

CHILDRENS PLACE RETAIL STORES INC

Form 10-Q

December 05, 2007

**UNITED STATES  
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 August 4, 2007

**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 0-23071









**THE CHILDREN S PLACE RETAIL STORES, INC.**

(Exact name of registrant as specified in its charter)



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**Delaware**

(State or other jurisdiction of  
Incorporation or organization)

**31-1241495**

(I.R.S. employer  
identification number)

**915 Secaucus Road**

**Secaucus, New Jersey**  
(Address of Principal Executive Offices)

**07094**

(Zip Code)

**(201) 558-2400**

(Registrant's Telephone Number, Including Area Code)

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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

Indicate by check mark whether the registrant is a large accelerated filer, an accelerated filer, or a non-accelerated filer. See definition of an accelerated filer and large accelerated filer in Rule 12b-2 of the Exchange Act. (Check one).

Large accelerated filer  Accelerated filer  Non-accelerated filer

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

Yes  No

The number of shares outstanding of the registrant's common stock with a par value of \$0.10 per share, as of October 6, 2007 was 29,083,916 shares.

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**THE CHILDREN S PLACE RETAIL STORES, INC. AND SUBSIDIARIES  
QUARTERLY REPORT ON FORM 10-Q  
FOR THE PERIOD ENDED AUGUST 4, 2007**

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**PART I. FINANCIAL INFORMATION**

**Item 1. Condensed Consolidated Financial Statements.**

## THE CHILDREN S PLACE RETAIL STORES, INC. AND SUBSIDIARIES

## CONDENSED CONSOLIDATED BALANCE SHEETS

(In thousands)

	August 4, 2007 (Unaudited)	February 3, 2007	July 29, 2006 (Unaudited)
<b>ASSETS:</b>			
Current assets:			
Cash and cash equivalents	\$ 84,569	\$ 116,991	\$ 97,419
Short term investments		75,175	12,665
Accounts receivable	36,200	35,173	34,853
Inventories	333,870	239,039	254,626
Prepaid expenses and other current assets	76,510	42,817	65,245
Deferred income taxes	15,116	16,410	7,400
Total current assets	546,265	525,605	472,208
Long-term assets:			
Property and equipment, net	402,108	341,739	282,998
Deferred income taxes	84,780	69,039	55,546
Other assets	3,119	3,103	5,258
Total assets	\$ 1,036,272	\$ 939,486	\$ 816,010
<b>LIABILITIES AND STOCKHOLDERS EQUITY</b>			
<b>LIABILITIES:</b>			
Current liabilities:			
Revolving loan	\$ 72,225	\$	\$
Accounts payable	124,751	82,970	101,580
Income taxes payable	6,670	20,116	11,711
Accrued expenses, interest and other current liabilities	121,033	138,770	108,768
Total current liabilities	324,679	241,856	222,059
Long-term liabilities:			
Deferred rent liabilities	126,315	123,585	115,072
Deferred royalty	43,395	45,941	36,398
Unrecognized tax benefits	21,809		
Other long-term liabilities	6,444	6,317	7,011
Total liabilities	522,642	417,699	380,540
<b>COMMITMENTS AND CONTINGENCIES</b>			
<b>STOCKHOLDERS EQUITY:</b>			
Common stock, \$0.10 par value; 100,000,000 shares authorized; 29,083,916 shares, 29,083,916 shares and 29,029,607 shares issued and outstanding at August 4, 2007, February 3, 2007 and July 29, 2006, respectively			
	2,909	2,909	2,903
Additional paid-in capital	193,724	188,566	185,082
Accumulated other comprehensive income	11,013	4,344	7,706
Retained earnings	305,984	325,968	239,779
Total stockholders equity	513,630	521,787	435,470
Total liabilities and stockholders equity	\$ 1,036,272	\$ 939,486	\$ 816,010

See accompanying notes to these condensed consolidated financial statements



## THE CHILDREN S PLACE RETAIL STORES, INC. AND SUBSIDIARIES

## CONDENSED CONSOLIDATED STATEMENTS OF OPERATIONS

(Unaudited)

(In thousands, except per share amounts)

