DENNYS CORP
Form 10-Q
August 04, 2009

UNITED STATES
SECURITIES AND EXCHANGE COMMISSION
Washington, D.C. 20549

FORM 10-Q

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

For the Quarterly Period Ended July 1, 2009

Commission File Number 0-18051
DENNY'S CORPORATION
(Exact name of registrant as specified in its charter)

Delaware	13-3487402
(State or other jurisdiction of incorporation or organization	(I.R.S. Employer Identification No.)

203 East Main Street
Spartanburg, South Carolina 29319-0001
(Address of principal executive offices)
(Zip Code)

(864) 597-8000
(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 þ No ¨

Indicate by check mark whether the registrant has submitted electronically and posted on its 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, or a smaller reporting company. See the definitions of "large accelerated filer," "accelerated filer" and "smaller reporting company" in Rule 12b-2 of the Exchange Act.

Large accelerated filer ¨ Accelerated filer þ
Non-accelerated filer ¨ (Do not check if a smaller reporting company) Smaller reporting company ¨

Indicate by check mark whether the registrant is a shell company (as defined in Rule 12b-2 of the Exchange Act).

Yes ¨ No þ

As of July 30, 2009, 96,541,829 shares of the registrant's common stock, par value $.01 per share, were outstanding.

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PART I - FINANCIAL INFORMATION

Item 1. Financial Statements

Denny's Corporation and Subsidiaries
Condensed Consolidated Statements of Operations
(Unaudited)

	Quarter Ended		Two Quarters Ended	
	July 1, 2009	June 25, 2008	July 1, 2009	June 25, 2008
	(In thousands, except per share amounts)			
Revenue:				
Company restaurant sales	$ 125,500	$ 163,233	$ 261,076	$ 332,826
Franchise and license revenue	30,313	27,039	60,497	53,442
Total operating revenue	155,813	190,272	321,573	386,268
Costs of company restaurant sales:				
Product costs	29,306	39,032	61,589	80,979
Payroll and benefits	52,151	69,021	109,911	142,749
Occupancy	8,056	9,976	17,100	20,528
Other operating expenses	17,994	24,730	38,592	49,938
Total costs of company restaurant sales	107,507	142,759	227,192	294,194
Costs of franchise and license revenue	10,689	8,520	21,987	16,691
General and administrative expenses	15,907	15,537	29,754	31,152
Depreciation and amortization	8,015	9,892	16,727	20,133
Operating gains, losses and other charges, net	(3,751)	3,027	(3,453)	(5,686)
Total operating costs and expenses	138,367	179,735	292,207	356,484
Operating income	17,446	10,537	29,366	29,784
Other expenses:				
Interest expense, net	8,239	8,883	16,730	18,084
Other nonoperating expense (income), net	(745)	(1,617)	(1,231)	3,759
Total other expenses, net	7,494	7,266	15,499	21,843
Net income before income taxes	9,952	3,271	13,867	7,941
Provision for income taxes	616	120	224	666
Net income	$ 9,336	$ 3,151	$ 13,643	$ 7,275
Net income per share:				
Basic	$ 0.10	$ 0.03	$ 0.14	$ 0.08
Diluted	$ 0.09	$ 0.03	$ 0.14	$ 0.07
Weighted average shares outstanding:				
Basic	96,113	95,017	96,079	94,922
Diluted	98,457	98,911	97,893	98,659

See accompanying notes to unaudited condensed consolidated financial statements

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Denny's Corporation and Subsidiaries
Condensed Consolidated Balance Sheets
(Unaudited)

	July 1, 2009	December 31, 2008
	(In thousands)	
Assets		
Current Assets:		
Cash and cash equivalents	$ 19,865	$ 21,042
Receivables, less allowance for doubtful accounts of $831 and $475, respectively	14,185	15,146
Inventories	4,383	5,455
Assets held for sale	3,100	2,285
Prepaid and other current assets	14,582	9,531
Total Current Assets	56,115	53,459
Property, net of accumulated depreciation of $264,174 and $284,933, respectively	140,513	159,978
Other Assets:		
Goodwill	38,804	40,006
Intangible assets, net	57,091	58,832
Deferred financing costs, net	3,307	3,879
Other noncurrent assets	33,649	31,041
Total Assets	$ 329,479	$ 347,195
Liabilities		
Current Liabilities:		
Current maturities of notes and debentures	$ 3,388	$ 1,403
Current maturities of capital lease obligations	3,506	3,535
Accounts payable	19,435	25,255
Other current liabilities	69,039	76,924
Total Current Liabilities	95,368	107,117
Long-Term Liabilities:		
Notes and debentures, less current maturities	288,563	300,617
Capital lease obligations, less current maturities	19,912	22,084
Liability for insurance claims, less current portion	24,663	25,832
Deferred income taxes	12,624	12,345
Other noncurrent liabilities and deferred credits	46,076	53,237
Total Long-Term Liabilities	391,838	414,115
Total Liabilities	487,206	521,232
Commitments and contingencies		
Total Shareholders' Deficit	(157,727)	(174,037)
Total Liabilities and Shareholders' Deficit	$ 329,479	$ 347,195

