RED ROBIN GOURMET BURGERS INC
Form 10-Q
May 17, 2012
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UNITED STATES

SECURITIES AND EXCHANGE COMMISSION

Washington, D.C. 20549

FORM 10-Q

(Mark One)

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

For the quarterly period ended April 15, 2012

or

o 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: 0-49916

RED ROBIN GOURMET BURGERS, INC.

(Exact name of registrant as specified in its charter)

Delaware	**84-1573084**
(State or other jurisdiction of incorporation or organization)	(I.R.S. Employer Identification No.)
6312 S. Fiddler s Green Circle, Suite 200N **Greenwood Village, CO**	**80111**
(Address of principal executive offices)	(Zip Code)

(303) 846-6000

(Registrant s telephone number, including area code)

(Former name, former address and former fiscal year, if changed since last report)

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 x No o

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 (§232.405 of this chapter) during the preceding 12 months (or for such shorter period that the registrant was required to submit and post such files). Yes x No o

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 o	Accelerated filer x
Non-accelerated filer o (Do not check if a smaller reporting company)	Smaller reporting company o

Indicate by check mark whether the registrant is a shell company (as defined in Rule 12b-2 of the Exchange Act). Yes o No x

Indicate the number of shares outstanding of each of the issuer s classes of common stock, as of the latest practicable date.

Class	Outstanding at May 15, 2012
Common Stock, $0.001 par value per share	14,686,943 shares

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PART I FINANCIAL INFORMATION

Item 1. **Financial Statements**

RED ROBIN GOURMET BURGERS, INC.

CONDENSED CONSOLIDATED BALANCE SHEETS

(In thousands, except share amounts)

(Unaudited)

	April 15, 2012	December 25, 2011
Assets:		
Current Assets:		
Cash and cash equivalents	$ 37,977	$ 35,036
Accounts receivable, net	9,621	14,785
Inventories	17,318	18,040
Prepaid expenses and other current assets	9,180	9,970
Income tax receivable	155	1,387
Deferred tax asset	2,096	1,429
Total current assets	76,347	80,647
Property and equipment, net	398,911	402,360
Goodwill	61,769	61,769
Intangible assets, net	37,874	38,969
Other assets, net	10,576	9,231
Total assets	$ 585,477	$ 592,976
Liabilities and Stockholders Equity:		
Current Liabilities:		
Trade accounts payable	$ 13,221	$ 14,798
Construction related payables	5,003	3,328
Accrued payroll and payroll related liabilities	30,620	35,044
Unearned revenue	16,545	24,139
Accrued liabilities	25,537	19,045
Current portion of term loan notes payable and capital lease obligations	12,031	10,132
Total current liabilities	102,957	106,486
Deferred rent	42,020	40,025
Notes payable, long-term portion	116,250	136,875
Other long-term debt and capital lease obligations	9,666	9,924
Other non-current liabilities	6,082	4,968
Total liabilities	276,975	298,278
Stockholders Equity:		
	17	17

Common stock; $0.001 par value: 30,000,000 shares authorized; 17,388,036 and 17,276,404 shares issued; 14,690,889 and 14,579,257 shares outstanding				
Preferred stock, $0.001 par value: 3,000,000 shares authorized; no shares issued and outstanding				
Treasury stock, 2,697,147 shares, at cost		(83,285)		(83,285)
Paid-in capital		181,577		178,111
Accumulated other comprehensive income (loss), net of tax		(545)		(326)
Retained earnings		210,738		200,181
Total stockholders equity		308,502		294,698
Total liabilities and stockholders equity	$	585,477	$	592,976

See notes to condensed consolidated financial statements.

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RED ROBIN GOURMET BURGERS, INC.

