

DOMINOS PIZZA INC
Form 10-Q
October 12, 2006
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SECURITIES AND EXCHANGE COMMISSION

Washington, DC 20549

FORM 10-Q

(Mark One)

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

For the quarterly period ended September 10, 2006

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 numbers:

Domino s Pizza, Inc. 333-114442

Domino s, Inc. 333-107774

Domino s Pizza, Inc.

Domino s, Inc.

(Exact name of registrant as specified in its charter)

Delaware
Delaware
(State or other jurisdiction of

38-2511577
38-3025165
(I.R.S. Employer

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incorporation or organization)

30 Frank Lloyd Wright Drive

Identification Number)

Ann Arbor, Michigan 48106

(Address of principal executive offices)

(734) 930-3030

(Registrant's telephone number, including area code)

Indicate by check mark whether 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 (only with respect to Domino's Pizza, Inc.)

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 October 8, 2006, Domino's Pizza, Inc. had 62,318,179 shares of common stock, par value \$0.01 per share, outstanding. As of October 8, 2006, Domino's, Inc. had 10 shares of common stock, par value \$0.01 per share, outstanding. All of the stock of Domino's, Inc. was held by Domino's Pizza, Inc.

This Quarterly Report on Form 10-Q is a combined quarterly report being filed separately by two registrants: Domino's Pizza, Inc. and Domino's, Inc. Except where the context clearly indicates otherwise, any references in this report to Domino's Pizza, Inc. includes all subsidiaries of Domino's Pizza, Inc., including Domino's, Inc. Domino's, Inc. makes no representation as to the information contained in this report in relation to Domino's Pizza, Inc. and its subsidiaries, other than Domino's, Inc. and its subsidiaries.

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Domino s Pizza, Inc.

Domino s, Inc.

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Table of Contents**PART I. FINANCIAL INFORMATION****Item 1. Financial Statements**

Domino s Pizza, Inc. and Subsidiaries
Condensed Consolidated Balance Sheets
(Unaudited)

(In thousands)	September 10, 2006	January 1, 2006 (Note)
Assets		
Current assets:		
Cash and cash equivalents	\$ 11,043	\$ 66,919
Accounts receivable	66,553	74,437
Inventories	19,108	24,231
Notes receivable	747	408
Prepaid expenses and other	11,502	13,771
Advertising fund assets, restricted	23,060	35,643
Deferred income taxes	5,825	5,937
Total current assets	137,838	221,346
Property, plant and equipment:		
Land and buildings	19,814	22,107
Leasehold and other improvements	82,756	82,802
Equipment	162,178	163,840
Construction in progress	4,406	2,892
	269,154	271,641
Accumulated depreciation and amortization	(148,292)	(140,186)
Property, plant and equipment, net	120,862	131,455
Other assets:		
Deferred financing costs	9,504	11,652
Goodwill	21,343	22,084
Capitalized software, net	17,771	20,337
Other assets	11,097	15,543
Deferred income taxes	41,234	38,657
Total other assets	100,949	108,273
Total assets	\$ 359,649	\$ 461,074
Liabilities and stockholders' deficit		
Current liabilities:		
Current portion of long-term debt	\$ 279	\$ 35,304
Accounts payable	55,301	60,330
Accrued income taxes	3,883	8,660
Insurance reserves	9,506	9,681
Advertising fund liabilities	23,060	35,643

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Other accrued liabilities	65,800	67,767
Total current liabilities	157,829	217,385
Long-term liabilities:		
Long-term debt, less current portion	740,656	702,358
Insurance reserves	24,484	23,640
Other accrued liabilities	29,115	28,676
Total long-term liabilities	794,255	754,674
Stockholders' deficit:		
Common stock	623	672
Additional paid-in capital	128,568	259,695
Retained deficit	(725,064)	(777,906)
Accumulated other comprehensive income	3,438	6,554
Total stockholders' deficit	(592,435)	(510,985)
Total liabilities and stockholders' deficit	\$ 359,649	\$ 461,074

Note: The balance sheet at January 1, 2006 has been derived from the audited consolidated financial statements at that date but does not include all of the information and footnotes required by accounting principles generally accepted in the United States for complete financial statements.

