

Edgar Filing: CHECKERS DRIVE IN RESTAURANTS INC /DE - Form 10-Q

CHECKERS DRIVE IN RESTAURANTS INC /DE

Form 10-Q

April 24, 2002

SECURITIES AND EXCHANGE COMMISSION  
WASHINGTON, D.C. 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 March 25, 2002

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 number 0-19649

Checkers Drive-In Restaurants, Inc.  
(Exact name of Registrant as specified in its charter)

Delaware  
(State or other jurisdiction of  
incorporation or organization)

58-1654960  
(I.R.S. employer  
identification no.)

4300 West Cypress Street  
Suite 600  
Tampa, FL  
(Address of principal executive offices)

33607  
(Zip code)

Registrant's telephone number, including area code: (813) 283-7000

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

The Registrant had 11,176,310 shares of Common Stock, par value \$.001 per  
share, outstanding as of March 25, 2002.

TABLE OF CONTENTS

PART I	FINANCIAL INFORMATION
Item 1	Financial Statements

Consolidated Balance Sheets	
March 25, 2002 and December 31, 2001.....	

Edgar Filing: CHECKERS DRIVE IN RESTAURANTS INC /DE - Form 10-Q

Consolidated Statements of Income and Comprehensive Income  
 Quarters ended March 25, 2002 and March 26, 2001.....

Consolidated Statements of Cash Flows  
 Quarters ended March 25, 2002 and March 26, 2001 .....

Notes to Consolidated Financial Statements.....

Item 2 Management's Discussion and Analysis of Financial Condition  
 and Results of Operations.....

Item 3 Quantitative and Qualitative Disclosures About Market Risk.....

PART II OTHER INFORMATION

Item 1 Legal Proceedings.....

Item 2 Changes in Securities and Use of Proceeds.....

Item 3 Defaults Upon Senior Securities.....

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

Item 5 Other Information.....

Item 6 Exhibits and Reports on Form 8-K.....

ITEM 1. FINANCIAL STATEMENTS

CHECKERS DRIVE-IN RESTAURANTS, INC.  
 AND SUBSIDIARIES  
 CONSOLIDATED BALANCE SHEETS  
 (Dollars in thousands)  
 (UNAUDITED)

	March 200
	-----
Current Assets:	
Cash and cash equivalents	\$
Restricted cash	
Accounts, notes and leases receivable, net	
Inventory	
Prepaid expenses and other current assets	
Property and equipment held for sale	
	-----
Total current assets	
Property and equipment, net	
Notes receivable, net - less current portion	
Lease receivable, net - less current portion	
Intangible assets, net	
Other assets, net	

Edgar Filing: CHECKERS DRIVE IN RESTAURANTS INC /DE - Form 10-Q

	----- \$ =====
Current Liabilities:	
Current maturities of long-term debt and obligations under capital leases	\$
Accounts payable	
Reserves for restaurant relocations and abandoned sites	
Accrued wages and benefits	
Accrued liabilities	
	-----
Total current liabilities	
Long-term debt, less current maturities	
Obligations under capital leases, less current maturities	
Long-term reserves for restaurant relocations and abandoned sites	
Minority interests in joint ventures	
Deferred revenue	
Other long-term liabilities	
	-----
Total liabilities	
Stockholders' Equity:	
Preferred stock, \$.001 par value, authorized 2,000,000 shares, none issued at March 25, 2002 and December 31, 2001	
Common stock, \$.001 par value, authorized 175,000,000 shares, issued 11,176,310 at March 25, 2002 and 10,914,727 at December 31, 2001	
Additional paid-in capital	
Accumulated deficit	
	-----
Less: Treasury stock, 48,242 at March 25, 2002 and December 31, 2001, at cost	
Note receivable - officer	
	-----
Total stockholders' equity	
	----- \$ =====

See accompanying notes to consolidated financial statements.

3

CHECKERS DRIVE-IN RESTAURANTS, INC.  
AND SUBSIDIARIES  
CONSOLIDATED STATEMENTS OF INCOME  
AND COMPREHENSIVE INCOME  
(Dollars in thousands except per share amounts)  
(UNAUDITED)

	Quarter Ended	
	March 25, 2002	March 26, 2001
	-----	
REVENUES:		
Restaurant sales	\$ 37,093	\$ 31,683

Edgar Filing: CHECKERS DRIVE IN RESTAURANTS INC /DE - Form 10-Q

Franchise royalty revenue	3,322	3,438
Franchise fees and other income	4	174
	-----	-----
Total revenues	\$ 40,419	\$ 35,295
	-----	-----
COSTS AND EXPENSES:		
Restaurant food and paper costs	11,247	10,219
Restaurant labor costs	11,787	10,423
Restaurant occupancy expenses	2,608	2,510
Restaurant depreciation and amortization	1,292	970
Other restaurant operating expenses	4,666	4,024
General and administrative expenses	3,012	2,831
Advertising	2,126	1,847
Bad debt expense	100	179
Non-cash compensation	23	23
Other depreciation and amortization	152	793
Restaurant closure expense	375	18
Gain on sale of assets	(77)	(364)
	-----	-----
Total costs & expenses	37,311	33,473
	-----	-----
Operating income	3,108	1,822
OTHER INCOME (EXPENSE):		
Interest income	397	449
Interest expense	(814)	(1,377)
	-----	-----
Income before minority interests and income tax expense	2,691	894
Minority interests in operations of joint ventures	(27)	(14)
	-----	-----
Income before income tax expense	2,664	880
Income tax expense	-	37
	-----	-----
Net income	\$ 2,664	\$ 843
	=====	=====
Comprehensive income	\$ 2,664	\$ 843
	=====	=====
Basic net earnings per share	\$ 0.24	\$ 0.09
	=====	=====
Diluted net earnings per share	\$ 0.21	\$ 0.07
	=====	=====
Weighted average number of common shares outstanding:		
Basic	10,960	9,744
Diluted	12,854	11,381

See accompanying notes to consolidated financial statements.

