

Edgar Filing: SHELLS SEAFOOD RESTAURANTS INC - Form 10-Q

SHELLS SEAFOOD RESTAURANTS INC  
Form 10-Q  
May 16, 2001

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 APRIL 1, 2001

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

FOR THE TRANSITION PERIOD FROM \_\_\_\_\_ TO \_\_\_\_\_

COMMISSION FILE NO. 0-28258

SHELLS SEAFOOD RESTAURANTS, INC.

-----  
(EXACT NAME OF REGISTRANT AS SPECIFIED IN ITS CHARTER)

DELAWARE

65-0427966

-----  
(STATE OR OTHER JURISDICTION OF  
INCORPORATION OR ORGANIZATION)

-----  
(IRS) EMPLOYER IDENTIFICATION NUMBER

16313 NORTH DALE MABRY HIGHWAY, SUITE 100, TAMPA, FL 33618

-----  
(ADDRESS OF PRINCIPAL EXECUTIVE OFFICES) (ZIP CODE)

(813) 961-0944

-----  
(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

CLASS

OUTSTANDING AT MAY 16, 2001

-----  
COMMON STOCK, \$.01 PAR VALUE

-----  
4,454,015

SHELLS SEAFOOD RESTAURANTS, INC. AND SUBSIDIARIES  
INDEX

PART I - FINANCIAL INFORMATION

PAGE NUMBER

ITEM 1 - FINANCIAL STATEMENTS

## Edgar Filing: SHELLS SEAFOOD RESTAURANTS INC - Form 10-Q

CONSOLIDATED BALANCE SHEETS AS OF APRIL 1, 2001 (UNAUDITED) AND DECEMBER 31, 2000	3
CONSOLIDATED STATEMENTS OF INCOME (UNAUDITED) FOR THE 13 WEEKS ENDED APRIL 1, 2001 AND APRIL 2, 2000	4
CONSOLIDATED STATEMENTS OF CASH FLOWS (UNAUDITED) FOR THE 13 WEEKS ENDED APRIL 1, 2001 AND APRIL 2, 2000	5
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS - (UNAUDITED)	6
ITEM 2 - MANAGEMENT'S DISCUSSION AND ANALYSIS OF FINANCIAL CONDITION AND RESULTS OF OPERATIONS	7-9
ITEM 3 - QUANTITATIVE AND QUALITATIVE DISCLOSURES ABOUT MARKET RISK	10
PART II - OTHER INFORMATION	11
SIGNATURES	12

2

### SHELLS SEAFOOD RESTAURANTS, INC. AND SUBSIDIARIES CONSOLIDATED BALANCE SHEETS

	(UNAUDITED) APRIL 1, 2001	DECEMBER 31, 2000
	-----	-----
<b>ASSETS</b>		
Cash	\$ 371,373	\$ 1,261,937
Inventories	940,848	1,007,520
Other current assets	892,305	495,506
Receivables from related parties	72,616	196,155
Deferred tax asset, net	638,000	638,000
	-----	-----
Total current assets	2,915,142	3,599,118
Property and equipment, net	12,442,912	14,165,527
Prepaid rent	160,522	173,122
Other assets	393,251	435,722
Goodwill	2,835,250	2,886,799
Deferred tax asset, net	85,441	200,223
	-----	-----
<b>TOTAL ASSETS</b>	<b>18,832,518</b>	<b>21,460,511</b>
	=====	=====
<b>LIABILITIES AND STOCKHOLDERS' EQUITY</b>		
Accounts payable	\$ 3,340,212	\$ 3,445,541
Accrued expenses	5,826,027	5,312,219
Sales tax payable	520,658	356,039
Current portion of long-term debt	1,969,522	1,985,447
	-----	-----
Total current liabilities	11,656,419	11,099,246
Deferred rent	1,799,965	1,783,994
Long-term debt, less current portion	3,539,491	3,714,316
	-----	-----
Total liabilities	16,995,875	16,597,556

Edgar Filing: SHELLS SEAFOOD RESTAURANTS INC - Form 10-Q

Minority partner interest	442,718	449,011
	-----	-----
STOCKHOLDERS' EQUITY:		
Preferred stock, \$0.01 par value; authorized 2,000,000 shares; none issued or outstanding	--	--
Common stock, \$.01 par value; authorized 20,000,000 shares; 4,454,015 shares issued and outstanding	44,540	44,540
Additional paid-in-capital	14,161,010	14,161,010
Retained earnings (deficit)	(12,811,625)	(9,791,606)
	-----	-----
Total stockholders' equity	1,393,925	4,413,944
	-----	-----
TOTAL LIABILITIES AND STOCKHOLDERS' EQUITY	18,832,518	21,460,511
	=====	=====

SEE NOTES TO CONSOLIDATED FINANCIAL STATEMENTS.

