

BUILD A BEAR WORKSHOP INC
Form 10-Q
August 10, 2017

UNITED STATES

SECURITIES AND EXCHANGE COMMISSION

WASHINGTON, DC 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 July 1, 2017

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: 001-32320

BUILD-A-BEAR WORKSHOP, INC.

(Exact Name of Registrant as Specified in Its Charter)

Delaware

43-1883836

(State or Other Jurisdiction of (IRS Employer

Incorporation or Organization) Identification No.)

1954 Innerbelt Business Center Drive

63114

St. Louis, Missouri

(Address of Principal Executive Offices) (Zip Code)

(314) 423-8000

(Registrant's Telephone Number, Including Area Code)

Indicate by check mark whether the registrant: (1) has filed all reports required to be filed by Section 13 or 15(d) of the Securities Exchange Act of 1934 during the preceding 12 months (or for such shorter period that the registrant was required to file such reports), and (2) has been subject to such filing requirements for the past 90 days. Yes No

Indicate by check mark whether the registrant has submitted electronically and posted on its corporate Web site, if any, every Interactive Data File required to be submitted and posted pursuant to Rule 405 of Regulation S-T (§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 No

Indicate by check mark whether the registrant is a large accelerated filer, an accelerated filer, a non-accelerated filer, smaller reporting company, or an emerging growth company. See the definitions of "large accelerated filer," "accelerated filer," "smaller reporting company," and "emerging growth company" in Rule 12b-2 of the Exchange Act.

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

If an emerging growth company, indicate by check mark if the registrant has elected not to use the extended transition period for complying with any new or revised financial accounting standards provided pursuant to Section 13(a) of the Exchange Act.

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

As of August 4, 2017, there were 16,033,667 issued and outstanding shares of the registrant's common stock.

1

BUILD-A-BEAR WORKSHOP, INC.

INDEX TO FORM 10-Q

	<u>Page</u>
Part I Financial Information	
Item 1. Financial Statements (Unaudited)	3
Consolidated Balance Sheets	3
Consolidated Statements of Operations and Comprehensive (Loss) Income	4
Consolidated Statements of Cash Flows	5
Notes to Consolidated Financial Statements	6
Item 2. Management's Discussion and Analysis of Financial Condition and Results of Operations	12
Item 3. Quantitative and Qualitative Disclosures About Market Risk	19
Item 4. Controls and Procedures	19
Part II Other Information	
Item 1A. Risk Factors	20
Item 2. Unregistered Sales of Equity Securities and Use of Proceeds	20
Item 6. Exhibits	21
Signatures	22

PART I-FINANCIAL INFORMATION**Item 1. Financial Statements****BUILD-A-BEAR WORKSHOP, INC. AND SUBSIDIARIES****CONDENSED CONSOLIDATED BALANCE SHEETS**

(Dollars in thousands, except share and per share data)

	July 1, 2017 (Unaudited)	December 31, 2016	July 2, 2016 (Unaudited)
ASSETS			
Current assets:			
Cash and cash equivalents	\$ 12,568	\$ 32,483	\$ 10,156
Inventories	58,403	51,885	55,463
Receivables	9,033	12,939	9,380
Prepaid expenses and other current assets	12,823	12,737	13,817
Total current assets	92,827	110,044	88,816
Property and equipment, net of accumulated depreciation of \$170,785; \$172,333 and \$183,829, respectively	75,667	74,924	69,872
Deferred tax assets	10,256	8,256	10,944
Other intangible assets, net	1,361	1,721	1,859
Other assets, net	2,493	4,650	4,869
Total Assets	\$ 182,604	\$ 199,595	\$ 176,360
LIABILITIES AND STOCKHOLDERS' EQUITY			
Current liabilities:			
Accounts payable	\$ 17,016	\$ 27,861	\$ 22,404
Accrued expenses	11,285	15,897	10,427
Gift cards and customer deposits	29,559	37,070	28,864
Deferred revenue	1,803	2,029	2,250
Other current liabilities	82	-	-
Total current liabilities	59,745	82,857	63,945
Deferred rent	17,432	15,438	14,412
Deferred franchise revenue	540	565	636
Other liabilities	1,560	1,623	927