See accompanying notes to unaudited condensed consolidated financial statements

Denny’s Corporation and Subsidiaries
Condensed Consolidated Statement of Shareholders’ Deficit and Comprehensive Loss
(Unaudited)

	Common Stock					Accumulated Other Comprehensive	Total Shareholders'
	Shares	Amount	Paid-in Capital	Deficit		Loss, Net	Deficit
			(In thousands)				
Balance, December 31, 2008	95,713	$ 957	$ 538,911	$ (688,984)		$ (24,921)	$ (174,037)
Comprehensive income:							
Net income	—	—	—	13,643		—	13,643
Amortization of unrealized loss on hedged transactions, net of tax	—	—	—	—		537	537
Comprehensive income	—	—	—	13,643		537	14,180
Share-based compensation on equity classified awards	—	—	2,106	—		—	2,106
Issuance of common stock for share-based compensation	437	4	(4)	—		—	—
Exercise of common stock options	23	—	24	—		—	24
Balance, July 1, 2009	96,173	$ 961	$ 541,037	$ (675,341)		$ (24,384)	$ (157,727)

See accompanying notes to unaudited condensed consolidated financial statements

Denny's Corporation and Subsidiaries
Condensed Consolidated Statements of Cash Flows
(Unaudited)

	Two Quarters Ended	
	July 1, 2009	June 25, 2008
	(In thousands)	
Cash Flows from Operating Activities:		
Net income	$ 13,643	$ 7,275
Adjustments to reconcile net income to cash flows provided by operating activities:		
Depreciation and amortization	16,727	20,133
Operating gains, losses and other charges, net	(3,453)	(5,686)
Amortization of deferred financing costs	542	553
(Gain) loss on early extinguishment of debt	12	(30)
(Gain) loss on interest rate swap	(875)	3,048
Deferred income tax expense	278	295
Share-based compensation	2,702	1,662
Changes in assets and liabilities, net of effects of acquisitions and dispositions:		
Decrease (increase) in assets:		
Receivables	1,242	2,072
Inventories	1,072	675
Other current assets	(5,051)	2,273
Other assets	(1,100)	(3,045)
Increase (decrease) in liabilities:		
Accounts payable	(3,112)	(6,827)
Accrued salaries and vacations	(3,067)	(3,756)
Accrued taxes	(342)	(1,207)
Other accrued liabilities	(9,230)	(4,080)
Other noncurrent liabilities and deferred credits	(2,561)	(6,224)
Net cash flows provided by operating activities	7,427	7,131
Cash Flows from Investing Activities:		
Purchase of property	(7,936)	(14,829)
Proceeds from disposition of property	13,030	18,008
Net cash flows provided by investing activities	5,094	3,179
Cash Flows from Financing Activities:		
Long-term debt payments	(12,025)	(17,837)
Proceeds from exercise of stock options	24	512
Net bank overdrafts	(1,697)	(2,504)
Net cash flows used in financing activities	(13,698)	(19,829)
Decrease in cash and cash equivalents	(1,177)	(9,519)
Cash and Cash Equivalents at:		
Beginning of period	21,042	21,565
End of period	$ 19,865	$ 12,046

See accompanying notes to unaudited condensed consolidated financial statements

Denny’s Corporation and Subsidiaries
Notes to Condensed Consolidated Financial Statements
(Unaudited)

Note 1. Introduction and Basis of Presentation

Denny’s Corporation, through its wholly owned subsidiaries, Denny’s Holdings, Inc. and Denny’s, Inc., owns and operates the Denny’s restaurant brand, or Denny’s.

Our unaudited condensed consolidated financial statements have been prepared pursuant to the rules and regulations of the Securities and Exchange Commission. Therefore, certain information and notes normally included in financial statements prepared in accordance with U.S. generally accepted accounting principles have been condensed or omitted. In our opinion, all adjustments considered necessary for a fair presentation of the interim periods presented have been included. Such adjustments are of a normal and recurring nature. The preparation of these financial statements requires us to make estimates and judgments that affect the reported amounts of assets, liabilities, revenues and expenses, and related disclosure of contingent assets and liabilities. Actual results may differ from these estimates under different assumptions or conditions; however, we believe that our estimates, including those for the above-described items, are reasonable.