3

SHELLS SEAFOOD RESTAURANTS, INC. AND SUBSIDIARIES  
CONSOLIDATED STATEMENTS OF INCOME

	13 WEEKS ENDED	
	APRIL 1, 2001	APRIL 2, 2000
	-----	-----
REVENUES	\$ 21,654,590	\$ 25,850,919
	-----	-----
COST AND EXPENSES:		
Cost of revenues	8,143,679	9,261,168
Labor and other related expenses	6,455,549	7,400,011
Other restaurant operating expenses	4,598,244	4,930,126
General and administrative expenses	1,694,154	1,812,437
Depreciation and amortization	536,022	676,549
Provision for impairment of assets	1,582,137	--
Provision for store closings	1,333,271	--
	-----	-----
	24,343,056	24,080,291
	-----	-----
INCOME (LOSS) FROM OPERATIONS	(2,688,466)	1,770,628
	-----	-----
OTHER INCOME (EXPENSE):		
Interest expense	(186,786)	(226,612)
Interest income	1,247	35,497
Other expense, net	(65,739)	(11,363)
	-----	-----
	(251,278)	(202,478)
	-----	-----
INCOME (LOSS) BEFORE ELIMINATION OF MINORITY PARTNER INTEREST AND INCOME TAXES	(2,939,744)	1,568,150
	-----	-----
ELIMINATION OF MINORITY PARTNER INTEREST	(78,707)	(95,963)
	-----	-----

Edgar Filing: SHELLS SEAFOOD RESTAURANTS INC - Form 10-Q

INCOME (LOSS) BEFORE PROVISION FOR INCOME TAXES	(3,018,451)	1,472,187
PROVISION FOR INCOME TAXES	--	(486,000)
	-----	-----
NET INCOME (LOSS)	\$ (3,018,451)	\$ 986,187
	=====	=====
BASIC NET INCOME (LOSS) PER SHARE OF COMMON STOCK	\$ (0.68)	\$ 0.22
	=====	=====
BASIC WEIGHTED AVERAGE NUMBER OF SHARES OF COMMON STOCK OUTSTANDING	4,454,015	4,454,015
	=====	=====
DILUTED NET INCOME (LOSS) PER SHARE OF COMMON STOCK	\$ (0.68)	\$ 0.22
	=====	=====
DILUTED WEIGHTED AVERAGE NUMBER OF SHARES OF COMMON STOCK OUTSTANDING	4,454,015	4,454,083
	=====	=====

SEE NOTES TO CONSOLIDATED FINANCIAL STATEMENTS.

4

SHELLS SEAFOOD RESTAURANTS, INC. AND SUBSIDIARIES  
CONSOLIDATED STATEMENTS OF CASH FLOWS

	13 WEEKS ENDED	
	APRIL 1, 2001	APRIL 2, 2001
	-----	-----
OPERATING ACTIVITIES:		
Net income (loss)	\$ (3,018,451)	\$ 986,187
Adjustments to reconcile net income to net cash (used in) provided by operating activities:		
Provision for impairment of assets	1,582,137	--
Depreciation and amortization	536,022	676,549
Minority partner interest	(6,293)	(19,037)
Changes in assets and liabilities:		
Decrease (increase) in inventories	66,672	(75,307)
Decrease (increase) in receivables from related parties	123,539	(21,740)
Increase in other assets	(359,582)	(803,867)
Decrease in prepaid rent	12,600	19,569
Decrease in deferred tax asset	114,782	484,290
(Decrease) increase in accounts payable	(105,329)	856,092
Increase in accrued expenses	513,808	256,616
Increase in sales tax payable	164,619	189,455
Increase in deferred rent	15,971	81,002
	-----	-----
Total adjustments	2,658,946	1,643,622
	-----	-----
Net cash (used in) provided by operating activities	(359,505)	2,629,809
	-----	-----
INVESTING ACTIVITIES:		
Purchase of property and equipment	(340,310)	(244,542)

## Edgar Filing: SHELLS SEAFOOD RESTAURANTS INC - Form 10-Q

Net cash used in investing activities	(340,310)	(244,542)
<b>FINANCING ACTIVITIES:</b>		
Proceeds from debt financing	227,636	245,432
Repayment of debt	(418,385)	(260,539)
Net cash used in financing activities	(190,749)	(15,107)
Net (decrease) increase in cash	(890,564)	2,370,160
CASH AT BEGINNING OF PERIOD	1,261,937	2,940,919
CASH AT END OF PERIOD	\$ 371,373	\$ 5,311,079
Supplemental disclosure of cash flow information:		
Cash paid for interest	\$ 188,786	\$ 224,451
Cash (refunds received) paid for income taxes	\$ (114,781)	\$ 1,710

SEE NOTES TO CONSOLIDATED FINANCIAL STATEMENTS.