Cash flows from operating activities:

Net income  
Adjustments to reconcile net earnings to net cash  
provided by operating activities:  
Depreciation and amortization  
Amortization of deferred loan costs  
Provisions for bad debt  
Non-cash compensation  
Gain on sale of assets  
Minority interest in operations of joint ventures  
Change in assets and liabilities:  
Decrease in receivables  
Decrease (increase) in inventory  
Decrease in prepaid expenses and other current assets  
Decrease in other assets  
Decrease in accounts payable  
Decrease in accrued liabilities

Net cash provided by operating activities

Cash flows from investing activities:

Capital expenditures  
Acquisition of restaurants, net of cash acquired  
Proceeds from sale of property & equipment

Net cash used in investing activities

Cash flows from financing activities:

Principal payments on long-term debt and capital lease obligations  
(Increase) decrease in restricted cash  
Proceeds from exercise of stock options and warrants  
Proceeds from issuance of long-term debt  
Repayment of note receivable - officer  
Purchase of treasury stock  
Deferred loan costs incurred  
Distributions to minority interests

Net cash (used in) provided by financing activities

Net increase in cash

Cash at beginning of period

Cash at end of period

Supplemental disclosures of cash flow information

Interest paid

Issuance of capital lease obligation for equipment

Note receivable accepted for market sale

Issuance of treasury stock

See accompanying notes to consolidated financial statements.

CHECKERS DRIVE-IN RESTAURANTS, INC.  
AND SUBSIDIARIES  
NOTES TO CONSOLIDATED  
FINANCIAL STATEMENTS  
(UNAUDITED)

Note 1: Summary of Significant Accounting Policies

(a) Basis of Presentation - The accompanying unaudited consolidated financial statements include the accounts of Checkers Drive-In Restaurants, Inc., its wholly-owned subsidiaries, and its joint ventures, collectively referred to as "the Company". The consolidated financial statements have been prepared in accordance with generally accepted accounting principles for interim financial information and the instructions to Form 10-Q and Article 10 of Regulation S-X. Accordingly, they do not include all the information and notes required by generally accepted accounting principles for complete financial statements. In the opinion of management, all adjustments necessary to present fairly the information set forth therein have been included.

The accounts of our joint ventures have been included with those of the Company in these consolidated financial statements. Intercompany balances and transactions have been eliminated in consolidation and minority interests have been established for the outside partners' interests. The Company reports on a fiscal year which will end on the Monday closest to December 31st. Each quarter consists of three 4-week periods, with the exception of the fourth quarter which consists of four 4-week periods.

The operating results for the quarter ended March 25, 2002, are not necessarily an indication of the results that may be expected for the fiscal year ending December 30, 2002. Except as disclosed herein, there has been no material change in the information disclosed in the notes to the consolidated financial statements included in the Company's Annual Report on Form 10-K for the year ended December 31, 2001. Therefore, it is suggested that the accompanying consolidated financial statements be read in conjunction with the Company's December 31, 2001 consolidated financial statements.

(b) Purpose and Organization - Our principal business is the operation and franchising of Checkers(R) and Rally's Hamburgers(R) (Rally's) restaurants. At March 25, 2002, there were 386 Rally's restaurants operating in 17 different states and there were 409 Checkers restaurants operating in 21 different states, the District of Columbia, Puerto Rico and the West Bank in the Middle East. Of the 795 total restaurants, 255 are owned by us and 540 are owned by franchisees. Three of the Company-owned restaurants are owned by joint venture partnerships in which we have a 50%, 51% and 75% ownership interest.

Our restaurants offer high quality food, serving primarily the drive-thru and take-out segments of the quick-service restaurant industry. Checkers commenced operations in April 1986 and began offering franchises in January 1987. Rally's opened its first restaurant in January 1985 and began offering franchises in November 1986.

(c) Use of Estimates - The preparation of the financial statements in conformity with accounting principles generally accepted in the United States of America require 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 reported period. Actual results could differ from those estimates.

## Edgar Filing: CHECKERS DRIVE IN RESTAURANTS INC /DE - Form 10-Q

(d) Reclassifications - Certain amounts in the 2001 financial statements have been reclassified to conform to the 2002 presentation.

### Note 2: Liquidity and Capital Resources

The restaurant industry, in general, operates with a working capital deficit because most of our investments are in long-term restaurant operating assets. We do not normally require large amounts of working capital to maintain operations since sales are for cash, purchases are on open accounts and meat and produce inventories are limited to a three-to-five day supply to assure freshness. We do not have significant levels of accounts receivable or inventory, and receive credit from our trade suppliers. Funds available from cash sales not needed immediately to pay our trade suppliers are used for non-current capital expenditures.

We have positive working capital of \$1.5 million at March 25, 2002 as compared to a \$2.5 million deficit at December 31, 2001. The change to liquidity is primarily due to operating profits for the quarter of \$2.7 million and additional capital contributions of \$0.8 million from the exercise of options and warrants into 261,583 shares of common stock.

The Company is subject to certain restrictive financial and non-financial covenants under certain of its debt agreements, including EBITDA and a Fixed Charge Coverage ratio. We were in compliance with all of the covenants for the quarter ended March 25, 2002.

6

Although there can be no assurance, we believe that our existing cash at March 25, 2002, the cash provided from operations, and the available \$2.8 million line of credit will be sufficient to meet our working capital and capital expenditure requirements for the next 12 months.

### Note 3: Lease Receivables

As a result of the sale of Company-owned restaurants in 1999 and 2000, we have recorded capital lease receivables for those restaurants sold which are subject to capital lease and mortgage obligations. The amount of capital lease receivables as of March 25, 2002 was approximately \$6.7 million. As of March 31, 2002, we have deferred gains of \$4.8 million from these sales since we continue to be responsible for the payment of these obligations to the original lessors and mortgagors. The gains are being recognized over the life of the related capital leases. The deferred gains are included in the consolidated balance sheet under the captions accrued liabilities-current and deferred revenue for \$0.5 million and \$4.3 million, respectively.

We have subleased the property associated with the sale of Company-owned restaurants under operating leases. The revenue from these subleases is offset against rent expense, as we continue to be responsible for the rent payments to the original lessors.

