782
Pre-opening costs	877	910	1,258	1,334
Impairment and other lease charges	784	10,762	122	43,176
Other expense (income), net	(3,545)	) 798	(3,179)	) 1,252
Total operating expenses	163,327	174,902	325,933	373,627
Income (loss) from operations	13,500	(2,278)	) 20,378	(25,396)
Interest expense	986	654	2,055	1,238
Income (loss) before income taxes	12,514	(2,932)	) 18,323	(26,634)
Provision for (benefit from) income taxes	3,021	(772)	) 4,646	(9,414)
Net income (loss)	\$ 9,493	\$ (2,160)	) \$ 13,677	\$ (17,220)
Basic net income (loss) per share	\$ 0.35	\$ (0.08)	) \$ 0.50	\$ (0.64)
Diluted net income (loss) per share	\$ 0.35	\$ (0.08)	) \$ 0.50	\$ (0.64)
Basic weighted average common shares outstanding	26,916,295	26,815,015	26,895,302	26,794,560
Diluted weighted average common shares outstanding	26,919,914	26,815,015	26,901,829	26,794,560

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

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FIESTA RESTAURANT GROUP, INC.
CONDENSED CONSOLIDATED STATEMENTS OF CHANGES IN STOCKHOLDERS' EQUITY
SIX MONTHS ENDED JULY 1, 2018 AND JULY 2, 2017
(In thousands of dollars, except share amounts)
(Unaudited)

	Number of Common Stock Shares	Common Stock	Additional Paid-In Capital	Retained Earnings	Treasury Stock	Total Stockholders' Equity
Balance at January 1, 2017	26,755,640	\$ 267	\$ 163,204	\$ 100,704	\$ —	\$ 264,175
Stock-based compensation	—	—	1,820	—	—	1,820
Vesting of restricted shares	79,497	1	—	—	—	1
Cumulative effect of adopting a new accounting standard	—	—	73	(47)	—	26
Net loss	—	—	—	(17,220)	—	(17,220)
Balance at July 2, 2017	26,835,137	\$ 268	\$ 165,097	\$ 83,437	\$ —	\$ 248,802
Balance at December 31, 2017	26,847,458	\$ 268	\$ 166,823	\$ 64,425	\$ —	\$ 231,516
Stock-based compensation	—	—	1,906	—	—	1,906
Vesting of restricted shares	114,926	2	(2)	—	—	—
Cumulative effect of adopting a new accounting standard (Note 1)	—	—	—	57	—	57
Purchase of treasury stock	(42,905)	—	—	—	(952)	(952)
Net income	—	—	—	13,677	—	13,677
Balance at July 1, 2018	26,919,479	\$ 270	\$ 168,727	\$ 78,159	\$ (952)	\$ 246,204

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

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FIESTA RESTAURANT GROUP, INC.
CONDENSED CONSOLIDATED STATEMENTS OF CASH FLOWS
SIX MONTHS ENDED JULY 1, 2018 AND JULY 2, 2017
(In thousands of dollars)
(Unaudited)

	Six Months Ended	
	July 1, 2018	July 2, 2017
Cash flows from operating activities:		
Net income (loss)	\$13,677	\$(17,220)
Adjustments to reconcile net income to net cash provided by operating activities:		
(Gain) loss on disposals of property and equipment	(930)	931
Stock-based compensation	1,906	1,820
Impairment and other lease charges	122	43,176
Depreciation and amortization	18,169	17,782
Amortization of deferred financing costs	135	154
Amortization of deferred gains from sale-leaseback transactions	(1,799)	(1,803)
Deferred income taxes	2,141	(14,646)
Changes in other operating assets and liabilities	(7,088)	5,232
Net cash provided by operating activities	26,333	35,426
Cash flows from investing activities:		
Capital expenditures:		
New restaurant development	(12,051)	(18,796)
Restaurant remodeling	(299)	(961)
Other restaurant capital expenditures	(10,026)	(3,587)
Corporate and restaurant information systems	(4,912)	(2,809)
Total capital expenditures	(27,288)	(26,153)
Proceeds from disposals of properties	4,676	—
Proceeds from insurance recoveries	531	—
Net cash used in investing activities	(22,081)	(26,153)
Cash flows from financing activities:		
Borrowings on revolving credit facility	15,000	5,000
Repayments on revolving credit facility	(17,000)	(14,000)
Principal payments on capital leases	(51)	(43)
Financing costs associated with issuance of debt	(150)	—
Payments to purchase treasury stock	(952)	—
Net cash used in financing activities	(3,153)	(9,043)
Net increase in cash	1,099	230
Cash, beginning of period	3,599	4,196
Cash, end of period	\$4,698	\$4,426
Supplemental disclosures:		
Interest paid on long-term debt	\$1,515	\$1,149
Interest paid on lease financing obligations	—	71
Accruals for capital expenditures	6,437	5,872
Income tax payments (refunds), net	(4,150)	2,486
Capital lease obligations incurred	322	—

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

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FIESTA RESTAURANT GROUP, INC.