5

### SHELLS SEAFOOD RESTAURANTS, INC. AND SUBSIDIARIES NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (UNAUDITED)

#### 1. BASIS OF PRESENTATION

The accompanying unaudited consolidated financial statements have been prepared in accordance with the instructions for Form 10-Q and, therefore, these statements do not include all of the information and footnotes required by generally accepted accounting principles for annual financial statements. In the opinion of management, all material adjustments (consisting of normal recurring adjustments) considered necessary for a fair presentation have been included.

The consolidated financial statements of Shells Seafood Restaurants, Inc. (the "Company") should be read in conjunction with the audited consolidated financial statements and notes thereto contained in the Form 10-K for the year ended December 31, 2000 filed with the Securities and Exchange Commission. Company management believes that the disclosures are sufficient for interim financial reporting purposes. Certain prior year amounts have been reclassified in the accompanying condensed consolidated financial statements to conform with the current year presentation.

#### 2. EARNINGS PER SHARE

The following table represents the computation of basic and diluted earnings per share of common stock as required by Statement of Financial Accounting Standards ("SFAS") No. 128, "Earnings Per Share":

13 WEEKS ENDED	
APRIL 1, 2001	APRIL 2, 2000
-----	-----

Edgar Filing: SHELLS SEAFOOD RESTAURANTS INC - Form 10-Q

Net income (loss) applicable to common stock	\$ (3,018,451)	\$ 986,187
	=====	=====
Weighted common shares outstanding	4,454,015	4,454,015
Basic net income (loss) per share of common stock	\$ (0.68)	\$ 0.22
Effect of dilutive securities:		
Warrants	--	--
Stock options	--	68
	-----	-----
Diluted weighted common shares outstanding	4,454,015	4,454,083
	-----	-----
Diluted net income per share of common stock	\$ (0.68)	\$ 0.22
	=====	=====

The earnings per share calculations excluded 1,411,425 options and warrants and 1,400,125 options and warrants during the first quarter of 2001 and 2000, respectively, as the exercise price of the options and warrants were greater than the average market price of the common shares.

3. NEW ACCOUNTING PRONOUNCEMENT

Statement of Financial Accounting Standards ("SFAS") No. 133, "Accounting for Derivative Instruments and Hedging Activities", establishes accounting and reporting standards for derivative instruments and hedging activities. It requires that an entity recognize all derivatives as either assets or liabilities in the balance sheet and measure those instruments at fair value. The accounting for changes in the fair value of a derivative (that is gains and losses) depends upon the intended use of the derivative and the resulting designation. SFAS No. 133, as amended, will be effective for all fiscal quarters of fiscal years beginning after June 15, 2000. The adoption of SFAS No. 133 is not expected to materially affect the Company's consolidated financial statements.

6

ITEM 2. MANAGEMENT'S DISCUSSION AND ANALYSIS OF FINANCIAL CONDITION AND RESULTS OF OPERATIONS

The following table sets forth, for the periods indicated, the percentages which the items in the Company's Consolidated Statements of Income bear to total revenues.

	13 WEEKS ENDED	
	APRIL 1, 2001	APRIL 2, 2000
	-----	-----
REVENUES	100.0%	100.0%
COST AND EXPENSES:		
Cost of revenues	37.6%	35.8%
Labor and other related expenses	29.8%	28.6%
Other restaurant operating expenses	21.2%	19.1%
	-----	-----
Total restaurant costs and expenses	88.6%	83.5%
	-----	-----
General and administrative expenses	7.8%	7.0%
Depreciation and amortization	2.5%	2.6%

## Edgar Filing: SHELLS SEAFOOD RESTAURANTS INC - Form 10-Q

Provision for impairment of assets	7.3%	0.0%
Provision for store closings	6.2%	0.0%
	-----	-----
Income (loss) from operations	(12.4)%	6.8%
	-----	-----
Interest expense, net	(0.9)%	(0.7)%
Other expense, net	(0.3)%	0.0%
Elimination of minority partner interest	(0.4)%	(0.4)%
	-----	-----
Income (loss) before provision for taxes	(14.0)%	5.7%
Provision for income taxes	0.0%	(1.9)%
	-----	-----
Net income (loss)	(14.0)%	3.8%
	=====	=====