### Note 4: Intangible Assets

We assess the impairment of long-lived, identifiable intangible assets and enterprise level goodwill whenever events or changes in circumstances indicate that the carrying value may not be recoverable. Factors we consider important which could trigger an impairment review include the following:

- . significant underperformance relative to expected historical or projected future operating results;

## Edgar Filing: CHECKERS DRIVE IN RESTAURANTS INC /DE - Form 10-Q

- . significant negative industry or economic trends;
- . significant decline in our stock price for a sustained period; and
- . our market capitalization relative to net book value.

We account for long-lived assets under Statement of Financial Accounting Standards No. 144, "Accounting for the Impairment or Disposal of Long-Lived Assets" (SFAS 144), which we adopted on January 1, 2002. SFAS 144 requires the write-down of certain intangibles and tangible property associated with under-performing sites. Impairments or recoveries are recorded to adjust the asset values to the amount recoverable under the discounted cash flow analysis, in accordance with SFAS No. 144. We did not recognize any impairments during the quarter ended March 25, 2002.

On January 1, 2002, we adopted Statement of Financial Accounting Standards No. 142, "Goodwill and Other Intangible Assets" (SFAS 142). As a result, we ceased to amortize approximately \$24 million of goodwill and \$17.5 million for the intangible value of our tradename. We recorded approximately \$549,000 of amortization on these amounts during the quarter ended March 26, 2001 and would have recorded approximately \$549,000 of amortization during the quarter ended March 25, 2002. In lieu of amortization, we performed an initial impairment review of our goodwill and tradename as of January 1, 2002. Based upon the review, no impairment charge was required and we do not believe circumstances have changed since the review date which would make it necessary to reassess their values as of the balance sheet date.

Intangible assets consist of the following:

	March 25, 2002 -----	Dec. 31, 2001 -----
Goodwill	\$ 24,252	\$ 24,252
Tradename	17,548	17,548
Amortizable intangible assets	3,304	3,389
	-----	-----
Intangible assets, net	\$ 45,104 =====	\$ 45,189 =====

	March 25, 2002			December 31, 2001	
	Gross Amount	Accum Amort	Net	Gross Amount	Accum Amort
Reacquired franchise rights	\$ 1,359	\$ (396)	\$ 963	\$ 1,359	\$ (358)
Other intangibles	4,191	(1,850)	2,341	4,191	(1,803)
	-----	-----	-----	-----	-----
Amortizable intangible assets	\$ 5,550 =====	\$ (2,246) =====	\$ 3,304 =====	\$ 5,550 =====	\$ (2,161) =====

7

### Note 5: Revolving Line of Credit

The Company has a revolving loan facility with Textron Financial Corporation that permits the Company to borrow up to 50% of collateral pledged. The credit facility is available through June 15, 2002 with an interest rate



## Edgar Filing: CHECKERS DRIVE IN RESTAURANTS INC /DE - Form 10-Q

equal to LIBOR plus 4.5% (6.37% at March 25, 2002). Total collateral pledged as of March 25, 2002 was approximately \$5.7 million, consisting primarily of property and equipment. There were no borrowings under the loan facility as of March 25, 2002.

Note 6: Long-term debt and Obligations under Capital Leases

Long-term debt and obligations under capital leases consist of the following:

Note payable (Loan A) to Textron Financial Corporation payable in 120 monthly installments, maturing July 1, 2010, including interest at LIBOR plus 3.7% (5.57% at March 25, 2002) secured by property and equipment.

Mortgages payable to FFCA Acquisition Corporation secured by thirty- three Company-owned restaurants, payable in 240 aggregate monthly installments of \$133,295, maturing January 1, 2019, including interest at 9.5%.

Note payable to Heller Financial secured by the equipment at Company-owned restaurants, payable in 30 monthly installments of \$153,712, maturing December 1, 2003, including interest at 14%. The balance was completely repaid on April 15, 2002.

Obligations under capital leases, maturing at various dates through December 1, 2019, secured by property and equipment, bearing interest ranging from 7.3% to 10%. The leases are payable in monthly principal and interest installments averaging \$86,000.

Obligations under capital leases, maturing at various dates through January 1, 2016, secured by property and equipment, bearing interest ranging from 10.3% to 16.3%. The leases are payable in monthly principal and interest installments averaging \$182,000.

Notes payable to former Rally's franchise owners for acquisition of markets, secured by the related assets acquired, with maturities through May 1, 2004, bearing interest at 7.5% and 7.75%. The notes are payable in monthly principal and interest installments of \$8,416 and \$15,420.

Other notes payable, maturing at various dates through September 17, 2004, secured by property and equipment, bearing interest ranging from 0% to 7.70%. The notes are payable in monthly principal and interest installments ranging from \$452 to \$18,095.

Total long-term debt and obligations under capital leases

Less current installments

Long-term debt, less current maturities

Although we continue to be obligated, approximately \$6.7 million of the mortgage and capital lease obligations noted above pass directly through to franchisees as a result of Company-owned restaurant sales (See Note 3).

## Edgar Filing: CHECKERS DRIVE IN RESTAURANTS INC /DE - Form 10-Q

### Note 7: Treasury Stock

On February 19, 2002, the Company issued 17,350 shares of common stock previously held as treasury stock to Mr. Dorsch, as compensation, in accordance with his employment agreement. In addition, the Company repurchased an additional 17,350 shares of common stock to be held as treasury stock on March 20, 2002 for \$208,755.

8

### Note 8: Acquisitions

On January 26, 2002, we reacquired the Checkers' restaurants in Philadelphia which were previously sold to a franchisee in February 2001. As a result of the acquisition, deferred revenues of \$2.1 million were removed from the balance sheet along with the associated note receivable as of December 31, 2001, which was to be collected in installments through 2005. As a result of the gain deferral in 2001 at the time of the sale, no gain or loss was recognized from this transaction.

On March 24, 2002, we reacquired eight Rally's restaurants located in Detroit from RJR Receiver, LLC. We paid a total of approximately \$131,000 for the restaurants.