	Thirteen Weeks Ended		Twenty-Six Weeks Ended	
	August 4, 2007	July 29, 2006	August 4, 2007	July 29, 2006(1)
Net sales	\$ 424,297	\$ 395,614	\$ 903,160	\$ 822,123
Cost of sales	293,994	258,300	581,911	517,846
Gross profit	130,303	137,314	321,249	304,277
Selling, general and administrative expenses	155,777	143,247	306,375	273,061
Asset impairment charges	635		635	
Depreciation and amortization	18,569	15,858	36,304	30,065
Operating (loss) income	(44,678)	(21,791)	(22,065)	1,151
Interest income, net	566	796	1,884	1,673
(Loss) income before income taxes	(44,112)	(20,995)	(20,181)	2,824
(Benefit from) provision for income taxes	(16,021)	(7,476)	(6,804)	1,623
Net (loss) income	\$ (28,091)	\$ (13,519)	\$ (13,377)	\$ 1,201
Basic net (loss) income per common share	\$ (0.97)	\$ (0.47)	\$ (0.46)	\$ 0.04
Basic weighted average common shares outstanding	29,084	28,899	29,084	28,571
Diluted net (loss) income per common share	\$ (0.97)	\$ (0.47)	\$ (0.46)	\$ 0.04
Diluted weighted average common shares and common share equivalents outstanding	29,084	28,899	29,084	29,729

(1) The Condensed Consolidated Statement of Operations for the twenty-six weeks ended July 29, 2006 includes information that was restated for the thirteen weeks ended April 29, 2006 in the Company's Annual Report on Form 10-K for the fiscal year ended February 3, 2007.

See accompanying notes to these condensed consolidated financial statements

## THE CHILDREN S PLACE RETAIL STORES, INC. AND SUBSIDIARIES

## CONDENSED CONSOLIDATED STATEMENTS OF CASH FLOWS

(Unaudited) (In thousands)

	Twenty-Six Weeks Ended	
	August 4, 2007	July 29, 2006(1)
<b>CASH FLOWS FROM OPERATING ACTIVITIES:</b>		
Net (loss) income	\$ (13,377)	\$ 1,201
Adjustments to reconcile net loss to net cash used in operating activities:		
Depreciation and amortization	36,304	30,065
Deferred financing fee amortization	160	175
Amortization of lease buyouts	117	81
Loss on disposals of property and equipment	115	711
Asset impairment charges	635	
Equity compensation expense	3,362	1,229
Stock-based compensation expense related to liability awards	(568)	
Deferred royalty, net	(863)	9,236
Deferred taxes	(9,598)	(7,389)
Deferred rent and lease incentives	(6,903)	(6,059)
Changes in operating assets and liabilities:		
Accounts receivable	(745)	(5,699)
Inventories	(91,527)	(40,691)
Prepaid income taxes	(33,643)	(25,601)
Prepaid expenses and other current assets	532	(580)
Other assets	(239)	(299)
Accounts payable	38,870	17,625
Accrued expenses, interest and other current liabilities	(7,696)	12,587
Income taxes payable	(6,875)	(40,998)
Deferred rent liabilities	8,332	15,129
Other liabilities	2,448	1,342
Total adjustments	(67,782)	(39,136)
Net cash used in operating activities	(81,159)	(37,935)
<b>CASH FLOWS FROM INVESTING ACTIVITIES:</b>		
Property and equipment purchases, lease acquisition and software costs	(100,988)	(62,398)
Purchase of investments	(1,040,025)	(725,576)
Sale of investments	1,115,200	712,911
Other investing activities		(24)
Net cash used in investing activities	(25,813)	(75,087)
<b>CASH FLOWS FROM FINANCING ACTIVITIES:</b>		
Exercise of stock options and employee stock purchases		25,971
Excess tax benefit for stock option exercises		10,924
Borrowings under revolving credit facility	200,275	109,103
Repayments under revolving credit facility	(128,050)	(109,103)
Net cash provided by financing activities	72,225	36,895
Effect of exchange rate changes on cash	2,325	223
Net decrease in cash and cash equivalents	(32,422)	(75,904)
Cash and cash equivalents, beginning of period	116,991	173,323
Cash and cash equivalents, end of period	\$ 84,569	\$ 97,419

See accompanying notes to these condensed consolidated financial statements



**THE CHILDREN'S PLACE RETAIL STORES, INC. AND SUBSIDIARIES**  
**CONDENSED CONSOLIDATED STATEMENTS OF CASH FLOWS (Continued)**  
**(Unaudited) (In thousands)**

	Twenty-Six Weeks Ended	
	August 4, 2007	July 29, 2006(1)
<b>OTHER CASH FLOW INFORMATION:</b>		
Cash paid during the period for interest	\$ 973	\$ 397
Cash paid during the period for income taxes	\$ 38,730	\$ 64,664
Accrued purchases of property and equipment, lease acquisition and software costs	\$ (8,724)	\$ 2,299
Land received for distribution center	\$ 1,800	\$

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(1) The Condensed Consolidated Statement of Cash Flows for the twenty-six weeks ended July 29, 2006 includes information that was restated for the thirteen weeks ended April 29, 2006 in the Company's Annual Report on Form 10-K for the fiscal year ended February 3, 2007.