Stockholders' equity:

Preferred stock, par value \$0.01, Shares authorized: 15,000,000; No shares issued or outstanding at July 1, 2017, December 31, 2016 and July 2, 2016	-	-	-
Common stock, par value \$0.01, Shares authorized: 50,000,000; Issued and outstanding: 16,034,437; 15,856,927 and 15,856,305 shares, respectively	160	159	159
Additional paid-in capital	69,689	68,001	66,455
Accumulated other comprehensive loss	(12,010)	(12,727)	(11,696)
Retained earnings	45,488	43,679	41,522
Total stockholders' equity	103,327	99,112	96,440
Total Liabilities and Stockholders' Equity	\$ 182,604	\$ 199,595	\$ 176,360

See accompanying notes to condensed consolidated financial statements.

BUILD-A-BEAR WORKSHOP, INC. AND SUBSIDIARIES**CONDENSED CONSOLIDATED STATEMENTS OF OPERATIONS AND COMPREHENSIVE (LOSS) INCOME****(Unaudited)**

(Dollars in thousands, except share and per share data)

	Thirteen weeks ended		Twenty-six weeks ended	
	July 1, 2017	July 2, 2016	July 1, 2017	July 2, 2016
Revenues:				
Net retail sales	\$74,422	\$73,928	\$163,007	\$167,984
Commercial revenue	2,126	798	3,733	1,279
Franchise fees	678	413	1,117	852
Total revenues	77,226	75,139	167,857	170,115
Costs and expenses:				
Cost of merchandise sold - retail	41,902	42,760	88,770	91,317
Cost of merchandise sold - commercial	1,231	429	2,122	678
Selling, general and administrative	35,843	37,050	73,492	76,731
Store reopening	873	1,154	1,512	2,398
Interest expense (income), net	(7)	(11)	(18)	(38)
Total costs and expenses	79,842	81,382	165,878	171,086
(Loss) income before income taxes	(2,616)	(6,243)	1,979	(971)
Income tax (benefit) expense	(1,083)	(1,942)	747	(188)
Net (loss) income	\$(1,533)	\$(4,301)	\$1,232	\$(783)
Foreign currency translation adjustment	495	(1,082)	717	(1,725)
Comprehensive (loss) income	\$(1,038)	\$(5,383)	\$1,949	\$(2,508)
(Loss) income per common share:				
Basic	\$(0.10)	\$(0.28)	\$0.08	\$(0.05)
Diluted	\$(0.10)	\$(0.28)	\$0.08	\$(0.05)
Shares used in computing common per share amounts:				
Basic	15,627,324	15,486,462	15,583,631	15,448,580
Diluted	15,627,324	15,486,462	15,773,051	15,448,580

See accompanying notes to condensed consolidated financial statements.

BUILD-A-BEAR WORKSHOP, INC. AND SUBSIDIARIES**CONDENSED CONSOLIDATED STATEMENTS OF CASH FLOWS****(Unaudited)**

(Dollars in thousands)

	Twenty-six weeks ended July 1, 2017	July 2, 2016
Cash flows from operating activities:		
Net income (loss)	\$ 1,232	\$ (783)
Adjustments to reconcile net income to net cash used in operating activities:		
Depreciation and amortization	7,883	7,619
Stock-based compensation	1,898	1,497
Deferred taxes	1,301	41
Provision for doubtful accounts	419	-
Impairment of store assets	82	94
Loss on disposal of property and equipment	41	132
Change in assets and liabilities:		
Inventories	(5,926)	(2,131)
Receivables	3,561	3,554
Prepaid expenses and other assets	74	(190)
Accounts payable and accrued expenses	(15,675)	(27,706)
Lease related liabilities	1,913	2,329
Gift cards and customer deposits	(7,645)	(6,256)
Deferred revenue	(261)	(437)
Net cash used in operating activities	(11,103)	(22,237)