### Note 9: Accounting Charges and Loss Provisions

At the end of fiscal 2001, we had reserves of \$4.4 million relating to restaurant relocations and abandoned sites. These reserves represent management's estimate of future lease obligations and are reviewed and adjusted periodically, as more information becomes available related to our ability to sublease or assign the lease and other negotiations with the landlord. During the quarter ended March 25, 2002, the Company made lease and other payments of \$434,000, relating to restaurant relocations and abandoned sites. Additional reserves of \$375,000 were recognized during the quarter ended March 25, 2002.

### Note 10: Income Taxes

We account for income taxes under Statement of Financial Accounting Standards No. 109, "Accounting for Income Taxes" (SFAS 109). Under the asset or liability method of SFAS 109, deferred tax assets and liabilities are recognized for the future tax consequences attributable to differences between the financial statement carrying amounts of existing assets and liabilities and their respective tax bases. Deferred tax assets and liabilities are measured using enacted tax rates expected to apply to taxable income in the years in which those temporary differences are expected to be recovered or settled. Under SFAS 109, the effect on deferred tax assets and liabilities of a change in tax rates is recognized in income in the period that includes the enactment date.

As a result of the Merger in 1999, both companies experienced an ownership change as defined by Internal Revenue Code Section 382. Pursuant to IRC Section 382, the surviving entity or post-merger Checkers is significantly limited in utilizing the net operating loss carryforwards that were generated before the Merger to offset taxable income arising after the ownership change. As of August 9, 1999 Rally's and Checkers had net operating loss carryforwards of approximately \$49.8 million and \$60.9 million, respectively for a combined total of \$110.7 million. We believe that the limitations imposed by IRC Section 382 could restrict the prospective utilization of the total pre-merger net operating loss carryforward to approximately \$31.3 million over the carryforwards life of the net operating losses. The remaining pre-merger net operating loss

## Edgar Filing: CHECKERS DRIVE IN RESTAURANTS INC /DE - Form 10-Q

carryforward of \$79.4 million could expire before becoming available under these limitations. The \$31.3 million net operating loss carryforwards are subject to limitation in any given year and will expire in 2018. The Company has approximately \$5 million of post-merger net operating loss carryforward available through 2020, and approximately \$1.8 million of alternative minimum tax credit carryforwards available indefinitely.

A valuation allowance has been provided for 100 percent of the deferred tax assets since management cannot determine that it is more likely than not that the deferred tax assets will be realized. Management will continue to review the likelihood of the future realization of the deferred tax assets, and the benefit related to the deductible temporary differences will be recognized as a reduction of income tax expense when realization is more likely than not to occur.

### Note 11: Subsequent Events

a) Acquired Restaurant - On March 26, 2002, we bought the minority interest in our 50% owned joint venture located in Marietta, Georgia for \$40,000 cash and assumed all liabilities.

b) Commitments - On March 29, 2002, we signed a lease agreement for the purchase and installation of \$552,000 of point-of-sale systems in 45 Company-owned restaurants.

c) Equity Proceeds - Subsequent to March 25, 2002, additional options and warrants were exercised into 826,851 shares of common stock for which the Company received net proceeds of \$1.05 million.

d) Stock-based Compensation - On April 8, 2002, the Board of Directors granted 652,250 stock options to certain employees of the Company in accordance with the 2001 stock option plan.

9

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

### Introduction

Checkers Drive-In Restaurants, Inc. ("Checkers"), a Delaware corporation, and its wholly-owned subsidiaries (collectively, the "Company") is in the business of operating and franchising Checkers Restaurants and Rally's restaurants. We are the single largest chain of double drive-thru restaurants in the United States. Our Company is a combination of two similar quick-service restaurant chains, Checkers and Rally's Hamburgers (Rally's), which were merged in August 1999. Both companies were founded on a simple premise - serve the highest quality food, made fresh-to-order, served quickly and at a fair price.

The Company has developed and owns a comprehensive system for developing and operating double drive-thru restaurants, which includes trademarks, building designs and layouts, equipment, ingredients, recipes and specifications for authorized food products, methods of inventory control and certain operational and business standards.

At March 25, 2002, there were 795 restaurant locations, consisting of 255 Company-owned restaurants and 540 franchisee-owned restaurants. Of the 795 locations, 386 are Rally's restaurants operating in 17 different states and 409 are Checkers restaurants operating in 21 different states, the District of Columbia, Puerto Rico and the West Bank in the Middle East. Three of the owned restaurants are owned by joint venture partnerships in which we have a 50%, 51%

## Edgar Filing: CHECKERS DRIVE IN RESTAURANTS INC /DE - Form 10-Q

and 75% ownership interest. Checkers was founded in 1986 and Rally's was founded in 1985.

We receive revenues from restaurant sales, franchise fees and royalties. Restaurant food and paper costs, labor costs, occupancy expense, other operating expenses, depreciation and amortization, and advertising and promotion expenses relate directly to Company-owned restaurants. Other expenses, such as depreciation and amortization, and general and administrative expenses, relate to Company-owned restaurant operations and the Company's franchise sales and support functions. Our revenues and expenses are affected by the number and timing of additional restaurant openings, closings, market sales and the sales volumes of both existing and new restaurants.

### Special Note Regarding Forward-Looking Statements

Certain statements in this Form 10-Q under "Part I, Item 2. Management's Discussion and Analysis of Financial Condition and Results of Operations," "Part II, Item 1. Legal Proceedings" and elsewhere in this Form 10-Q constitute "forward-looking statements" which we believe are within the meaning of the Securities Act of 1933, as amended and the Securities Exchange Act of 1934, as amended. Also, when we use words such as "believes", "expects", "anticipates" or similar expressions, we are making forward looking statements. Such forward-looking statements involve known and unknown risks, uncertainties, and other factors which may cause the actual results, performance, or achievements of the Company to be materially different from any future results, performance, or achievements expressed or implied by such forward-looking statements. Some of the risks that should be considered include:

(i) The fact that we compete with numerous well established competitors who have substantially greater financial resources and longer operating histories than us, which enables them to engage in heavy and sustained discounting as well as substantial advertising and promotion. While this competition is already intense, if it increases, it could have an even greater adverse impact on revenues and profitability of company and franchise restaurants.