NOTES TO UNAUDITED CONDENSED CONSOLIDATED FINANCIAL STATEMENTS

(In thousands of dollars, except share and per share amounts)

1. Basis of Presentation

Business Description. Fiesta Restaurant Group, Inc. ("Fiesta Restaurant Group" or "Fiesta") owns, operates and franchises two restaurant brands through its wholly-owned subsidiaries Pollo Operations, Inc. and its subsidiaries, Pollo Franchise, Inc. (collectively "Pollo Tropical") and Taco Cabana, Inc. and its subsidiaries (collectively "Taco Cabana"). Unless the context otherwise requires, Fiesta and its subsidiaries, Pollo Tropical and Taco Cabana, are collectively referred to as the "Company". At July 1, 2018, the Company owned and operated 150 Pollo Tropical® restaurants and 170 Taco Cabana® restaurants. The Pollo Tropical restaurants included 141 located in Florida and 9 located in Georgia. All of the Taco Cabana restaurants are located in Texas. At July 1, 2018, the Company franchised a total of 30 Pollo Tropical restaurants and eight Taco Cabana restaurants. The franchised Pollo Tropical restaurants included 17 in Puerto Rico, four in Panama, two in Guyana, one in the Bahamas, and six on college campuses and at a hospital in Florida. The franchised Taco Cabana restaurants included six in New Mexico and two on college campuses in Texas.

Basis of Consolidation. The unaudited condensed consolidated financial statements presented herein reflect the consolidated financial position, results of operations and cash flows of Fiesta and its wholly-owned subsidiaries. All intercompany transactions have been eliminated in consolidation.

Fiscal Year. The Company uses a 52-53 week fiscal year ending on the Sunday closest to December 31. The fiscal year ended December 31, 2017 contained 52 weeks. The three and six months ended July 1, 2018 and July 2, 2017 each contained thirteen and twenty-six weeks, respectively. The fiscal year ending December 30, 2018 will contain 52 weeks.

Basis of Presentation. The accompanying unaudited condensed consolidated financial statements for the three and six months ended July 1, 2018 and July 2, 2017 have been prepared without an audit pursuant to the rules and regulations of the Securities and Exchange Commission and do not include certain information and footnotes required by U.S. Generally Accepted Accounting Principles ("GAAP") for complete financial statements. In the opinion of management, all normal and recurring adjustments considered necessary for a fair presentation of such financial statements have been included. The results of operations for the three and six months ended July 1, 2018 and July 2, 2017 are not necessarily indicative of the results to be expected for the full year.

These unaudited condensed consolidated financial statements should be read in conjunction with the consolidated financial statements and notes thereto for the year ended December 31, 2017 included in the Company's Annual Report on Form 10-K for the fiscal year ended December 31, 2017. The December 31, 2017 balance sheet data is derived from those audited financial statements.

Reclassification. Write-offs of site development costs were reclassified from general and administrative expense to other expense (income), net in the condensed consolidated statement of operations to conform with the current year presentation.

Guidance Adopted in 2018. In May 2014, and in subsequent updates, the Financial Accounting Standards Board ("FASB") issued Accounting Standards Update ("ASU") No. 2014-09, Revenue from Contracts with Customers (Topic 606), which supersedes the guidance in former Topic 605, Revenue Recognition, and requires entities to recognize revenue when control of the promised goods or services is transferred to customers at an amount that reflects the consideration to which the entity expects to be entitled to in exchange for those goods or services. The Company adopted this new accounting standard and all the related amendments as of January 1, 2018 using the modified retrospective method, and recognized a total cumulative effect adjustment to increase retained earnings by less than \$0.1 million, which consisted of a \$0.3 million increase related to gift card breakage and a \$0.3 million decrease related to initial franchise and area development fees, as a result of adopting the standard. The new standard did not impact the Company's recognition of revenue from Company-owned and operated restaurants or its recognition of sale-based royalties from restaurants operated by franchisees. The comparative period information has not been

restated and continues to be reported under the accounting standard in effect for those periods. When compared to the previous accounting policies, the impact of adopting the new standard was immaterial to current and long-term other liabilities and retained earnings at January 1, 2018 and to net income for the three and six months ended July 1, 2018. The adoption of the new standard had no impact on the Company's consolidated statements of cash flows.