See accompanying notes.

Table of Contents**Domino s Pizza, Inc. and Subsidiaries****Condensed Consolidated Statements of Income****(Unaudited)**

(In thousands, except per share data)	Fiscal Quarter Ended		Three Fiscal Quarters Ended	
	September 10, 2006	September 11, 2005	September 10, 2006	September 11, 2005
Revenues:				
Domestic Company-owned stores	\$ 89,284	\$ 91,024	\$ 275,987	\$ 280,923
Domestic franchise	35,696	35,914	109,588	112,384
Domestic distribution	175,531	182,085	527,967	572,127
International	26,158	28,553	88,523	88,764
Total revenues	326,669	337,576	1,002,065	1,054,198
Cost of sales:				
Domestic Company-owned stores	71,785	71,784	218,221	223,017
Domestic distribution	157,070	164,430	471,317	516,753
International	12,035	14,850	43,688	46,504
Total cost of sales	240,890	251,064	733,226	786,274
Operating margin	85,779	86,512	268,839	267,924
General and administrative	35,066	41,992	117,836	127,207
Income from operations	50,713	44,520	151,003	140,717
Interest income	381	83	860	373
Interest expense	(13,600)	(11,674)	(38,564)	(32,852)
Income before provision for income taxes	37,494	32,929	113,299	108,238
Provision for income taxes	12,970	12,645	38,117	40,152
Net income	\$ 24,524	\$ 20,284	\$ 75,182	\$ 68,086
Earnings per share:				
Common stock basic	\$ 0.39	\$ 0.31	\$ 1.18	\$ 1.02
Common stock diluted	0.39	0.30	1.16	0.99
Dividends declared per share	\$ 0.12	\$ 0.10	\$ 0.36	\$ 0.30
See accompanying notes.				

Table of Contents**Domino s Pizza, Inc. and Subsidiaries****Condensed Consolidated Statements of Cash Flows****(Unaudited)**

(In thousands)	Three Fiscal Quarters Ended	
	September 10, 2006	September 11, 2005
Cash flows from operating activities:		
Net income	\$ 75,182	\$ 68,086
Adjustments to reconcile net income to net cash provided by operating activities:		
Depreciation and amortization	22,390	22,240
Amortization of deferred financing costs and debt discount	2,568	2,057
Provision (benefit) for deferred income taxes	(2,570)	1,281
Non-cash compensation expense	3,412	1,984
Other	(3,832)	1,368
Changes in operating assets and liabilities	(7,034)	(5,941)
Net cash provided by operating activities	90,116	91,075
Cash flows from investing activities:		
Capital expenditures	(14,794)	(20,692)
Proceeds from sale of property, plant and equipment	12,974	2,672
Other	73	(678)
Net cash used in investing activities	(1,747)	(18,698)
Cash flows from financing activities:		
Net proceeds from issuance of common stock	3,332	859
Repurchase of common stock	(145,000)	(75,000)
Proceeds from issuance of long-term debt	100,000	40,000
Repayments of long-term debt and capital lease obligation	(95,194)	(65,220)
Cash paid for financing fees	(250)	(514)
Common stock dividends	(14,875)	(13,512)
Proceeds from exercise of stock options	3,575	3,761
Tax benefit from exercise of stock options	4,112	17,814
Other		722
Net cash used in financing activities	(144,300)	(91,090)
Effect of exchange rate changes on cash and cash equivalents	55	219
Decrease in cash and cash equivalents	(55,876)	(18,494)
Cash and cash equivalents, at beginning of period	66,919	40,396
Cash and cash equivalents, at end of period	\$ 11,043	\$ 21,902

See accompanying notes.