7

13 WEEKS ENDED APRIL 1, 2001 AND APRIL 2, 2000

REVENUES. Total revenues for the first quarter of 2001 were \$21,655,000 as compared to \$25,851,000 for the first quarter of 2000. The \$4,196,000, or 16.2% decrease in revenues was due to the closing of four restaurants in the fourth quarter of 2000 and an additional six restaurants in the first quarter of 2001, and by a 5.4% decrease in comparable store sales. Comparisons of same store sales include only stores, which were open during the entire periods being compared and, due to the time needed for a restaurant to become established and fully operational, at least six months prior to the beginning of that period.

COST OF REVENUES. The cost of revenues as a percentage of revenues increased to 37.6% for the first quarter of 2001 from 35.8% for the first quarter of 2000. This increase primarily was due to rising shrimp costs coupled with menu changes and resulting shifts in customer preferences. The Company is continually anticipating and reacting to fluctuations in food costs by purchasing seafood directly from numerous suppliers, promoting certain alternative menu selections in response to price and availability of supply and adjusting its menu prices accordingly to help control the cost of revenues.

LABOR AND OTHER RELATED EXPENSES. Labor and other related expenses as a percentage of revenues increased to 29.8% during the first quarter of 2001 as compared to 28.6% for the first quarter of 2000. This increase was primarily attributable to labor inefficiencies in the Company's Midwest restaurants and general increases in hourly wage rates. Also included is a one-time nonrecurring charge of \$102,000 for severance pay primarily related to store closings in the Midwest.

OTHER RESTAURANT OPERATING EXPENSES. Other restaurant operating expenses as a percentage of revenues increased to 21.2% for the first quarter of 2001 as compared with 19.1% for the first quarter of 2000. The increase primarily was due to increased advertising costs mostly in the Florida markets and an increase in utility costs associated with fuel prices.

GENERAL AND ADMINISTRATIVE EXPENSES. General and administrative expenses as a percentage of revenues increased to 7.8% for the first quarter of 2001 as compared with 7.0% for the first quarter of 2000. The increase was due to increased salaries and wages and related travel costs resulting from the hiring of an additional director of operations for the Florida market in fiscal 2000. Also included is a one-time nonrecurring charge of \$150,000 for severance pay related to reorganization and downsizing of administrative and supervisory staff.

## Edgar Filing: SHELLS SEAFOOD RESTAURANTS INC - Form 10-Q

DEPRECIATION AND AMORTIZATION. Depreciation and amortization expense as a percentage of revenues decreased to 2.5% for the first quarter of 2001 from 2.6% in the first quarter of 2000. The decrease primarily was due to the reduced basis of property and equipment resulting from the recognition of asset impairments in the third quarter of 2000.

PROVISION FOR IMPAIRMENT OF ASSETS. The Company recorded a \$1,582,000 charge relating to the write-down of impaired assets to their estimated fair value in accordance with Statement of Financial Accounting Standards No. 121. The asset impairment charge related to 14 restaurants, 13 restaurants in the Midwest and one restaurant in Florida. Eleven of the 14 restaurants had incurred previous write-downs in the third quarter of 2000. The Company subsequently decided to close most of these under-performing units in which six units were closed during the first quarter of 2001 and additional six units were closed during the second quarter of 2001. The Company is presently in negotiations with an unaffiliated entity to continue to operate the three remaining Midwest units as Shells restaurants under a licensing arrangement.

PROVISION FOR STORE CLOSINGS. The Company recorded a one-time charge of \$1,333,000 relating to store closing costs primarily related to restaurants in the Midwest. The Midwest restaurants were closed during the first and second quarters of 2001 due to poor operating results. Store closing costs consist primarily of real estate lease obligations incurred or anticipated to complete lease terminations or continuing costs while new tenants are located.

8

PROVISION FOR INCOME TAXES. A provision for income taxes of \$0 was recognized for the first quarter of 2001 as compared to \$486,000 during the same quarter in 2000. The decrease related to the net loss before the provision for income taxes incurred for the first quarter 2001.

INCOME (LOSS) FROM OPERATIONS AND NET INCOME (LOSS). As a result of the factors discussed above, the Company incurred a loss from operations of \$2,688,000 for the first quarter of 2001 as compared to income from operations of \$1,771,000 for the first quarter of 2000. The Company incurred a net loss of \$3,018,000 for the first quarter of 2001 compared to net income of \$986,000 for the first quarter of 2000. Exclusive of nonrecurring charges of \$3,167,000, first quarter 2001 net income was \$149,000.

