REGIS CORP
Form 10-Q
November 03, 2006

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 September 30, 2006

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 0-11230

Regis Corporation
(Exact name of registrant as specified in its charter)

Minnesota	**41-0749934**
(State or other jurisdiction of incorporation or organization)	(I.R.S. Employer Identification No.)
7201 Metro Boulevard, Edina, Minnesota	**55439**
(Address of principal executive offices)	(Zip Code)

(952)947-7777
(Registrant s telephone number, including area code)

N/A
(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 is a large accelerated filer, an accelerated filer, or a non-accelerated filer. See definition of accelerated filer and large accelerated filer in Rule 12b-2 of the Exchange Act. (Check one):

Large accelerated filer x Accelerated filer o Non-accelerated filer o

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

Indicate the number of shares outstanding of each of the issuer s classes of common stock as of November 3, 2006:

Common Stock, $.05 par value	**45,058,062**
Class	Number of Shares

REGIS CORPORATION

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PART I - FINANCIAL INFORMATION

Item 1. Condensed Consolidated Financial Information

REGIS CORPORATION
CONDENSED CONSOLIDATED BALANCE SHEET (Unaudited)
as of September 30, 2006 and June 30, 2006
(Dollars in thousands, except per share amounts)

	September 30, 2006	June 30, 2006
ASSETS		
Current assets:		
Cash and cash equivalents	$ 146,860	$ 135,397
Receivables, net	73,652	62,558
Inventories	207,720	193,999
Deferred income taxes	15,938	16,224
Other current assets	44,038	33,588
Total current assets	488,208	441,766
Property and equipment, net	490,610	483,764
Goodwill	795,398	778,228
Other intangibles, net	216,858	216,831
Other assets	70,121	61,475
Total assets	$ 2,061,195	$ 1,982,064
LIABILITIES AND SHAREHOLDERS EQUITY		
Current liabilities:		
Long-term debt, current portion	$ 153,326	$ 101,912
Accounts payable	80,599	70,807
Accrued expenses	223,415	230,236
Total current liabilities	457,340	402,955
Long-term debt	537,770	520,357
Other noncurrent liabilities	188,527	187,345
Total liabilities	1,183,637	1,110,657
Commitments and contingencies		
Shareholders equity:		
Preferred stock, authorized 250,000 shares at September 30, 2006 and June 30, 2006		
Common stock, $.05 par value; issued and outstanding 44,858,121 and 45,303,459 common shares at September 30, 2006 and June 30, 2006, respectively	2,244	2,266
Additional paid-in capital	213,982	232,284
Accumulated other comprehensive income	61,288	58,066
Retained earnings	600,044	578,791
Total shareholders equity	877,558	871,407
Total liabilities and shareholders equity	$ 2,061,195	$ 1,982,064

The accompanying notes are an integral part of the unaudited Condensed Consolidated Financial Information.

REGIS CORPORATION
CONDENSED CONSOLIDATED STATEMENT OF OPERATIONS (Unaudited)
for the three months ended September 30, 2006 and 2005
(Dollars in thousands, except per share amounts)

	2006	2005
Revenues:		
Service	$ 434,552	$ 390,969
Product	184,925	173,752
Royalties and fees	19,766	19,508
	639,243	584,229
Operating expenses:		
Cost of service	245,525	221,859
Cost of product	94,229	88,536
Site operating expenses	55,806	49,716
General and administrative	77,953	74,067
Rent	92,172	82,835
Depreciation and amortization	29,542	25,896
Total operating expenses	595,227	542,909
Operating income	44,016	41,320
Other income (expense):		
Interest	(9,838)	(8,264)
Other, net	811	799
Income before income taxes	34,989	33,855
Income taxes	(11,896)	(11,696)
Net income	$ 23,093	$ 22,159
Net income per share:		
Basic	$ 0.51	$ 0.49
Diluted	$ 0.50	$ 0.48
Weighted average common and common equivalent shares outstanding:		
Basic	45,044	44,964
Diluted	46,132	46,336
Cash dividends declared per common share	$ 0.04	$ 0.04

The accompanying notes are an integral part of the unaudited Condensed Consolidated Financial Information.

REGIS CORPORATION
CONDENSED CONSOLIDATED STATEMENT OF CASH FLOWS (Unaudited)
for the three months ended September 30, 2006 and 2005
(Dollars in thousands)

	2006	2005
Cash flows from operating activities:		
Net income	$ 23,093	$ 22,159
Adjustments to reconcile net income to net cash provided by operating activities:		
Depreciation	25,068	21,768
Amortization	2,989	2,878
Deferred income taxes	5,039	83
Asset impairment	1,485	1,250
Excess tax benefits from stock-based compensation plans	(1,170)	(2,713)
Stock-based compensation	1,146	1,675
Other noncash items affecting earnings	187	(136)
Changes in operating assets and liabilities:		
Receivables	(10,906)	2,488
Inventories	(11,875)	(14,514)
Other current assets	(10,196)	(9,558)
Other assets	(1,404)	(400)
Accounts payable	10,562	8,459
Accrued expenses	(6,933)	958
Other noncurrent liabilities	4,485	3,606
Net cash provided by operating activities	31,570	38,003
Cash flows from investing activities:		
Capital expenditures	(23,929)	(29,654)
Proceeds from sale of assets	118	21
Purchase of salon, school and hair restoration center net assets, net of cash acquired	(22,767)	(35,963)
Loans and investments	(7,250)	
Net investment hedge settlement	(8,897)	
Net cash used in investing activities	(62,725)	(65,596)
Cash flows from financing activities:		
Borrowings on revolving credit facilities	1,211,806	656,729
Payments on revolving credit facilities	(1,149,000)	(617,930)
Proceeds from issuance of long-term debt	25,000	
Repayments of long-term debt	(25,458)	(12,051)
Excess tax benefits from stock-based compensation plans	1,170	2,713
Other, primarily increase in negative book cash balances	1,177	3,426
Repurchase of common stock	(25,057)	
Proceeds from issuance of common stock	3,857	5,274
Dividends paid	(1,840)	(1,805)
Net cash provided by financing activities	41,655	36,356
Effect of exchange rate changes on cash and cash equivalents	963	327
Increase in cash and cash equivalents	11,463	9,090
Cash and cash equivalents:		
Beginning of period	135,397	102,718
End of period	$ 146,860	$ 111,808