Table of Contents**Domino s Pizza, Inc. and Subsidiaries****Notes to Condensed Consolidated Financial Statements**

(Unaudited; tabular amounts in thousands, except percentages, share and per share amounts)

September 10, 2006

1. Basis of Presentation

The accompanying unaudited condensed consolidated financial statements have been prepared in accordance with accounting principles generally accepted in the United States 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 accounting principles generally accepted in the United States for complete financial statements. For further information, refer to the consolidated financial statements and footnotes for the fiscal year ended January 1, 2006 included in our annual report on Form 10-K.

In the opinion of management, all adjustments, consisting of normal recurring items, considered necessary for a fair presentation have been included. Operating results for the fiscal quarter and three fiscal quarters ended September 10, 2006 are not necessarily indicative of the results that may be expected for the fiscal year ending December 31, 2006.

Domino s Pizza, Inc. is the parent and holding company of Domino s, Inc. Accordingly, all 10 outstanding shares of Domino s, Inc. common stock, par value \$0.01 per share, are owned by Domino s Pizza, Inc. As the holding company of Domino s, Inc., Domino s Pizza, Inc. does not conduct ongoing business operations. As a result, the financial information for Domino s Pizza, Inc. and subsidiaries and Domino s, Inc. and subsidiaries is substantially similar. As the differences are minor, we have presented Domino s Pizza, Inc. and subsidiaries information throughout this filing, except for the supplemental guarantor condensed consolidating financial statements of Domino s, Inc. and subsidiaries included in Note 9.

2. Comprehensive Income

	Fiscal Quarter Ended		Three Fiscal Quarters Ended	
	September 10, 2006	September 11, 2005	September 10, 2006	September 11, 2005
Net income	\$ 24,524	\$ 20,284	\$ 75,182	\$ 68,086
Unrealized gains (losses) on derivative instruments, net of tax	(505)	356	1,085	1,831
Reclassification adjustment for gains included in net income, net of tax	(3,381)	(220)	(4,935)	(1,162)
Currency translation adjustment	31	598	734	(790)
Comprehensive income	\$ 20,669	\$ 21,018	\$ 72,066	\$ 67,965

3. Segment Information

The following table summarizes revenues, income from operations and earnings before interest, taxes, depreciation, amortization and other, which is the measure by which management allocates resources to its segments and which we refer to as Segment Income, for each of our reportable segments.

	Fiscal Quarters Ended September 10, 2006 and September 11, 2005					Total
	Domestic Stores	Domestic Distribution	International	Intersegment Revenues	Other	
Revenues						
2006	\$ 124,980	\$ 199,893	\$ 26,158	\$ (24,362)	\$	\$ 326,669

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2005	126,938	208,559	28,553	(26,474)	337,576
Income from operations					
2006	\$ 31,649	\$ 12,900	\$ 14,371	N/A	\$ (8,207) \$ 50,713
2005	33,225	11,736	8,761	N/A	(9,202) 44,520
Segment Income					
2006	\$ 34,041	\$ 15,067	\$ 11,679	N/A	\$ (4,780) \$ 56,007
2005	36,382	14,148	9,144	N/A	(6,309) 53,365

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	Three Fiscal Quarters Ended September 10, 2006 and September 11, 2005					
	Domestic Stores	Domestic Distribution	International	Intersegment Revenues	Other	Total
Revenues						
2006	\$ 385,575	\$ 601,380	\$ 88,523	\$ (73,413)	\$	\$ 1,002,065
2005	393,307	654,385	88,764	(82,258)		1,054,198
Income from operations						
2006	\$ 100,661	\$ 40,239	\$ 36,572	N/A	\$ (26,469)	\$ 151,003
2005	104,179	36,536	26,687	N/A	(26,685)	140,717
Segment Income						
2006	\$ 109,344	\$ 46,741	\$ 34,459	N/A	\$ (16,804)	\$ 173,740
2005	112,954	43,909	27,797	N/A	(19,284)	165,376

The following table reconciles Total Segment Income to consolidated income before provision for income taxes.