(ii) The fact that we anticipate the need to continue the improvement in same restaurant sales if we are to achieve improved profitability. Sales increases will depend, among other things, on the success of our advertising and promotion efforts and the success of other operating and training initiatives, all of which are speculative.

We may also be negatively impacted by other factors common to the restaurant industry such as changes in consumer tastes away from red meat and fried foods; consumer acceptance of new products; consumer frequency; increases in the costs of food; paper, labor, health care, workers' compensation or energy; an inadequate number of available hourly paid employees; and/or decreases in the availability of affordable capital resources; development and operating costs. Other factors which may negatively impact the Company include, among others, adverse publicity; general economic and business conditions; availability, locations, and terms of sites for restaurant development; changes in business strategy or development plans; quality of management; availability, terms and deployment of capital; the results of financing efforts; business abilities and judgement of personnel; availability of qualified personnel; changes in, or failure to comply with, government regulations; continued NASDAQ listing; weather conditions; construction schedules, results of existing and future litigation and other factors referenced in this Form 10-Q.

Edgar Filing: CHECKERS DRIVE IN RESTAURANTS INC /DE - Form 10-Q

	June 19, 2000	Sept. 11, 2000	Jan. 1, 2001	March 26, 2001	June 18, 2001	Sept. 1 2001
<b>Company-operated:</b>						
Beginning of quarter	367	287	224	195	207	
Openings/transfers in	-	1	-	29	-	
Closings/transfers out	(80)	(64)	(29)	(17)	-	
End of quarter	287	224	195	207	207	
<b>Franchise:</b>						
Beginning of quarter	537	601	649	659	638	
Openings/transfers in	81	65	42	17	5	
Closings/transfers out	(17)	(17)	(32)	(38)	(3)	
End of quarter	601	649	659	638	640	
	888	873	854	845	847	

RESULTS OF OPERATIONS

The table below sets forth the percentage relationship to total revenues, unless otherwise indicated, of certain items included in the Company's consolidated statements of income and operating data for the periods indicated:

	Quarter Ended	
	March 25, 2002	March 26, 2001
<b>REVENUES:</b>		
Restaurant sales	91.8%	89.8%
Franchise royalty revenue	8.2%	9.7%
Franchise fees and other income	0.0%	0.5%
Total revenues	100.0%	100.0%
<b>COSTS AND EXPENSES:</b>		
Restaurant food and paper costs (1)	30.3%	32.3%
Restaurant labor costs (1)	31.8%	32.9%
Restaurant occupancy expenses (1)	7.0%	7.9%
Restaurant depreciation and amortization (1)	3.5%	3.1%
Other restaurant operating expenses (1)	12.6%	12.7%
General and administrative expenses	7.5%	8.0%
Advertising (1)	5.7%	5.8%
Bad debt expense	0.2%	0.5%
Non-cash compensation	0.0%	0.0%
Other depreciation and amortization	0.4%	2.2%
Restaurant closure expense	0.9%	0.0%
Gain on sale of assets	(0.2%)	(1.0%)

## Edgar Filing: CHECKERS DRIVE IN RESTAURANTS INC /DE - Form 10-Q

Total costs & expenses	92.3%	94.8%
	-----	-----
Operating income	7.7%	5.2%
OTHER INCOME (EXPENSE):		
Interest income	1.0%	1.2%
Interest expense	(2.0%)	(3.9%)
	-----	-----
Income before minority interests and income tax expense	6.7%	2.5%
Minority interests in operations of joint ventures	(0.1%)	(0.0%)
	-----	-----
Income before income tax expense	6.6%	2.5%
Income tax expense	0.0%	0.1%
	-----	-----
Net income	6.6%	2.4%
	=====	=====

(1) As a percentage of restaurant sales

11

### Comparison of Historical Results - Quarter Ended March 25, 2002 and Quarter Ended March 26, 2001

Revenues. Total revenues were \$40.4 million for the quarter ended March 25, 2002, compared to \$35.3 million for the quarter ended March 26, 2001. Company-owned restaurant sales increased by \$5.4 million for the quarter ended March 25, 2002 to \$37.1 million, as compared to \$31.7 million for the quarter ended March 26, 2001 due to the increased number of Company-owned stores. California, Arizona, Macon and Philadelphia accounted for \$5.5 million in additional sales for the first quarter of 2002.

Sales at comparable restaurants, which include only the units that were in operation during the entire quarters being compared increased 0.2% for the quarter ended March 25, 2002 as compared with the quarter ended March 26, 2001.

Royalty income decreased by \$116,000 as compared to the first quarter one year ago due to the decreased number of franchise locations. There was an average of 648 franchise locations during the first quarter of 2001 as compared to 563 during the first quarter of 2002.

Franchise fees decreased for the quarter ended March 25, 2002 as compared to the quarter ended March 26, 2001 due to the recognition of income from CKE Restaurants, Inc. of approximately \$150,000 in the first quarter of 2001 prior to repossessing the 21 stores on July 3, 2001.

Costs and expenses. Restaurant food and paper costs totaled \$11.2 million or 30.3% of restaurant sales for the quarter ended March 25, 2002, compared to \$10.2 million or 32.3% of restaurant sales for the quarter ended March 26, 2001. The decrease in food and paper costs as a percentage of restaurant sales is due to beef costs beginning to soften during the fourth quarter of 2001 and into the current quarter, while they were near their high point during the first quarter of 2001. In addition, gross margin for the current promotion was more favorable to the Company compared to the promotion that ran during the first quarter in the prior year.

Restaurant labor costs, which include restaurant employees' salaries, wages, benefits and related taxes, totaled \$11.8 million or 31.8% of restaurant

## Edgar Filing: CHECKERS DRIVE IN RESTAURANTS INC /DE - Form 10-Q

sales for the quarter ended March 25, 2002, compared to \$10.4 million or 32.9% of restaurant sales for the quarter ended March 26, 2001. The decrease in restaurant labor costs as compared to last year was due to operations planning put in place by management. During 2001, emphasis was put on staffing the stores so service time would decrease and customer satisfaction would increase. Focus was shifted to labor efficiencies toward the end of 2001.