CONDENSED CONSOLIDATED STATEMENTS OF OPERATIONS

(In thousands, except per share data)

(Unaudited)

	Sixteen Weeks Ended	
	April 15, 2012	**April 17, 2011**
Revenues:		
Restaurant revenue	$ 294,642	$ 281,548
Franchise royalties and fees and other revenues	4,817	5,282
Total revenues	299,459	286,830
Costs and expenses:		
Restaurant operating costs (exclusive of depreciation and amortization shown separately below):		
Cost of sales	75,075	70,361
Labor (includes $143 and $245 of stock- based compensation, respectively)	98,606	96,871
Operating	37,405	38,761
Occupancy	21,114	19,828
Depreciation, amortization and other	16,652	17,111
Selling, general, and administrative (includes $1,059 and $613 of stock-based compensation, respectively)	33,877	32,042
Pre-opening costs	983	661
Total costs and expenses	283,712	275,635
Income from operations	15,747	11,195
Other expense:		
Interest expense, net and other	1,833	1,355
Income before income taxes	13,914	9,840
Income tax expense	3,356	1,132
Net income	$ 10,558	$ 8,708
Earnings per share:		
Basic	$ 0.72	$ 0.56
Diluted	$ 0.71	$ 0.56
Weighted average shares outstanding:		
Basic	14,611	15,466
Diluted	14,984	15,641

See notes to condensed consolidated financial statements.

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RED ROBIN GOURMET BURGERS, INC.

CONDENSED CONSOLIDATED STATEMENTS OF COMPREHENSIVE INCOME

(In thousands)

(Unaudited)

	Sixteen Weeks Ended	
	April 15, 2012	**April 17, 2011**
Comprehensive income	$ 10,339	$ 8,905

See notes to condensed consolidated financial statements.

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RED ROBIN GOURMET BURGERS, INC.

CONDENSED CONSOLIDATED STATEMENTS OF CASH FLOWS

(In thousands)

(Unaudited)

	Sixteen Weeks Ended	
	April 15, 2012	April 17, 2011
Cash Flows From Operating Activities:		
Net income	$ 10,558	$ 8,708
Adjustments to reconcile net income to net cash provided by operating activities:		
Depreciation, amortization and other	16,652	17,111
Gift card breakage	(224)	(757)
Stock-based compensation expense	1,202	858
Other, net	394	(1,036)
Changes in operating assets and liabilities	970	5,034
Cash provided by operating activities	29,552	29,918
Cash Flows From Investing Activities:		
Purchases of property and equipment	(10,447)	(7,628)
Proceeds from sales of property	382	
Changes in marketing fund restricted cash	480	123
Cash used in investing activities	(9,585)	(7,505)
Cash Flows From Financing Activities:		
Borrowings of long-term debt		28,000
Payments of long-term debt	(18,750)	(44,370)
Payments to acquire Treasury Stock		(9,537)
Proceeds from exercise of stock options and employee stock purchase plan	1,958	530
Payments of other debt and capital lease obligations	(234)	(313)
Cash used in financing activities	(17,026)	(25,690)
Net change in cash and cash equivalents	2,941	(3,277)
Cash and cash equivalents, beginning of period	35,036	17,889
Cash and cash equivalents, end of period	$ 37,977	$ 14,612
Supplemental Disclosure of Cash Flow Information:		
Income taxes paid	$ 199	$ 41
Interest paid, net of amounts capitalized	1,901	1,306

See notes to condensed consolidated financial statements.

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RED ROBIN GOURMET BURGERS, INC.

NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS

(Unaudited)

1. Basis of Presentation and Recent Accounting Pronouncements

Red Robin Gourmet Burgers, Inc., a Delaware corporation, together with its subsidiaries (Red Robin or the Company), develops and operates casual-dining restaurants. At April 15, 2012, the Company operated 330 company-owned restaurants located in 32 states. The Company operates its business as one operating and one reportable segment. The Company also franchises its restaurants, of which there were 136 restaurants in 21 states and two Canadian provinces as of April 15, 2012.

Basis of Presentation

The accompanying unaudited condensed consolidated financial statements include the accounts of Red Robin and its wholly owned subsidiaries. All intercompany accounts and transactions have been eliminated in consolidation. The Company s financial statements have been prepared in accordance with accounting principles generally accepted in the United States of America (GAAP) for interim financial information and with the instructions to Form 10-Q and Article 10 of Regulation S-X. In the opinion of management, all adjustments (consisting of normal recurring adjustments) considered necessary for a fair presentation have been included. The preparation of financial statements in conformity with GAAP requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities and disclosure of contingent assets and liabilities at the date of the financial statements and the reported amounts of revenues and expenses during the reporting period. Some of the more significant estimates included in the preparation of these financial statements pertain to recoverability of long-lived assets, recoverability of goodwill, estimated useful lives of other intangible assets, variable compensation accruals, lease accounting, estimated fair value, self-insurance liabilities, stock-based compensation expense, estimated breakage on unredeemed gift cards and deferred revenue related to our customer loyalty program, legal contingencies, and income taxes. Actual results could differ from those estimates. The results of operations for any interim period are not necessarily indicative of results for the full year.