Cash flows from investing activities:			
Purchases of property and equipment	(7,896)	(11,317
Purchases of other assets and other intangible assets	(131)	(565
Proceeds from sale or maturity of short term investments	-		1,461
Cash used in investing activities	(8,027)	(10,421
Cash flows from financing activities:			
Proceeds from the exercise of employee stock options, net of withholding tax payments	(454)	(495
Payments made under capital leases	(36)	-
Purchases of Company's common stock	-		(1,469
Cash used in financing activities	(490)	(1,964
Effect of exchange rates on cash	(295)	(418
Net decrease in cash and cash equivalents	(19,915)	(35,040
Cash and cash equivalents, beginning of period	32,483		45,196
Cash and cash equivalents, end of period	\$	12,568	\$
			10,156

See accompanying notes to condensed consolidated financial statements.

Notes to Condensed Consolidated Financial Statements

1. Basis of Presentation

The condensed consolidated financial statements included herein are unaudited and have been prepared by Build-A-Bear Workshop, Inc. and its subsidiaries (collectively, the Company) pursuant to the rules and regulations of the U.S. Securities and Exchange Commission (SEC). Certain information and footnote disclosures normally included in financial statements prepared in accordance with U.S. generally accepted accounting principles (GAAP) have been condensed or omitted pursuant to such rules and regulations. The condensed consolidated balance sheet of the Company as of December 31, 2016 was derived from the Company's audited consolidated balance sheet as of that date. All other condensed consolidated financial statements contained herein are unaudited and reflect all adjustments which are, in the opinion of management, necessary to summarize fairly the financial position of the Company and the results of the Company's operations and cash flows for the periods presented. All of these adjustments are of a normal recurring nature. All significant intercompany balances and transactions have been eliminated in consolidation. Because of the seasonal nature of the Company's operations, results of operations of any single reporting period should not be considered as indicative of results for a full year. These condensed consolidated financial statements should be read in conjunction with the Company's audited consolidated financial statements for the fiscal year ended December 31, 2016, which were included in the Company's annual report on Form 10-K filed with the SEC on March 16, 2017.

The Company adopted Accounting Standards Update (ASU) No. 2016-09, *Compensation – Stock Compensation: Improvements to Employee Share-Based Payment Accounting*, effective January 1, 2017. The Company made an accounting policy election to account for forfeitures as they occur. The impact of this election, along with the adoption of the other provisions of the standard in the first quarter of 2017, was to increase deferred tax assets by \$1.6 million, increase additional paid-in-capital by \$0.3 million, increase retained earnings by \$1.9 million and decrease taxes payable by \$0.6 million.

Additionally, the Company early adopted ASU No. 2016-16, *Income Taxes – Intra-Entity Transfers of Assets Other Than Inventory*, effective January 1, 2017. Using the modified retrospective method, the impact of the adoption of the standard in the first quarter of 2017 was to increase deferred tax assets by \$1.0 million, decrease other assets, net by \$2.3 million and decrease retained earnings by \$1.3 million.

2. Prepaid Expenses and Other Assets

Prepaid expenses and other current assets consist of the following (in thousands):

	July 1, 2017	December 31, 2016	July 2, 2016
Prepaid rent	\$7,529	\$ 7,191	\$6,920
Other	5,294	5,546	6,897
Total	\$12,823	\$ 12,737	\$13,817

3. Accrued Expenses

Accrued expenses consist of the following (in thousands):

	July 1, 2017	December 31, 2016	July 2, 2016
Accrued wages, bonuses and related expenses	\$5,491	\$ 5,596	\$4,787
Sales tax payable	1,816	5,075	1,284
Accrued rent and related expenses	3,950	4,615	4,062
Current income taxes payable	28	611	294
Total	\$11,285	\$ 15,897	\$10,427