### LIQUIDITY AND CAPITAL RESOURCES

As of April 1, 2001, the Company's current liabilities of \$11,656,000 exceeded its current assets of \$2,915,000, resulting in a working capital deficiency of \$8,741,000. A decrease in revenues resulting from fewer restaurants in operation and a decrease in comparable store sales, coupled by increased operating costs and costs incurred to close six restaurants during the first quarter of 2001, negatively affected cash. Historically, the Company has generally operated with minimal or negative working capital as a result of the investing of current assets into non-current property and equipment as well as the turnover of restaurant inventory relative to more favorable vendor terms in accounts payable.

The Company continues to be negatively impacted by its Midwest locations. The Company is implementing its plan to divest itself of the Midwest restaurants. Such divestiture has had and, in the near term, will continue to have an adverse affect on the Company's cash position and operating results. The Company anticipates requiring additional outside financing during the second and third quarters of 2001. There can be no assurance that any such financing will be



## Edgar Filing: SHELLS SEAFOOD RESTAURANTS INC - Form 10-Q

available to the Company on terms acceptable to the Company, or at all. In addition, in view of the closure of several restaurants and restructuring of the Company, as well as the present inability to supply adequate security for any borrowing, the Company's line of credit is not available to be drawn upon.

Cash used by operating activities for the first quarter of 2001 was \$360,000 as compared to cash provided by operating activities of \$2,630,000 for the first quarter of 2000. The net decrease of \$2,989,000 primarily was attributable to less favorable store operating results in first quarter 2001 in addition to costs incurred to close six restaurants.

The cash used in investing activities increased to \$340,000 for the first quarter of 2001 compared to \$245,000 for the first quarter of 2000. The increase of \$95,000 was due to the completion of remodeling of six Florida restaurants started in fourth quarter.

The cash used in financing activities was \$191,000 for the first quarter of 2001 compared to \$15,000 in the first quarter of 2000. The increase in cash used in financing activities primarily was due to debt repayments associated with stores closed in 2001 and 2000.

### SEASONALITY

The restaurant industry in general is seasonal, depending on restaurant location and the type of food served. The Company has experienced fluctuations in its quarter-to-quarter operating results due primarily to its high concentration of restaurants in Florida. Business in Florida is influenced by seasonality due to various factors which include but are not limited to weather conditions in Florida relative to other areas of the U.S. and the health of Florida's economy in general and the tourism industry in particular. The Company's restaurant sales are generally highest from January through April and June through August, the peaks of the Florida tourism season, and generally lower from September through mid-December. In many cases, locations are in coastal cities, where sales are significantly dependent on tourism and its seasonality patterns.

9

In addition, quarterly results have been, and in the future could be, affected by the timing and conditions under which restaurants are closed both in and outside of Florida. Because of the seasonality of the Company's business and the impact of restaurant closures and openings, if applicable, results for any quarter are not generally indicative of the results that may be achieved for a full fiscal year on an annualized basis and cannot be used to indicate financial performance for the entire year.

### ITEM 3. - QUANTITATIVE AND QUALITATIVE DISCLOSURES ABOUT MARKET RISK

The Company is exposed to market risk from changes in interest rates on debt and changes in commodity prices. The Company's exposure to interest rate risk relates to its \$3,220,000 in outstanding debt with banks that is based on variable rates. Borrowings under the loan agreements bear interest at rates ranging from 50 basis points under the prime lending rate to 100 basis points over the prime lending rate. There is also one loan that is based on 225 basis points over the 30 day London Interbank Offered Rate.

10

Edgar Filing: SHELLS SEAFOOD RESTAURANTS INC - Form 10-Q

PART II - OTHER INFORMATION

Item 1 - Legal Proceedings

None

Item 2 - Changes in Securities and Use of Proceeds

None

Item 3 - Defaults Upon Senior Securities

None

Item 4 - Submission of Matters to a Vote of Security Holders

None

Item 5 - Other Information

None

Item 6 - Exhibits and Reports on Form 8-K

None

11

SIGNATURES

Pursuant to the requirements of the Securities Exchange Act of 1934, the registrant has duly caused this report to be signed on its behalf by the undersigned thereunto duly authorized.

SHELLS SEAFOOD RESTAURANTS, INC.  
(Registrant)

/s/ DAVID W. HEAD

Date May 16, 2001

-----  
David W. Head  
President and Chief Executive Officer

/s/ WARREN R. NELSON

Date May 16, 2001

-----  
Warren R. Nelson  
Executive Vice President and  
Chief Financial Officer

12