These interim condensed consolidated financial statements should be read in conjunction with our consolidated financial statements and notes thereto for the year ended December 31, 2008 and the related Management’s Discussion and Analysis of Financial Condition and Results of Operations, both of which are contained in our Annual Report on Form 10-K for the fiscal year ended December 31, 2008. The results of operations for the interim periods presented are not necessarily indicative of the results for the entire fiscal year ending December 30, 2009.

Note 2. Summary of Significant Accounting Policies

Effective July 1, 2009, we adopted Statement of Financial Accounting Standards No. 165 (“SFAS 165”), “Subsequent Events,” which was issued by the Financial Accounting Standards Board ("FASB") in May 2009. SFAS 165 establishes general standards of accounting for and disclosure of events that occur after the balance sheet date, but before financial statements are issued or are available to be issued. The adoption of SFAS 165 did not have a material impact on our Condensed Consolidated Financial Statements as of July 1, 2009. See Note 18.

Effective July 1, 2009, we adopted FASB Staff Position No. FAS 107-1 and APB 28-1 ("FSP FAS 107-1 and APB 28-1"), "Interim Disclosures about Fair Value of Financial Instruments." The FSP amends Statement of Financial Accounting Standards No. 107, "Disclosure about Fair Value of Financial Instruments," and Accounting Principles Board Opinion No. 28, "Interim Financial Reporting," to require disclosures about fair value of financial instruments for interim reporting periods of publicly traded companies as well as in annual financial statements. The adoption of FSP FAS 107-1 and APB 28-1did not have a material impact on our Condensed Consolidated Financial Statements.

Effective July 1, 2009, we adopted FASB Staff Position No. FSP FAS 115-2 and FAS 124-2 ("FSP FAS 115-2 and FAS 124-2"), "Recognition and Presentation of Other-Than-Temporary Impairments." The FSP amends the other-than-temporary impairment guidance in U.S. GAAP for debt securities to make the guidance more operational and to improve the presentation and disclosure of other-than-temporary impairments on debt and equity securities in the financial statements. This FSP does not amend existing recognition and measurement guidance related to other-than-temporary impairments of equity securities. The adoption of FSP FAS 115-2 and FAS 124-2 did not have a material impact on our Condensed Consolidated Financial Statements.

Effective July 1, 2009, we adopted FASB Staff Position No. FAS 157-4 ("FSP FAS 157-4"), "Determining Fair Value When the Volume and Level of Activity for the Asset or Liability Have Significantly Decreased and Identifying Transactions That Are Not Orderly." The FSP provides additional guidance for estimating fair value in accordance with FASB Statement of Financial Accounting Standards No. 157, "Fair Value Measurements", when the volume and level of activity for the asset or liability have significantly decreased. This FSP also includes guidance on identifying circumstances that indicate a transaction is not orderly. The adoption of FSP FAS 157-4 did not have a material impact on our Condensed Consolidated Financial Statements.

Effective January 1, 2009, the first day of fiscal 2009, we adopted FASB Staff Position No. FSP FAS 142-3 (“FSP FAS 142-3”), “Determination of the Useful Life of Intangible Assets.” FSP FAS 142-3 amends the factors that should be considered in developing renewal or extension assumptions used to determine the useful life of a recognized intangible asset under Statement of Financial Accounting Standards No. 142 ("SFAS 142"), “Goodwill and Other Intangible Assets.” We will apply FSP FAS 142-3 prospectively to intangible assets acquired subsequent to the adoption date. The adoption of FSP FAS 142-3 had no impact on our Condensed Consolidated Financial Statements.

Effective January 1, 2009, we adopted Statement of Financial Accounting Standards No. 161 (“SFAS 161”), “Disclosures about Derivative Instruments and Hedging Activities,” which amends and expands Statement of Financial Accounting Standards No. 133, "Accounting for Derivative Instruments and Hedging Activities." SFAS 161 requires tabular disclosure of the fair value of derivative instruments and their gains and losses. This Statement also requires disclosure regarding the credit-risk related contingent features in derivative agreements, counterparty credit risk, and strategies and objectives for using derivative instruments. The adoption of SFAS 161 did not have a material impact on our Condensed Consolidated Financial Statements. See Note 8.