The accompanying condensed consolidated financial statements of Red Robin have been prepared pursuant to the rules and regulations of the Securities and Exchange Commission (the SEC). Certain information and footnote disclosures normally included in the Company s annual consolidated financial statements on Form 10-K have been condensed or omitted. The condensed consolidated balance sheet as of December 25, 2011, has been derived from the audited consolidated financial statements as of that date, but does not include all disclosures required by generally accepted accounting principles. For further information, please refer to and read these interim condensed consolidated financial statements in conjunction with the Company s audited consolidated financial statements included in the Company s Annual Report on Form 10-K for the fiscal year ended December 25, 2011 filed with the SEC on February 23, 2012.

The Company s quarter which ended April 15, 2012, is referred to as first quarter 2012, or the sixteen weeks ended April 15, 2012; the first quarter ended April 17, 2011, is referred to as first quarter 2011, or the sixteen weeks ended April 17, 2011.

Recent Accounting Pronouncements

In May 2011, the FASB issued, Amendments to Achieve Common Fair Value Measurement and Disclosure Requirements in U.S. GAAP and International Financial Reporting Standards (IFRS). This pronouncement was issued to provide a consistent definition of fair value and ensure that the fair value measurement and disclosure requirements are similar between U.S. GAAP and IFRS. This guidance changes certain fair value measurement principles and enhances the disclosure requirements particularly for Level 3 fair value measurements. This pronouncement is effective for reporting periods beginning on or after December 15, 2011. The adoption of this guidance did not have a significant impact on the Company s consolidated financial position, results of operations, or disclosures.

In June 2011, the FASB finalized guidance on the Presentation of Comprehensive Income, which revises the manner in which entities present comprehensive income in their financial statements. The new guidance removes the presentation options and requires entities to report components of comprehensive income in either (1) a continuous statement of comprehensive income or (2) two separate but consecutive statements. Under the two-statement approach, the first statement would include components of net income, which is consistent with the income statement format used today, and the second statement would include components of other comprehensive income (OCI). This guidance is effective for fiscal years and interim periods within those years beginning after December 15, 2011. In December 2011, the FASB issued a Deferral of the Effective Date for Amendments to the Presentation of Reclassification of Items Out of Accumulated Other Comprehensive Income. This defers only the changes that relate to the presentation of reclassification adjustments on the face of the financial statements where the components of net income and the components of other comprehensive income are presented. These amendments are to be applied retrospectively and are effective for

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fiscal years, and interim periods within those years, beginning after December 15, 2011. The adoption of this guidance did not have a significant impact on the Company s consolidated financial position, results of operations, or disclosures.

In September 2011, the FASB finalized guidance on Testing Goodwill for Impairment. The new guidance simplifies how entities test goodwill for impairment and permits an entity to first assess qualitative factors to determine whether it is more likely than not that the fair value of a reporting unit is less than its carrying amount as a basis for determining whether it is necessary to perform the two-step goodwill impairment test. This guidance is effective for fiscal years beginning after December 15, 2011. The Company has the option of adopting the guidance. If adopted, the guidance is not expected to have a significant impact on the Company s consolidated financial position or results of operations.

2. Restaurant Impairment and Closures

The Company closed one restaurant in the first quarter of 2012, and no impairments to restaurants were recorded during first quarter 2012. The Company closed no restaurants in the first quarter of 2011, and no impairments to restaurants were recorded during first quarter 2011.

3. Stock-Based Compensation

Stock Options

During the sixteen weeks ended April 15, 2012, the Company issued 97,000 options under the Second Amended and Restated 2007 Performance Incentive Plan (the Stock Plan) with a weighted average grant date fair value of $14.60 per share and a weighted average exercise price of $35.44 per share. Compensation expense for these options is recognized over the remaining vesting period less expected forfeitures. The weighted average vesting period for all options outstanding is approximately 1.4 years. The Company issued 23,000 options with a weighted average grant date fair value of $10.36 per share and a weighted average exercise price of $24.26 per share during the sixteen weeks ended April 17, 2011.