4. Stock-based Compensation

On March 14, 2017, the Company's Board of Directors (the Board) adopted, subject to stockholder approval, the Build-A-Bear Workshop, Inc. 2017 Omnibus Incentive Plan (the Incentive Plan). On May 11, 2017, at the Company's 2017 Annual Meeting of Stockholders, the Company's stockholders approved the Incentive Plan. The Incentive Plan, which is administered by the Compensation and Development Committee of the Board, permits the grant of stock options (including both incentive and non-qualified stock options), stock appreciation rights, restricted stock, cash and other stock-based awards, some of which may be performance-based pursuant to the terms of the Incentive Plan. The Board may amend, modify or terminate the Incentive Plan at any time, except as provided in the Incentive Plan. The Incentive Plan will terminate on March 14, 2027, unless earlier terminated by the Board. The number of shares of the Company's common stock authorized for issuance under the Incentive Plan is 1,000,000, plus shares of stock subject to outstanding awards made under the Company's Third Amended and Restated 2004 Stock Incentive Plan that on or after March 21, 2017 may be forfeited, expire or be settled for cash.

For the thirteen and twenty-six weeks ended July 1, 2017, selling, general and administrative expense includes \$0.9 million and \$1.9 million, respectively, of stock-based compensation expense. For the thirteen and twenty-six weeks ended July 2, 2016, selling, general and administrative expense includes \$0.8 million and \$1.5 million, respectively, of stock-based compensation expense. As of July 1, 2017, there was \$5.4 million of total unrecognized compensation expense related to unvested restricted stock and option awards which is expected to be recognized over a weighted-average period of 1.6 years.

The following table is a summary of the balances and activity for stock options for the twenty-six weeks ended July 1, 2017:

	Options	
	Shares	Weighted Average Exercise Price
Outstanding, December 31, 2016	757,784	\$ 9.91
Granted	72,051	8.85
Exercised	1,269	6.36
Forfeited	26,795	13.45
Canceled or expired	8,320	11.27
Outstanding, July 1, 2017	793,451	\$ 9.69

The following table is a summary of the balances and activity for the plan related to time-based and performance-based restricted stock for the twenty-six weeks ended July 1, 2017:

	Restricted Stock		Performance Shares	
	Weighted		Weighted	
	Average		Average	
	Shares	Grant	Shares	Grant
		Date Fair		Date Fair
		Value		Value
Outstanding, December 31, 2016	316,116	\$ 13.30	241,141	\$ 15.39
Granted	252,121	9.19	83,897	8.85
Vested	174,032	12.16	6,472	20.54
Forfeited	24,331	12.96	15,247	14.28
Canceled or expired	—	—	13,704	13.68
Outstanding, July 1, 2017	369,874	\$ 11.05	289,615	\$ 13.66

The total fair value of shares vested during the twenty-six weeks ended July 1, 2017 and July 2, 2016 was \$2.2 million and \$1.6 million, respectively.

In March 2017, the Company awarded three-year performance-based restricted stock subject to the achievement of pre-established consolidated total pre-tax income goals for fiscal 2017, 2018 and 2019. These shares have a payout opportunity ranging from 25% to 200% of the target number of shares. In 2017, 13,704 performance shares issued in fiscal 2016 were canceled as the pre-established pre-tax income objectives for 2016 were not achieved.

The outstanding performance shares as of July 1, 2017 consist of the following:

	Performance
	Shares
Earned shares subject to time-based restrictions at actual	6,325
Unearned shares subject to performance-based restrictions at target:	
2015 - 2017 consolidated total revenues	50,000
2016 - 2018 consolidated total revenues	149,393
2017 - 2019 consolidated pre-tax income	83,897
Performance shares outstanding, July 1, 2017	289,615

5. Income Taxes

The effective tax rate was 41.4% and 37.7% for the thirteen and twenty-six weeks ended July 1, 2017, respectively, compared to 31.1% and 19.4% for the thirteen and twenty-six weeks ended July 2, 2016, respectively. The 2017 effective tax rate differed from the statutory rate of 34% primarily due to the implementation of the new accounting standard related to the accounting for the tax impact of equity awards vesting and other discrete items. The fluctuation in the 2016 effective tax rate was primarily due to the effect of permanent items and a discrete item.

6. Stockholders' Equity

The following table sets forth the changes in stockholders' equity for the twenty-six weeks ended July 1, 2017 and July 2, 2016:

Twenty-six weeks ended	
July	July
1,	2,
2017	2016

Beginning balance