Restaurant occupancy expenses, which include rent, property taxes, licenses and insurance, totaled \$2.6 million or 7.0% of restaurant sales for the quarter ended March 25, 2002 compared to \$2.5 million or 7.9% of restaurant sales for the quarter ended March 26, 2001. While restaurant occupancy expense remained relatively constant, it decreased 0.9% as a percentage of restaurant sales. The decrease is due to decreases in several of these expenses as compared to the prior year. In addition, six of the operating restaurants, which were reacquired subsequent to March 26, 2001, are located on land owned by the Company, resulting in additional sales without corresponding rent expense, thereby decreasing occupancy as a percentage of sales.

Restaurant depreciation and amortization totaled \$1.3 or 3.5% of restaurant sales for the quarter ended March 25, 2002, compared to \$1.0 million or 3.1% for the quarter ended March 26, 2001. The increase is the result of management's plan to continue to operate 45 Company-owned restaurants and their classification for accounting purposes. Restaurants that were originally forecasted to be sold as part of the 1999 restructuring plan were reclassified from Held for Sale to Held for Use at December 31, 2001. As a result, we began recognizing depreciation on these assets at the beginning of the quarter ended March 25, 2002.

Other restaurant operating expenses include all other restaurant level operating expenses, and specifically include utilities, maintenance and other costs. These expenses totaled \$4.7 million, or 12.6% of restaurant sales for the quarter ended March 25, 2002 compared to \$4.0 million, or 12.7% of restaurant sales for the quarter ended March 26, 2001. These costs, as a percentage of sales, have remained consistent for the two quarters. The increase in dollars spent is due to the increase in Company-owned restaurants.

General and administrative expenses were \$3.0 million, or 7.5% of total revenues for the quarter ended March 25, 2002 compared to \$2.8 million, or 8.0% of total revenues for the quarter ended March 26, 2001. These costs have decreased as a percentage of total revenues due to their relatively fixed nature and increased revenues.

Advertising expense was \$2.1 million, or 5.7% of restaurant sales for the quarter ended March 25, 2002 compared to \$1.8 million, or 5.8% of restaurant sales for the quarter ended March 26, 2001. The costs have remained relatively consistent between the two quarters.

Bad debt expense remained relatively consistent at \$0.1 million, or 0.2% of total revenues for the quarter ended March 25, 2002 compared to \$0.2 million, or 0.5% of total revenues for the quarter ended March 26, 2001.

12

Non-cash compensation resulted from certain options granted and modified in fiscal 2000. Non-cash compensation recognized for the quarter ended March 25, 2002 and the quarter ended March 26, 2001 was \$23,000 for those options granted with a vesting period through 2003.

Other depreciation and amortization decreased by \$641,000 to \$152,000. The decrease is due to the application of FAS 142 for intangible assets. The goodwill and tradename carried on the books of the company are no longer

## Edgar Filing: CHECKERS DRIVE IN RESTAURANTS INC /DE - Form 10-Q

amortized. Quarterly amortization for goodwill and the tradename amounted to approximately \$549,000 for the quarter ended March 26, 2001.

Interest expense. Interest expense decreased to \$814,000, or 2.0% of total  
-----  
revenues for the quarter ended March 25, 2002 from \$1.4 million, or 3.9% of total revenues for the quarter ended March 26, 2001. The decrease in interest expense is due primarily to the decrease in debt by approximately \$5 million since January 2, 2001. In addition, 30% interest rate debt was partially paid off and refinanced with 14% debt in June 2001.

Income tax expense. The Company recorded no income tax expense for the  
-----  
quarter ended March 25, 2002. Available federal and state net operating losses will reduce taxable income to zero based upon operations during the quarter ended March 25, 2002. The income tax expense recorded during the quarter ended March 26, 2001 was for estimated federal alternative minimum tax prior to the Jobs Creation and Workers' Assistance Act of 2002.

### Liquidity and Capital Resources

The restaurant industry in general, operates with a working capital deficit because most of our investments are in long-term restaurant operating assets. We do not normally require large amounts of working capital to maintain operations since sales are for cash, purchases are on open accounts and meat and produce inventories are limited to a three-to-five day supply to assure freshness. We do not have significant levels of accounts receivable or inventory, and receive credit from our trade suppliers. Funds available from cash sales not needed immediately to pay our trade suppliers are used for non-current capital expenditures.

We have positive working capital of \$1.5 million at March 25, 2002 as compared to a \$2.5 million deficit at December 31, 2001. The change to liquidity is primarily due to operating profits for the quarter of \$2.7 million, and additional capital contributions of \$0.8 million from the exercise of options and warrants into 261,583 shares of common stock.

The Company is subject to certain restrictive financial and non-financial covenants under certain of its debt agreements, including EBITDA and a Fixed Charge Coverage ratio. We were in compliance with all of the covenants for the quarter ended March 25, 2002.

Cash and cash equivalents have increased approximately \$4.5 million to \$11.6 million since the fiscal year ended December 31, 2001. Cash flow from operating activities was \$5.1 million compared to \$1.4 million during the same period last year. Current year cash flows are largely attributable to current profits, a decrease in outstanding accounts receivable and prepaid expenses, partially offset by a net decrease in the balances of accounts payable and accrued liabilities.

Cash flow used for investing activities was \$0.2 million related primarily to capital expenditures at existing restaurants and the acquisition of 23 restaurants from former franchisees. The capital expenditures related primarily to restaurant level renovation.

Cash used by financing activities was \$0.5 million. We received \$0.8 million from the issuance of common stock from the exercise of stock options and warrants during the quarter ended March 25, 2002. The Company paid \$1.0 million for monthly principal payments on long-term debt and also purchased treasury stock for \$0.2 million.