The fair value of options at the grant date was estimated utilizing the Black-Scholes multiple option-pricing model with the following weighted average assumptions for the periods presented:

	Sixteen Weeks Ended	
	April 15, 2012	**April 17, 2011**
Risk-free interest rate	0.7%	1.3%
Expected years until exercise	4.1	3.4
Expected stock volatility	52.8%	60.8%
Dividend yield	0.0%	0.0%
Weighted-average Black-Scholes fair value per share at date of grant	$ 14.60	$ 10.36

Restricted Stock

The Company did not issue any shares of restricted stock during the sixteen weeks ended April 15, 2012 or during the sixteen weeks ended April 17, 2011. Compensation expense for the aggregate 4,000 shares of non-vested common stock outstanding at April 15, 2012 is recognized over the remaining vesting period, less expected forfeitures. The remaining weighted average vesting period is approximately 0.7 years. These awards vest in installments over four years on the anniversary dates.

Time Based RSUs

During the sixteen weeks ended April 15, 2012, the Company granted 30,000 time based restricted stock units (RSUs) to employees under the Stock Plan with a weighted average grant date fair value of $35.47. The fair value of each RSU granted is equal to the market price of the Company s stock at date of grant. Compensation expense for RSUs is recognized over the vesting period, less expected forfeitures. The Company granted 3,000 RSUs under the Stock Plan with a weighted average grant date fair value of $24.05 during the sixteen weeks ended April 17, 2011.

The weighted average vesting period for all RSUs outstanding is approximately 1.5 years. The RSUs granted to employees vest in equal installments over three to four years on the anniversary date and, upon vesting, the Company issues one share of the Company s common stock for each RSU. The RSUs granted to non-employee directors are scheduled to vest in three equal

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installments on the first, second, and third anniversaries of the date of grant and the shares underlying the units will be distributed upon vesting.

Performance Based RSUs

During the sixteen weeks ended April 15, 2012 and April 17, 2011, the Company granted no performance based restricted stock units (PSUs). During 2010, the Company issued 40,500 and 20,400 PSUs under its 2007 Stock Plan with a grant date fair value of $35.90 and $33.01, respectively. These PSUs are subject to Company performance metrics based on Total Shareholder Return and measure the overall stock price performance of the Company to the stock price performance of a selected industry peer group, thus resulting in a market condition. The actual number of PSUs subject to the awards will be determined at the end of the performance period based on the performance metrics. The fair value of the PSUs is calculated using the Monte Carlo valuation method. This method utilizes multiple input variables to determine the probability of the Company achieving the market condition and the fair value of the awards. These awards have a three-year performance period and are classified as equity because each unit is convertible into one share of the Company s common stock upon vesting. Compensation expense is recognized on a straight-line basis over the requisite service period (or to an employee s eligible retirement date, if earlier).

4. Earnings Per Share

Basic earnings (loss) per share amounts are calculated by dividing net income (loss) by the weighted-average number of common shares outstanding during the period. Diluted earnings (loss) per share amounts are calculated based upon the weighted-average number of common shares and potentially dilutive shares of common stock outstanding during the period. Potentially dilutive shares are excluded from the computation in periods in which they have an anti-dilutive effect. Diluted earnings per share reflect the potential dilution that could occur if holders of options exercised their options into common stock. During the sixteen weeks ended April 15, 2012, weighted stock options outstanding of 280,000 were not included in the computation of diluted earnings per share because to do so would have been anti-dilutive for the periods presented. During the sixteen weeks ended April 17, 2011, weighted stock options outstanding of 389,000 were not included in the computation of diluted earnings per share because to do so would have been anti-dilutive for the periods presented. The Company uses the treasury stock method to calculate the effect of outstanding stock options. The computations for basic and diluted earnings (loss) per share are as follows (in thousands, except per share data):

	Sixteen Weeks Ended	
	April 15, 2012	**April 17, 2011**
Net income	$ 10,558	$ 8,708
Basic weighted-average shares outstanding	14,611	15,466
Dilutive effect of stock options and awards	283	175
Diluted weighted-average shares outstanding	14,984	15,641
Earnings (loss) per share:		
Basic	$ 0.72	$ 0.56
Diluted	$ 0.71	$ 0.56

5. Acquisition of Red Robin Franchised Restaurants

On April 9, 2012, the Company entered into an agreement with one of its franchisees to purchase one restaurant location in Clifton, New Jersey. The purchase price will be approximately $3 million and is expected to close in second or third quarter 2012, subject to a variety of customary closing conditions.