During 2008, we adopted FASB Staff Position No. 157-2 ("FSP FAS 157-2"), "Effective Date of FASB Statement 157,"which deferred the provisions of SFAS 157 for nonfinancial assets and liabilities to the first fiscal period beginning after November 15, 2008. Deferred nonfinancial assets and liabilities include items such as goodwill and other nonamortizable intangibles. Effective January 1, 2009, we adopted the provisions of SFAS 157 for nonfinancial assets and liabilities. The adoption of FSP FAS 157-2 did not have a material impact on our Condensed Consolidated Financial Statements. See Note 6.

Effective January 1, 2009, we adopted Statement of Financial Accounting Standards No. 160 ("SFAS 160"), "Noncontrolling Interests in Consolidated Financial Statements — an amendment of ARB No. 51." SFAS 160 amends Accounting Research Bulletin No. 51, "Consolidated Financial Statements" to establish accounting and reporting standards for the noncontrolling interest in a subsidiary and for the deconsolidation of a subsidiary. It clarifies that a noncontrolling interest in a subsidiary, which is sometimes referred to as minority interest, is an ownership interest in the consolidated entity that should be reported as equity in our Consolidated Financial Statements. Among other requirements, this Statement requires that the consolidated net income attributable to the parent and the noncontrolling interest be clearly identified and presented on the face of the consolidated income statement. The adoption of SFAS 160 did not have a material impact on our Condensed Consolidated Financial Statements.

Effective January 1, 2009, we adopted Statement of Financial Accounting Standards No. 141 (revised 2007) ("SFAS 141R"), "Business Combinations." SFAS 141R establishes principles and requirements for how an acquirer recognizes and measures in its financial statements the identifiable assets acquired, the liabilities assumed, any noncontrolling interest in an acquiree and the goodwill acquired. We will apply SFAS 141R to any business combinations subsequent to adoption. In addition, this Statement requires that any additional reversal of deferred tax asset valuation allowance established in connection with our fresh start reporting on January 7, 1998 be recorded as a component of income tax expense rather than as a reduction to the goodwill established in connection with the fresh start reporting. See Note 12.

Effective January 1, 2009, we adopted FASB Staff Position Financial Accounting Standard 141R-1 ("FSP FAS 141R-1"), "Accounting for Assets Acquired and Liabilities Assumed in a Business Combination That Arise from Contingencies." FSP FAS 141R-1 amends SFAS 141R to require that an acquirer recognize at fair value, at the acquisition date, an asset acquired or a liability assumed in a business combination that arises from a contingency if the acquisition-date fair value of that asset or liability can be determined during the measurement period. If the acquisition-date fair value of such an asset acquired or liability assumed cannot be determined, the acquirer should apply the provisions of SFAS 5, "Accounting for Contingencies", to determine whether the contingency should be recognized at the acquisition date or after such date. The adoption of FSP FAS 141R-1 did not have a material impact on our Condensed Consolidated Financial Statements.

There have been no other material changes to our significant accounting policies and estimates from the information provided in Note 2 of our Consolidated Financial Statements included in our Form 10-K for the fiscal year ended December 31, 2008.

Note 3. Assets Held for Sale

Assets held for sale of $3.1 million and $2.3 million as of July 1, 2009 and December 31, 2008, respectively, include restaurants to be sold to franchisees and real estate to be sold to third parties. We expect to sell each of these assets within 12 months. Our Credit Facility (defined in Note 7) requires us to make mandatory prepayments to reduce outstanding indebtedness with the net cash proceeds from the sale of specified real estate properties and restaurant operations to franchisees, net of a voluntary $10.0 million annual exclusion related to proceeds from the sale of restaurant operations to franchisees. As of July 1, 2009, as a result of the mandatory prepayment requirements, we classified $2.1 million of our long-term debt as a current liability in our Condensed Consolidated Balance Sheet. This amount represents the required prepayment based on the net book value of the specified properties as of the balance sheet date less the remaining balance of the annual exclusion. As of December 31, 2008, no reclassification of long-term debt to current liabilities was required. As a result of classifying certain assets as held for sale, we recognized impairment charges of $0.1 million and $0.4 million for the quarter and two quarters ended July 1, 2009. This expense is included as a component of operating gains, losses and other charges, net in our Condensed Consolidated Statements of Operations. There were no impairment charges recognized related to assets held for sale for the quarter or two quarters ended June 25, 2008.