See accompanying notes to these condensed consolidated financial statements



**THE CHILDREN S PLACE RETAIL STORES, INC. AND SUBSIDIARIES**

**NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS**

**(Unaudited)**

**1. BASIS OF PRESENTATION**

The accompanying unaudited condensed consolidated financial statements have been prepared in accordance with accounting principles generally accepted in the United States ( U.S. GAAP ) for interim financial information and the rules and regulations of the Securities and Exchange Commission (the SEC ). Accordingly, certain information and footnote disclosures normally included in the annual consolidated financial statements prepared in accordance with U.S. GAAP have been condensed or omitted.

In the opinion of management, the accompanying unaudited condensed consolidated financial statements contain all adjustments (consisting only of normal recurring accruals) necessary to present fairly The Children s Place Retail Stores, Inc. s (the Company ) consolidated financial position as of August 4, 2007 and July 29, 2006, the results of its consolidated operations for the thirteen and twenty-six weeks ended August 4, 2007 and July 29, 2006, respectively and its consolidated cash flows for the twenty-six weeks ended August 4, 2007 and July 29, 2006. Due to the seasonal nature of the Company s business, the results of operations for the thirteen and twenty-six weeks ended August 4, 2007 and July 29, 2006 are not necessarily indicative of operating results for a full fiscal year. The condensed consolidated balance sheet as of February 3, 2007 has been taken from the audited consolidated financial statements as of that date. These condensed consolidated financial statements should be read in conjunction with the consolidated financial statements for the fiscal year ended February 3, 2007 included in the Company s Annual Report on Form 10-K for the year ended February 3, 2007 filed with the SEC. The consolidated statement of operations for the twenty-six weeks ended July 29, 2006 contains information for the thirteen weeks ended April 29, 2006 that was restated in the Company s Form 10-K for the year ended February 3, 2007.

**2. STOCK-BASED COMPENSATION**

The Company maintains several equity compensation plans and has granted stock options under its 1996 Stock Option Plan (the 1996 Plan ), its 1997 Stock Option Plan (the 1997 Plan ) and its 2005 Equity Incentive Plan (the 2005 Equity Plan ). The 2005 Equity Plan enabled the Compensation Committee (the Compensation Committee ) of the Company s Board of Directors (the Board ) to grant multiple forms of equity compensation such as stock options, stock appreciation rights, restricted stock awards, deferred stock awards and performance awards. In connection with the adoption of the 2005 Equity Plan, the Compensation Committee agreed not to issue any additional stock options under the 1996 Plan or the 1997 Plan and to limit the aggregate grant of awards under the 2005 Plan during fiscal years 2005, 2006 and 2007 to less than 2.5% of the aggregate number of shares of the Company s common stock outstanding on the last day of the 2005, 2006, and 2007 fiscal years, respectively. The Company also has an Employee Stock Purchase Plan (the ESPP ), in which participants purchase stock at 95% of fair market value, which is deemed to be non-compensatory.

The Company accounts for its equity compensation utilizing the guidance provided in Statement of Financial Accounting Standards ( SFAS ) No. 123 (Revised 2004) ( SFAS 123(R) ), Accounting for Share-Based Payments. The Company uses the Black-Scholes option model, which requires extensive use of accounting judgment and financial estimates, including estimates of how long an associate will hold vested stock options before exercise, the estimated volatility of the Company s common stock over the expected term, and the number of options that will be forfeited prior to the completion of vesting requirements. Application of other assumptions could result in significantly different estimates of fair value of stock-based compensation and consequently, the related expense recognized in the Company s financial statements. The Company has

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applied the provisions of SFAS 123(R) to stock option grants made on or after January 29, 2006 and stock options outstanding, but not yet vested, as of January 29, 2006. Prior to the adoption of SFAS 123(R), the Company accounted for its equity compensation expense under the provisions of Accounting Principles Board Opinion No. 25, Accounting for Stock Issued to Employees.