## Edgar Filing: CHECKERS DRIVE IN RESTAURANTS INC /DE - Form 10-Q

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

#### Interest rate and foreign exchange rate fluctuations

-----

Our exposure to financial market risks is the impact that interest rate changes and availability could have on our debt. Borrowings under our primary debt facilities bear interest ranging from 5.6% to 16.3%. An increase in short-term and long-term interest rates would result in a reduction of pre-tax earnings. Substantially all of our business is transacted in U.S. dollars. Accordingly, foreign exchange rate fluctuations have never had a significant impact on the Company and are not expected to in the foreseeable future.

#### Commodity Price Risk

-----

We purchase certain products which are affected by commodity prices and are, therefore, subject to price volatility caused by weather, market conditions and other factors which are not considered predictable or within the Company's control. Although many of the products purchased are subject to changes in commodity prices, certain purchasing contracts or pricing arrangements have been negotiated in advance to minimize price volatility. Typically, the Company uses these types of purchasing techniques to control costs as an alternative to directly managing financial instruments to hedge commodity prices. In many cases, the Company believes it will be able to address commodity cost increases, which are significant and appear to be long-term in nature by adjusting its menu pricing or changing our product delivery strategy. However, increases in commodity prices could result in lower restaurant-level operating margins.

### PART II. OTHER INFORMATION

#### ITEM 1. LEGAL PROCEEDINGS

Jonathan Mittman et al. v. Rally's Hamburgers, Inc., et al. In January and

-----

February 1994, two putative class action lawsuits were filed, purportedly on behalf of the stockholders of Rally's, in the United States District Court for the Western District of Kentucky, Louisville division, against Rally's, Burt Sugarman and Giant Group, Ltd. and certain of Rally's former officers and directors and its auditors. The cases were subsequently consolidated under the case name Jonathan Mittman et. al. vs. Rally's Hamburgers, Inc., et. al. The complaints allege that the defendants violated the Securities Exchange Act of 1934, among other claims, by issuing inaccurate public statements about Rally's in order to arbitrarily inflate the price of its common stock. The plaintiffs seek compensatory and other damages, and costs and expenses associated with the litigation. On April 15, 1994, Rally's filed a motion to dismiss and a motion to strike. On April 5, 1995, the Court struck certain provisions of the complaint but otherwise denied Rally's motion to dismiss. In addition, the Court denied plaintiffs' motion for class certification; the plaintiffs renewed this motion, and despite opposition by the defendants, the Court granted such motion for class certification on April 16, 1996, certifying a class from July 20, 1992 to September 29, 1993. Motions for Summary Judgment were filed by the parties in September 2000, and rulings by the Court are pending. The defendants deny all wrongdoing and intend to defend themselves vigorously in this matter. Management is unable to predict the outcome of this matter at the present time or whether or not certain available insurance coverages will apply; however, if the Company is found to be liable, such a result may have a material adverse impact on the Company's financial condition and results of operations.

Greenfelder et al. v. White, Jr., et al. On August 10, 1995, a state court

-----  
complaint was filed in the Circuit Court of the Sixth Judicial Circuit in and for Pinellas County, Florida, Civil Division, entitled Gail P. Greenfelder and Powers Burgers, Inc. v. James F. White, Jr., Checkers Drive-In Restaurants, Inc., Herbert G. Brown, James E. Mattei, Jared D. Brown, Robert G. Brown and George W. Cook. A companion complaint was also filed in the same Court on May 21, 1997, entitled Gail P. Greenfelder, Powers Burgers of Avon Park, Inc., and Power Burgers of Sebring, Inc. v. James F. White, Jr., Checkers Drive-In Restaurants, Inc., Herbert G. Brown, James E. Mattei, Jared D. Brown, Robert G. Brown and George W. Cook. The original complaint alleged, generally, that certain officers of Checkers intentionally inflicted severe emotional distress upon Ms. Greenfelder, who is the sole stockholder, president and director of Powers Burgers, Inc., a Checkers franchisee. The present versions of the amended complaints in the two actions assert a number of claims for relief, including claims for breach of contract, fraudulent inducement to contract, post-contract fraud and breaches of implied duties of "good faith and fair dealings" in connection with various franchise agreements and an area development agreement, battery, defamation, negligent retention of employees, and violation of Florida's Franchise Act. The parties reached a tentative settlement on January 11, 2001. The settlement has not yet been consummated, and we intend to defend vigorously unless formal settlement is completed with terms similar to those reached in the tentative settlement on January 11, 2001.

Checkers Drive-In Restaurants, Inc. v. Tampa Checkmate Food Services,  
-----  
Inc., et al. On August 10, 1995, a state court counterclaim and third party  
-----  
complaint was filed in the Circuit Court of the Thirteenth Judicial Circuit in and for Hillsborough County, Florida, Civil Division, entitled Tampa Checkmate Food Services, Inc., Checkmate Food Services, Inc. and Robert H. Gagne v. Checkers Drive-In Restaurants, Inc., Herbert G. Brown, James E. Mattei, James F. White, Jr., Jared D. Brown, Robert G. Brown and George W. Cook.

14

A Complaint was originally filed by the Company in July of 1995 against Mr. Gagne ("Gagne") and Tampa Checkmate Food Services, Inc. ("Tampa Checkmate"), a company controlled by Mr. Gagne, to collect on a promissory note in the original principal amount of \$1,007,295 (the "promissory note") and foreclose on a mortgage securing the promissory note issued by Tampa Checkmate, enforce the terms of a personal guaranty executed by Mr. Gagne, and obtain declaratory relief regarding the rights of the respective parties under Tampa Checkmate's franchise agreement with the Company. The counterclaim and third party complaint, as amended, generally alleged that Mr. Gagne, Tampa Checkmate and Checkmate Food Services, Inc. ("Checkmate") were induced into entering into various franchise agreements with personal guarantees to the Company based upon misrepresentations by the Company and the named individuals and alleged violations of Florida's Franchise Act, Florida's Deceptive and Unfair Trade Practices Act, and breaches of implied duties of "good faith and fair dealings" in connection with a settlement agreement and franchise agreement between various of the parties.