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6. Gift Card Breakage

The Company sells gift cards which do not have an expiration date, and it does not deduct dormancy fees from outstanding gift card balances. The Company recognizes revenue from gift cards when: (i) the gift card is redeemed by the customer or (ii) the likelihood of the gift card being redeemed by the customer is remote, and the Company determines that there is not a legal obligation to remit the unredeemed gift card balance to the relevant jurisdiction (gift card breakage). The determination of the gift card breakage rate is based upon the Company s specific historical redemption patterns. The Company recognizes gift card breakage by applying its estimate of the rate of gift card breakage over the period of estimated performance (generally, 24 months). The Company completed initial analysis of unredeemed gift card liabilities for gift cards sold in third party locations during the first quarter of 2011 and recognized $438,000 into revenue as an initial adjustment. For the sixteen weeks ended April 15, 2012, the Company recognized gift card breakage of $224,000. For the sixteen weeks ended April 17, 2011, the Company recognized $757,000 (inclusive of the initial cumulative program adjustment for third party gift card sales). Gift card breakage is included in other revenue in the consolidated statements of operations.

7. Advertising Costs

Costs incurred in connection with the advertising and marketing of the Company are included in selling, general, and administrative expenses. These costs include salaries, variable compensation, advertising, media, and marketing materials. Media costs are expensed as incurred or when the advertisement first runs. Such costs amounted to $9.9 million and $8.9 million for the sixteen weeks ended April 15, 2012 and April 17, 2011, respectively.

Under the Company s franchise agreements, both the Company and the franchisees must contribute a minimum percentage of revenues to two marketing and national media advertising funds (the Marketing Funds). These Marketing Funds are used to develop and distribute Red Robin branded marketing materials, for media purchases and for administrative costs. The Company s portion of costs incurred by the Marketing Funds is recorded as selling, general, and administrative expenses in the Company s financial statements.

8. Derivative and Other Comprehensive Income

The Company enters into derivative instruments for risk management purposes only, including derivatives designated as a cash flow hedge under guidance for derivative instruments and hedging activities. The Company uses interest rate-related derivative instruments to manage its exposure to fluctuations in interest rates. By using these instruments, the Company exposes itself, from time to time, to credit risk and market risk. Credit risk is the failure of either party to the contract to perform under the terms of the derivative contract. When the fair value of a derivative contract is positive, the counterparty owes the Company, which creates credit risk for the Company. The Company minimizes the credit risk by entering into transactions with high-quality counterparties whose credit rating is evaluated on a quarterly basis. The Company has one interest rate swap at April 15, 2012 and its counterparty is Rabobank International, Utrecht (Rabobank). Market risk, as it relates to the Company s interest-rate derivative, is the adverse effect on the value of a financial instrument that results from changes in interest rates. The Company minimizes market risk by establishing and monitoring parameters that limit the types and degree of market risk that the Company takes.

In August 2011, the Company entered into a variable-to-fixed interest rate swap agreement with Rabobank to hedge the Company s floating interest rate on half of the remaining term loan that is outstanding at April 15, 2012 under the Company s amended and restated credit facility, or $71.3 million notional at April 15, 2012. The interest rate swap has an effective date of August 5, 2011, in accordance with its original terms $1.9 and $0.9 million of the initial $74.1 million expired in 2012 and 2011, respectively. The notional amount of the hedge will decrease quarterly based on the remaining required principal term loan payments, and will expire on June 30, 2015 with a notional hedge amount of $50.6 million. The Company is required to make quarterly payments based on a fixed interest rate of 1.135%, calculated based on the remaining notional amount. In exchange, the Company receives interest on the notional amount at a variable rate that is based on the 3-month spot LIBOR rate quarterly. The Company entered into this interest rate swap to offset the variability of its interest expense arising out of changes in the variable interest rate for the designated interest payments and designated the swap as a cash flow hedge. Accordingly, changes in fair value of the interest rate swap contract are recorded, net of taxes, as a component of accumulated other comprehensive loss (AOCL) in the accompanying condensed consolidated balance sheets. The Company reclassifies the effective gain or loss from AOCL, net of tax, on the Company s consolidated balance sheet to interest expense on the Company s consolidated statements of income as the interest expense is recognized on the related debt.