	Fiscal Quarter Ended		Three Fiscal Quarters Ended	
	September 10, 2006	September 11, 2005	September 10, 2006	September 11, 2005
Total Segment Income	\$ 56,007	\$ 53,365	\$ 173,740	\$ 165,376
Depreciation and amortization	(7,416)	(7,554)	(22,390)	(22,240)
Gains (losses) on sale/disposal of assets	3,444	(346)	3,065	(435)
Non-cash stock compensation expense	(1,322)	(945)	(3,412)	(1,984)
Income from operations	50,713	44,520	151,003	140,717
Interest income	381	83	860	373
Interest expense	(13,600)	(11,674)	(38,564)	(32,852)
Income before provision for income taxes	\$ 37,494	\$ 32,929	\$ 113,299	\$ 108,238

4. Earnings Per Share

	Fiscal Quarter Ended		Three Fiscal Quarters Ended	
	September 10, 2006	September 11, 2005	September 10, 2006	September 11, 2005
Net income available to common stockholders basic and diluted	\$ 24,524	\$ 20,284	\$ 75,182	\$ 68,086
Weighted average number of shares	62,201,247	66,379,392	63,481,768	66,867,837
Earnings per share basic	\$ 0.39	\$ 0.31	\$ 1.18	\$ 1.02
Diluted weighted average number of shares	63,405,773	68,226,744	64,856,318	68,995,839
Earnings per share diluted	\$ 0.39	\$ 0.30	\$ 1.16	\$ 0.99

The denominator in calculating diluted earnings per share for common stock for both the third quarter and first three quarters of 2006 does not include 3,371,500 and 3,363,900 options to purchase common stock, respectively, as the effect of including these options would have been anti-dilutive.

5. Sale of Certain Company-owned Operations

During the second quarter of 2006, the Company signed a stock purchase agreement to sell its Company-owned operations in France and the Netherlands to its master franchisee for Australia and New Zealand. The sale closed in the third quarter. During the third quarter, the Company recognized a gain of approximately \$2.8 million related to the sale, due primarily to the recognition of foreign currency translation adjustments. The gain was included in general and administrative expenses. During the second quarter of 2006, the Company recorded a \$2.9 million tax benefit as it was apparent that it would realize a benefit resulting from tax losses to be realized upon the sale of these operations.

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Additionally, during the third quarter of 2006, the Company sold 11 domestic Company-owned stores to an existing franchisee. The sale resulted in a pre-tax gain of approximately \$0.7 million, or \$0.4 million after tax.

6. Supplemental Disclosure of Cash Flow Information

The Company recorded a \$7.5 million dividend payable during the third quarter of 2006. The dividend was subsequently paid on September 30, 2006.

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7. Effect of Adoption of Statement of Financial Accounting Standard No. 123(R)

During 2005, the Company adopted Statement of Financial Accounting Standard (SFAS) No. 123(R) (revised 2004), Share-Based Payment using the modified retrospective method. This method allows the restatement of interim financial statements in the year of adoption based on the amounts previously calculated in the pro forma footnote disclosures required by SFAS No. 123. The amounts presented herein for the third quarter and first three quarters of 2005 have been revised to include the effects of this adoption. As a result of the adoption, net income decreased approximately \$0.5 million and \$1.1 million from the amounts previously reported for the third quarter and first three quarters of 2005, respectively.

8. New Accounting Pronouncement

In June 2006, the Financial Accounting Standards Board (FASB) issued FASB Interpretation No. 48, Accounting for Uncertainty in Income Taxes – an interpretation of FASB Statement No. 109 (FIN 48). FIN 48 prescribes a recognition threshold and measurement attribute for financial statement recognition and measurement of a tax position taken or expected to be taken in a tax return, and also provides guidance on derecognition, classification, interest and penalties, accounting in interim periods, disclosure, and transition. FIN 48 is effective for fiscal years beginning after December 15, 2006. The Company is assessing FIN 48 and has not determined the impact that the adoption of FIN 48 will have on its results of operations.