The action was tried before a jury in August of 1999. The Company's action against Tampa Checkmate to collect the promissory note was stayed by virtue of Tampa Checkmate's bankruptcy filing (see discussion below). The Court entered a directed verdict and an involuntary dismissal as to all claims alleged against Jared D. Brown, Robert G. Brown, and George W. Cook and also entered a directed verdict and an involuntary dismissal as to certain other claims asserted against the Company and the remaining individual Counterclaim Defendants, Herbert G. Brown ("H. Brown"), James E. Mattei ("Mattei"), James F. White, Jr. ("White"). The jury rendered a verdict in favor of the Company, H. Brown, Mattei, and White

## Edgar Filing: CHECKERS DRIVE IN RESTAURANTS INC /DE - Form 10-Q

as to all claims asserted by Checkmate and in favor of Mattei as to all claims asserted by Tampa Checkmate and Gagne. In response to certain jury interrogatories, however, the jury made the following determinations: (i) That Gagne was fraudulently induced to execute a certain Unconditional Guaranty and that the Company was therefore not entitled to enforce its terms; (ii) That Tampa Checkmate was fraudulently induced to execute a certain franchise agreement by the actions of the Company, H. Brown, and White, jointly and severally, and that Tampa Checkmate was damaged as a result thereof in the amount of \$151, 331; (iii) That the Company, H. Brown, and J. White, jointly and severally, violated (S) 817.416(2)(a)(1) of the Florida Franchise Act relating to the franchise agreement and that Tampa Checkmate was damaged as a result thereof in the amount of \$151, 331 and that Gagne was damaged as a result thereof in the amount of \$151,331; and (iv) That the Company, H. Brown, and J. White did not violate Florida's Deceptive and Unfair Trade Practices Act relating to the Ehrlich Road franchise agreement.

The foregoing jury determinations were adopted by the trial court and judgments were entered accordingly. The judgments were appealed to the Second District Court of Appeal and on November 14, 2001, the Appeals Court (i) affirmed the \$151,331 judgment, plus statutory interest from August of 1999, entered in favor of Tampa Checkmate and against the Company and White for fraudulent inducement, but reversed as to Brown and that portion of the judgment awarding Tampa Checkmate statutory interest prior to the jury's verdict in August of 1999; (ii) affirmed the \$151,331 judgment, plus statutory interest from August of 1999, entered in favor of Tampa Checkmate and against the Company and White for violation of (S) 817.416(2)(a)(1) of the Florida Franchise Act, but reversed as to Brown; and (iii) reversed, in toto, the judgment entered in favor of Gagne. Reciprocal motions for attorney fees remain pending in the state court.

On February 4, 2002, the state trial court granted a motion filed by Tampa Checkmate to enter summary judgment as to the Company's affirmative defenses of setoff and recoupment, the legal significance of which is unclear, and reciprocal motions for attorney fees remain pending in the state court. The Company has appealed the before-described summary judgment to the Second District Court of Appeal and that appeal remains pending. The two judgments, as modified by the Second District Court of Appeal, have been satisfied by making payment to Tampa Checkmate's Chapter 7 Bankruptcy Trustee, but the Company believes the liability to Tampa Checkmate under the two judgments, and any liability for the payment of attorney fees, is subject to the Company's right of setoff arising from Tampa Checkmate's liability to the Company under the promissory note described above.

On or about July 15, 1997, Tampa Checkmate filed a Chapter 11 petition in the United States Bankruptcy Court for the Middle District of Florida, Tampa Division entitled In re: Tampa Checkmate Food Services, Inc., and numbered as 97-11616-8G-1 on the docket of said Court. As noted above, the bankruptcy filing stayed the Company's claim against Tampa Checkmate to collect the promissory note. The Company filed a motion in the Bankruptcy Court to establish its right to set-off, or in the alternative, recoup, the full amount due the Company under the promissory note against the judgments. On March 17, 2001 and May 23, 2001, the Bankruptcy Court entered orders recognizing the Company's right to setoff the amount owed by Tampa Checkmate under the promissory note against the judgments and lifting the automatic stay to allow the Company to proceed "to effect the setoff and/or recoupment permitted by this Court to include proceeding in state court or other appropriate forum to determine the amounts owed, if any, by the Debtor (Tampa Checkmate) to Checkers."

The Company has filed a motion in the Bankruptcy Court to determine the amounts owed under the promissory note. Tampa Checkmate has opposed the motion by asserting that the February 4, 2002 order entered in the state court proceedings referenced above was dispositive of the Company's claim of setoff.

## Edgar Filing: CHECKERS DRIVE IN RESTAURANTS INC /DE - Form 10-Q

The Bankruptcy Court denied the Company's motion and directed that the amounts owed under the promissory note be determined in the state court proceedings.

15

Dorothy Hawkins v. Checkers Drive-In Restaurants, Inc. and KPMG Peat  
-----

Marwick. On March 4, 1999, a state court complaint was filed in the Circuit  
-----

Court in and for Pinellas County, Florida, Civil Division. The complaint alleges that Mrs. Hawkins was induced into purchasing a restaurant site and entering into a franchise agreement with Checkers based on misrepresentations and omissions made by Checkers. The complaint asserts claims for breach of contract, breach of the implied covenant of good faith and fair dealing, violation of Florida's Deceptive Trade Practices Act, fraudulent concealment, fraudulent inducement, and negligent representation. The Company denies the material allegations of the complaint and intends to defend this lawsuit vigorously.

We are also involved in various other claims and legal actions arising in the ordinary course of business. In the opinion of management, the ultimate disposition of these matters will not have a material adverse effect on our consolidated financial position, results of operations or liquidity.

### 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

#### (a) Exhibits:

None.

#### (b) Reports on 8-K:

The following reports on Form 8-K were filed during the quarter covered by this report:

None.

### SIGNATURE -----

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.

Checkers Drive-In Restaurants, Inc.

Edgar Filing: CHECKERS DRIVE IN RESTAURANTS INC /DE - Form 10-Q

-----  
(Registrant)

Date: April 24, 2002

By: /s/ David G. Koehler

-----  
Treasurer and Chief Financial Officer

16