Revenue Recognition. Revenue is recognized upon transfer of promised products or services to customers in an amount that reflects the consideration the Company received in exchange for those products or services. Revenues from the Company's owned and operated restaurants are recognized when payment is tendered at the time of sale. Franchise royalty revenues are based on a percent of gross sales and are recorded as income when earned. Initial franchise fees and area development fees associated with new franchise agreements are not distinct from the continuing rights and services offered by the Company during the term of the related franchise agreements and are recognized as income over the term of the related franchise agreements. A portion of the

Table of Contents**FIESTA RESTAURANT GROUP, INC.****NOTES TO UNAUDITED CONDENSED CONSOLIDATED FINANCIAL STATEMENTS—(Continued)**

(In thousands of dollars, except share and per share amounts)

initial franchise fee is allocated to training services and is recognized as revenue when the Company completes the training services. Prior to adopting Topic 606, the Company recognized initial franchise fees as revenue in the period that a franchised location opened for business. See Note 6 - Business Segment Information.

Gift cards. The Company sells gift cards to its customers in its restaurants and through select third parties. The Company recognizes revenue from gift cards upon redemption by the customer. For unredeemed gift cards that the Company expects to be entitled to breakage, the Company recognizes expected breakage as revenue in proportion to the pattern of redemption by the customers. The gift cards have no stated expiration dates. Revenues from unredeemed gift cards and gift card liabilities, which are recorded in other current liabilities, are not material to the Company's financial statements. Prior to adopting Topic 606, the Company did not recognize breakage on its gift cards.

Fair Value of Financial Instruments. Fair value is defined as the price that would be received to sell an asset or paid to transfer a liability in an orderly transaction between market participants at the measurement date under current market conditions. In determining fair value, the accounting standards establish a three level hierarchy for inputs used in measuring fair value as follows: Level 1 inputs are quoted prices in active markets for identical assets or liabilities; Level 2 inputs are observable for the asset or liability, either directly or indirectly, including quoted prices in active markets for similar assets or liabilities; and Level 3 inputs are unobservable and reflect our own assumptions. The following methods were used to estimate the fair value of each class of financial instruments for which it is practicable to estimate the fair value:

Current Assets and Liabilities. The carrying values reported on the balance sheet of cash, accounts receivable and accounts payable approximate fair value because of the short maturity of those financial instruments.

Revolving Credit Borrowings. The fair value of outstanding revolving credit borrowings under the Company's senior credit facility, which is considered Level 2, is based on current LIBOR rates. The fair value of the Company's senior credit facility was approximately \$72.8 million at July 1, 2018, and \$75.0 million at December 31, 2017. The carrying value of the Company's senior credit facility was \$73.0 million at July 1, 2018 and \$75.0 million at December 31, 2017.

Long-Lived Assets. The Company assesses the recoverability of property and equipment and definite-lived intangible assets by determining whether the carrying value of these assets can be recovered over their respective remaining lives through undiscounted future operating cash flows. Impairment is reviewed when events or changes in circumstances indicate that the carrying amounts of these assets may not be fully recoverable. See Note 3 - Impairment of Long-Lived Assets.

Use of Estimates. The preparation of the condensed consolidated financial statements in conformity with GAAP requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities and the disclosure of contingent assets and liabilities at the dates of the financial statements. Estimates also affect the reported amounts of expenses during the reporting periods. Significant items subject to such estimates and assumptions include: accrued occupancy costs, insurance liabilities, evaluation for impairment of goodwill and long-lived assets and lease accounting matters. Actual results could differ from those estimates.

2. Prepaid Expenses and Other Current Assets

Prepaid expenses and other current assets, consist of the following:

	July 1, 2018	December 31, 2017
Prepaid contract expenses	\$4,132	\$ 3,681
Assets held for sale ⁽¹⁾	—	2,705
Other	4,160	3,719
	\$8,292	\$ 10,105

⁽¹⁾ Two closed Pollo Tropical restaurant properties owned by the Company that were classified as held for sale as of December 31, 2017 were

sold in 2018 for a total of \$3.3 million.

3. Impairment of Long-Lived Assets and Other Lease Charges