9. Supplemental Guarantor Condensed Consolidating Financial Statements of Domino's, Inc. and Subsidiaries

The tables below present condensed consolidating financial information for the applicable periods for: (1) Domino's, Inc.; (2) on a combined basis, the guarantor subsidiaries of Domino's, Inc.'s senior subordinated notes due 2011, which includes most of the domestic subsidiaries of Domino's, Inc. and one foreign subsidiary of Domino's, Inc.; and (3) on a combined basis, the non-guarantor subsidiaries of Domino's, Inc.'s senior subordinated notes due 2011. The separate financial statements of Domino's, Inc. and subsidiaries are presented using the equity method of accounting. Accordingly, Domino's, Inc.'s investment in subsidiaries is included in Other assets and the net earnings of the subsidiaries are included in Equity earnings in subsidiaries. Except for the minor differences noted in the footnote to the condensed consolidating balance sheet below, the consolidated financial statements of Domino's, Inc. and subsidiaries are substantially similar to the consolidated financial statements of Domino's Pizza, Inc. and subsidiaries. Each of the guarantor subsidiaries is jointly, severally, fully and unconditionally liable under the related guarantee.

Domino's, Inc. and Subsidiaries**Supplemental Guarantor Condensed Consolidating Balance Sheets**

	As of September 10, 2006				
	Domino's, Inc.	Guarantor Subsidiaries	Non-Guarantor Subsidiaries	Eliminations	Consolidated
Cash and cash equivalents	\$	\$ 11,043	\$	\$	\$ 11,043
Accounts receivable		66,553			66,553
Advertising fund assets, restricted			23,060		23,060
Other current assets	5,215	31,967			37,182
Current assets	5,215	109,563	23,060		137,838
Property, plant and equipment, net		120,862			120,862
Other assets	155,544	61,723		(116,318)	100,949
Total assets	\$ 160,759	\$ 292,148	\$ 23,060	\$ (116,318)	\$ 359,649
Current portion of long-term debt	\$	\$ 279	\$	\$	\$ 279
Accounts payable		55,301			55,301
Advertising fund liabilities			23,060		23,060
Other current liabilities	10,055	61,669			71,724

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Current liabilities ⁽¹⁾	10,055	117,249	23,060	150,364	
Long-term debt	735,421	5,235		740,656	
Other long-term liabilities	253	53,346		53,599	
Long-term liabilities	735,674	58,581		794,255	
Stockholder's equity (deficit) ⁽²⁾	(584,970)	116,318	(116,318)	(584,970)	
Total liabilities and stockholder's equity (deficit)	\$ 160,759	\$ 292,148	\$ 23,060	\$ (116,318)	\$ 359,649

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- (1) Domino's Pizza, Inc. and subsidiaries had current liabilities of \$157,829, or \$7,465 more than Domino's, Inc. and subsidiaries at September 10, 2006. Domino's Pizza, Inc. and subsidiaries had total stockholders' deficit of \$592,435, or \$7,465 more than Domino's, Inc. and subsidiaries at September 10, 2006. These differences resulted from the inclusion of a dividend payable recorded on Domino's Pizza, Inc. and subsidiaries that was not recorded on Domino's, Inc. and subsidiaries. While Domino's, Inc. and subsidiaries distributed funds to Domino's Pizza, Inc. and subsidiaries subsequent to the third quarter to pay this dividend, it was not a liability for Domino's, Inc. and subsidiaries at September 10, 2006. There were no other differences between Domino's, Inc. and subsidiaries as compared to Domino's Pizza, Inc. and subsidiaries for the periods presented.

	As of January 1, 2006				Consolidated
	Domino's, Inc.	Guarantor Subsidiaries	Non-Guarantor Subsidiaries	Eliminations	
Cash and cash equivalents	\$	\$ 66,389	\$ 530	\$	\$ 66,919
Accounts receivable		78,533	8,281	(12,377)	74,437
Advertising fund assets, restricted			35,643		35,643
Other current assets	6,098	36,253	1,996		44,347
Current assets	6,098	181,175	46,450	(12,377)	221,346
Property, plant and equipment, net		128,724	2,731		