Note 4. Goodwill and Other Intangible Assets

The changes in carrying amounts of goodwill for the quarter ended July 1, 2009 are as follows:

	(In thousands)
Balance at December 31, 2008	$ 40,006
Write-offs associated with sale of restaurants	(1,202)
Balance at July 1, 2009	$ 38,804

The following table reflects goodwill and intangible assets as of July 1, 2009 and December 31, 2008:

	July 1, 2009		December 31, 2008	
	Gross Carrying Amount	Accumulated Amortization	Gross Carrying Amount	Accumulated Amortization
	(In thousands)			
Goodwill	$ 38,804	$ —	$ 40,006	$ —
Intangible assets with indefinite lives:				
Trade names	$ 42,445	$ —	$ 42,438	$ —
Liquor licenses	262	—	262	—
Intangible assets with definite lives:				
Franchise and license agreements	51,344	37,057	55,332	39,303
Foreign license agreements	241	144	241	138
Intangible assets	$ 94,292	$ 37,201	$ 98,273	$ 39,441
Other assets with definite lives:				
Software development costs	$ 32,476	$ 27,425	$ 31,979	$ 26,446

Note 5. Operating Gains, Losses and Other Charges, Net

Operating gains, losses and other charges, net are comprised of the following:

	Quarter Ended		Two Quarters Ended	
	July 1, 2009	June 25, 2008	July 1, 2009	June 25, 2008
	(In thousands)			
Gains on sales of assets and other, net	$ (3,508)	$ (3,176)	$ (4,032)	$ (12,924)
Restructuring charges and exit costs	(673)	5,719	(244)	6,754
Impairment charges	430	484	823	484
Operating gains, losses and other charges, net	$ (3,751)	$ 3,027	$ (3,453)	$ (5,686)

Gains on Sales of Assets

Proceeds and gains on sales of assets were comprised of the following:

	Quarter Ended July 1, 2009		Quarter Ended June 25, 2008	
	Net Proceeds	Gains	Net Proceeds	Gains
	(In thousands)			
Sales of restaurant operations and related real estate to franchisees	$ 6,960	$ 2,343	$ 5,544	$ 2,201
Sales of other real estate assets	2,754	1,134	1,647	944
Recognition of deferred gains	—	31	—	31
Total	$ 9,714	$ 3,508	$ 7,191	$ 3,176

During the quarter ended July 1, 2009, as part of our Franchise Growth Initiative ("FGI"), we recognized $2.3 million of gains on the sale of 22 restaurant operations to eight franchisees for net proceeds of $7.0 million, which included a note receivable of $0.1 million. During the quarter ended June 25, 2008, we recognized $2.2 million of gains on the sale of 20 restaurant operations to seven franchisees for net proceeds of $5.5 million, which included a note receivable of $0.3 million and a $3.2 million receivable related to proceeds of a transaction that were collected immediately after the end of the period.

	Two Quarters Ended July 1, 2009		Two Quarters Ended June 25, 2008	
	Net Proceeds	Gains	Net Proceeds	Gains
	(In thousands)			
Sales of restaurant operations and related real estate to franchisees	$ 11,751	$ 2,803	$ 21,999	$ 11,943
Sales of other real estate assets	2,754	1,134	1,622	919
Recognition of deferred gains	—	95	—	62
Total	$ 14,505	$ 4,032	$ 23,621	$ 12,924

During the two quarters ended July 1, 2009, as part of our FGI, we recognized $2.8 million of gains on the sale of 52 restaurant operations to ten franchisees for net proceeds of $11.8 million, which included a note receivable of $1.5 million. During the two quarters ended June 25, 2008, we recognized $11.9 million of gains on the sale of 41 restaurant operations to eleven franchisees for net proceeds of $22.0 million, which included notes receivable of $2.4 million and a $3.2 million receivable related to proceeds of a transaction that were collected immediately after the end of the period.

Restructuring Charges and Exit Costs

Restructuring charges and exit costs were comprised of the following:

	Quarter Ended		Two Quarters Ended	
	July 1, 2009	June 25, 2008	July 1, 2009	June 25, 2008
	(In thousands)			
Exit costs	$ (795)	$ 815	$ (745)	$ 1,655
Severance and other restructuring charges	122	4,904	501	5,099

Total restructuring and exit costs	$ (673)	$ 5,719	$ (244)	$ 6,754

The components of the change in accrued exit cost liabilities are as follows:

	(In thousands)
Balance at December 31, 2008	$ 9,239
Provisions for units closed during the year (1)	—
Changes in estimates of accrued exit costs, net (1)	(745)
Payments, net of sublease receipts	(2,265)
Interest accretion	408
Balance at July 1, 2009	6,637
Less current portion included in other current liabilities	1,692
Long-term portion included in other noncurrent liabilities	$ 4,945

(1) Included as a component of operating gains, losses and other charges, net.

Estimated net cash payments related to exit cost liabilities in the next five years are as follows:

	(In thousands)
Remainder of 2009	$ 1,074
2010	1,592