In March 2008, the Company entered into a variable-to-fixed interest rate swap agreement with SunTrust to hedge the Company s floating interest rate on an aggregate of up to $120 million of debt that was outstanding under the Company s amended and restated credit facility. The interest rate swap had an effective date of March 19, 2008, and $50 million of the initial $120 million expired on March 19, 2010, and the remaining $70 million expired on March 19, 2011, in accordance with its original terms. The

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Company was required to make payments based on a fixed interest rate of 2.7925%, calculated on the remaining notional amount of $70 million. In exchange, the Company received interest on $70 million of the notional amount at a variable rate that was based on the 3-month LIBOR rate. The Company entered into this interest rate swap with the objective of offsetting the variability of its interest expense that arises because of changes in the variable interest rate for the designated interest payments and designated the swap as a cash flow hedge since its inception. Accordingly, changes in fair value of the interest rate swap contract were recorded, net of taxes, as a component of accumulated other comprehensive loss (AOCL) in the accompanying condensed consolidated balance sheets. The Company reclassifies the effective gain or loss from AOCL, net of tax, on the Company s consolidated balance sheet to interest expense on the Company s consolidated statements of income as the interest expense is recognized on the related debt.

The following table summarizes the fair value and presentation in the condensed consolidated balance sheets of the interest rate swap as hedging instruments as of April 15, 2012 and December 25, 2011 (in thousands):

	Derivative Liability	
Balance Sheet Location	**Fair value at April 15, 2012**	**Fair value at December 25, 2011**
Accrued liabilities	$ 442	$ 449
Other non-current liabilities	451	85
Total derivatives	$ 893	$ 534

The following table summarizes the effect of the interest rate swap on the condensed consolidated statements of operations for the sixteen weeks ended April 15, 2012 and April 17, 2011 (in thousands):

	Sixteen Weeks Ended	
	April 15, 2012	**April 17, 2011**
Unrealized gain (loss) on swap in AOCL (pretax)	$ (491)	$
Realized gain (loss) [pretax effective portion] recognized in interest expense	$ (131)	$ (408)

As a result of this activity, AOCL increased by $359,000 and $440,000 on a pretax basis or $219,000 and $197,000 on an after tax basis for the sixteen weeks ended April 15, 2012 and April 17, 2011, respectively. The interest rate swap had no hedge ineffectiveness, and as a result, no unrealized gains or losses were reclassified into net earnings as a result of hedge ineffectiveness. The company expects no ineffectiveness in the next twelve months. Additionally, the Company had no obligations at April 15, 2012 to post collateral under the terms of the Interest Rate Swap Agreement.

Comprehensive income consists of net income and other gains and losses affecting stockholders equity that are excluded from net income. Comprehensive income consisted of (in thousands):

	Sixteen Weeks Ended			
		April 15, 2012		April 17, 2011
Net income (loss)	$	10,558	$	8,708
Unrealized gain (loss) on cash flow swap, net of tax		(219)		197
Total comprehensive income (loss)	$	10,339	$	8,905

9. Fair Value Measurement

Fair value measurements are made under a three-tier fair value hierarchy, which prioritizes the inputs used in the measuring of fair value:

Level One: Observable inputs that reflect unadjusted quoted prices in active markets that are accessible at the measurement date for identical, unrestricted assets or liabilities.

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Level Two: Inputs other than quoted prices included in Level 1 that are observable for the asset or liability, either directly or indirectly.

Level Three: Inputs that are generally unobservable. These inputs may be used with internally developed methodologies that result in management s best estimate of fair value.

Assets and Liabilities Measured at Fair Value

The derivative liability associated with the interest rate swap is considered to be a Level Two instrument. The interest rate swap was a standard cash flow hedge with a fair value estimated using industry-standard valuation models. Such models project future cash flows and discount the future amounts to a present value using market-based observable inputs, including interest rate curves. See Note 8, *Derivative and Other Comprehensive Income*, for the discussion of the derivative liability.