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The following tables summarize the Company's equity compensation expense for the thirteen and twenty-six weeks ended August 4, 2007 and July 29, 2006 (in thousands):

	Thirteen Weeks Ended August 4, 2007		
	Cost of Goods Sold	Selling, General & Administrative	Total
Stock option expense	\$	\$ 303	\$ 303
Performance award expense (1)			
Stock compensation expense related to the issuance of liability awards (2)		8	8
Expense related to modification of previously issued stock options (i.e., tolling) (3)	8	1,890	1,898
Tolled stock options accounted for as liability awards and related fair market value adjustment (3)	(390)	(171)	(561)
Total stock based compensation expense	\$ (382)	\$ 2,030	\$ 1,648

	Twenty-Six Weeks Ended August 4, 2007		
	Cost of Goods Sold	Selling, General & Administrative	Total
Stock option expense	\$	\$ 612	\$ 612
Performance award expense (1)			
Stock compensation expense related to the issuance of liability awards (2)		147	147
Expense related to modification of previously issued stock options (i.e., tolling) (3)	684	2,066	2,750
Tolled stock options accounted for as liability awards and related fair market value adjustment (3)	(508)	(207)	(715)
Total stock based compensation expense	\$ 176	\$ 2,618	\$ 2,794

	Thirteen Weeks Ended July 29, 2006		
	Cost of Goods Sold	Selling, General & Administrative	Total
Stock option expense	\$	\$ 437	\$ 437
Performance award expense (1)	(875)	(1,395)	(2,270)
Total stock based compensation expense	\$ (875)	\$ (958)	\$ (1,833)

	Twenty-Six Weeks Ended July 29, 2006(4)		
	Cost of Goods Sold	Selling, General & Administrative	Total
Stock option expense	\$	\$ 1,229	\$ 1,229
Performance award expense (1)			
Total stock based compensation expense	\$	\$ 1,229	\$ 1,229

(1) The Company determined that it is not probable that the Minimum Performance Target will be met. Accordingly, the Company has not recognized compensation expense related to Performance Awards (as defined below).

(2) Compensation expense for awards of restricted stock and stock options promised for which the Company has not completed the granting process due to the suspension of equity award grants. When the Company lifts the suspension of equity award grants, these awards will be reclassified as equity awards.

(3) Terminated employees have 90 days from date of termination to exercise their vested options. Due to the suspension of stock option exercises, the Company modified options held by terminated employees to extend their expiration dates until after the date the suspension is lifted (i.e., tolled stock options). After the suspension is lifted, terminated employees will have the same number of days to exercise their options as if the suspension had not occurred. Options that were tolled after the Company suspended option activity on September 14, 2006 were accounted for as liability awards because the option holders were no longer employees at the time of the modification and because of the Company's inability to provide shares upon exercise. When the Company lifts the suspension of stock option exercises, these awards will be reclassified as equity awards. Options that were tolled after September 14, 2006 were accounted for as equity awards because their options were tolled in conjunction with their termination.

(4) The Condensed Consolidated Statement of Operations for the twenty-six weeks ended July 29, 2006 includes information that was restated for the thirteen weeks ended April 29, 2006 in the Company's Annual Report on Form 10-K for the fiscal year ended February 3, 2007.

The Company recognized a tax benefit of approximately \$0.7 million and \$1.1 million for the thirteen and twenty-six weeks ended August 4, 2007, respectively. The Company recognized tax expense of approximately \$0.7 million related to equity compensation for the thirteen weeks ended July 29, 2006 due to the reversal of the accrual for Performance Awards (as defined below). The Company recognized a tax benefit of approximately \$0.5 million related to equity compensation expense for the twenty-six weeks ended July 29, 2006.

### Stock Option Plans

The fair value of issued stock options has been estimated on the date of grant using the Black-Scholes option pricing model, incorporating the following assumptions(1):

	July 29, 2006
Dividend yield	0%
Volatility factor(2)	41.4%
Weighted average risk-free interest rate(3)	4.35%
Expected life of options(4)	4.8years
Weighted average fair value on grant date	\$ 19.37 per share



- (1) Due to the Company's suspension of equity awards, no options were granted in the thirteen weeks ended August 4, 2007.
- (2) Expected volatility is based on a 50:50 blend of the historical and implied volatility with a two-year look back on the date of each grant.
- (3) The risk-free interest rate is based on the risk-free rate corresponding to the grant date and expected term.
- (4) The expected life used in the Black-Scholes calculation is based on a Monte Carlo simulation incorporating a forward-looking stock price model and a historical model of employee exercise and post-vest forfeiture behavior.

Changes in the Company's stock options for the twenty-six weeks ended August 4, 2007 were as follows:

	Number of Options (in thousands)	Weighted Average Exercise Price	Weighted Average Remaining Contractual Life (in years)	Aggregate Intrinsic Value (in thousands)
Options outstanding, beginning of fiscal year	2,322	\$ 30.36		
Granted (1)				