The Company s deferred compensation plan is a nonqualified deferred compensation plan which allows highly compensated employees to defer a portion of their base salary, variable compensation and commissions each plan year. The carrying value of both the liability for the deferred compensation plan and associated life insurance policy are equal to their fair value. These agreements are required to be measured at fair value on a recurring basis and are valued using Level Two inputs. At April 15, 2012, and December 25, 2011, a liability for participant contributions and investment income thereon of $2.7 million and $2.6 million, respectively, is included in other non-current liabilities. To offset its obligation, the Company s plan administrator purchases corporate-owned whole-life insurance contracts on certain team members. The cash surrender value of these policies at April 15, 2012, and December 25, 2011, was $2.8 million and $2.5 million, respectively, and is included in other assets, net.

As of April 15, 2012, the Company had no financial assets or liabilities that were measured using Level One or Level Three inputs. The Company also had no non-financial assets or liabilities that were required to be measured at fair value on a recurring basis.

The following table presents our assets and liabilities that are fair valued on a recurring basis for the quarter ended April 15, 2012, and for the fiscal year ended December 25, 2011 (in thousands):

		April 15, 2012		Level One		Level Two		Level Three
Assets:								
Life insurance policy	$	2,776	$		$	2,776	$	
Total assets measured at fair value	$	2,776	$		$	2,776	$	
Liabilities:								
Derivative - interest rate swap	$	893	$		$	893	$	
Deferred compensation plan		2,726				2,726		
Total liabilities measured at fair value	$	3,619	$		$	3,619	$	

	December 25, 2011	Level One	Level Two	Level Three
Assets:				
Life insurance policy	$ 2,534	$	$ 2,534	$
Total assets measured at fair value	$ 2,534	$	$ 2,534	$
Liabilities:				
Derivative - interest rate swap	$ 534	$	$ 534	$
Deferred compensation plan	2,608		2,608	
Total liabilities measured at fair value	$ 3,142	$	$ 3,142	$

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Disclosures of Fair Value of Other Assets and Liabilities

The Company s liabilities under its credit agreement and capital leases are carried at historical cost in the accompanying consolidated balance sheet. For disclosure purposes, we estimate the fair value of the credit facility and capital lease obligations using discounted cash flow analysis based on market rates obtained from independent third parties for similar types of debt. The inputs used to value both the credit facility and the Company s capital lease obligations are considered to be Level 2 instruments. The carrying amount of the Company s credit facility as of April 15, 2012, and December 25, 2011, was approximately $127.5 million and $146.3 million, respectively. The fair value of the Company s credit facility as of April 15, 2012, and December 25, 2011, was approximately $127.5 million and approximately $147.6 million, respectively. There are $10.4 million of outstanding borrowings recorded for the Company s capital leases as of April 15, 2012, which have an estimated fair value of $11.2 million. At December 25, 2011, the carrying amount of the Company s capital lease obligations was $10.7 million, and the fair value was $11.7 million.

10. Related Party Transactions

In 2009, the Company appointed a former franchisee to its board of directors who qualifies as a related party. This board member is a principal of, and holds, directly or indirectly, interests of between 45% and 100% in, each of three privately-held entities that hold the leases for three Company-owned restaurants. The Company acquired the three restaurants as part of a larger acquisition of franchised restaurants in 2006. As part of the acquisition, the Company assumed the existing leases for the three restaurants, which had been in place prior to the acquisition. This transaction was completed and the leases were assumed approximately three years before the director joined the Company s board. Under the leases, the Company recognized rent and other related payments in the amounts of $378,000 and $342,000 for the sixteen weeks ended April 15, 2012 and April 17, 2011, respectively. Future minimum lease commitments under these leases are $4.4 million as of April 15, 2012.

11. Commitments and Contingencies

In the normal course of business, there are various legal claims in process, matters in litigation, and other contingencies. These include claims resulting from employment related claims and claims from guests or team members alleging illness, injury or other food quality, health, or operational concerns. To date, no claims of this nature, certain of which are covered by insurance policies, have had a material adverse effect on us. While it is not possible to predict the outcome of these suits, legal proceedings, and claims with certainty, management is of the opinion that adequate provision for potential losses associated with these matters has been made in the financial statements and that the ultimate resolution of these matters will not have a material adverse effect on our financial position and results of operations.