The accompanying notes are an integral part of the unaudited Condensed Consolidated Financial Information.

REGIS CORPORATION
NOTES TO CONDENSED CONSOLIDATED FINANCIAL INFORMATION
(Unaudited)

1. BASIS OF PRESENTATION OF UNAUDITED INTERIM CONDENSED CONSOLIDATED FINANCIAL INFORMATION AND SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES:

The unaudited interim Condensed Consolidated Financial Information of Regis Corporation (the Company) as of September 30, 2006 and for the three months ended September 30, 2006 and 2005, reflect, in the opinion of management, all adjustments necessary to fairly state the consolidated financial position of the Company as of September 30, 2006 and the consolidated results of its operations and its cash flows for the interim periods. Adjustments consist only of normal recurring items, except for any discussed in the notes below. The results of operations and cash flows for any interim period are not necessarily indicative of results of operations and cash flows for the full year.

The Consolidated Balance Sheet data for June 30, 2006 was derived from audited Consolidated Financial Statements, but does not include all disclosures required by accounting principles generally accepted in the United States of America (GAAP). The unaudited interim Condensed Consolidated Financial Information should be read in conjunction with the Company s Annual Report on Form 10-K for the year ended June 30, 2006 and other documents filed or furnished with the Securities and Exchange Commission (SEC) during the current fiscal year.

With respect to the unaudited condensed financial information of the Company for the three month periods ended September 30, 2006 and 2005 included in this Form 10-Q, PricewaterhouseCoopers LLP reported that they have applied limited procedures in accordance with professional standards for a review of such information. However, their separate report dated November 3, 2006 appearing herein, states that they did not audit and they do not express an opinion on that unaudited financial information. Accordingly, the degree of reliance on their report on such information should be restricted in light of the limited nature of the review procedures applied. PricewaterhouseCoopers LLP is not subject to the liability provisions of Section 11 of the Securities Act of 1933 for their report on the unaudited financial information because that report is not a report or a part of the registration statement prepared or certified by PricewaterhouseCoopers LLP within the meaning of Sections 7 and 11 of the Act.

Inventories:

Inventories consist principally of hair care products held either for use in services or for sale. Inventories are stated at the lower of cost or market with cost determined on a weighted average basis. Cost of product used in salon services is determined by applying estimated gross profit margins to service revenues, which are based on historical factors including product pricing trends and estimated shrinkage. In addition, the estimated gross profit margin is adjusted based on the results of physical inventory counts performed at least semi-annually. Cost of product sold to salon customers is determined based on the actual cost of product to the Company, adjusted for an estimated shrinkage factor. Product and service inventories are adjusted based on the results of physical inventory counts performed at least semi-annually.

Stock-Based Employee Compensation:

Stock-based awards are granted under the terms of the 2004 Long Term Incentive Plan (2004 Plan) and the 2000 Stock Option Plan. Additionally, the Company has outstanding stock options under its 1991 Stock Option Plan, although the Plan terminated in 2001. Under these plans, three types of stock-based compensation awards are granted: stock options, equity-based stock appreciation rights (SARS) and restricted stock. These stock-based awards expire within ten years from the grant date. The company recognizes compensation expense for these awards on a straight-line basis over the five-year vesting period (includes retirement eligible recipients as there is no accelerated vesting terms for these recipients).

A summary of option activity under the Plan as of September 30, 2006, and changes during the three month period then ended is presented below:

Options	Shares (in thousands)	Weighted-Average Exercise Price ($)
Outstanding at July 1, 2006	2,908	$ 20.59
Granted		
Exercised	(236)	16.25
Cancelled	(9)	38.02
Outstanding at September 30, 2006	2,663	$ 20.89
Exercisable at September 30, 2006	2,219	$ 18.26

There are an additional 420,493 shares expected to vest with a $34.03 weighted average exercise price and a weighted average remaining contractual life of 8.0 years. The total intrinsic value of options exercised during the three months ended September 30, 2006 and 2005, was $4.9 and $7.3 million, respectively.

As of September 30, 2006, 187,445 unvested restricted stock shares with a weighted average grant-date fair value of $36.91 were outstanding, of which 192,855 were outstanding at June 30, 2006.

As of September 30, 2006, 222,250 SARS with a weighted average grant-date fair value of $37.37 were outstanding, of which 231,250 were outstanding at June 30, 2006.

The company s primary employee stock-based compensation grant occurs during the fourth quarter. The total unrecognized compensation cost related to unvested stock-based compensation arrangements was $12.8 million and the related weighted average period over which it is expected to be recognized is approximately 3.4 years.

Recent Accounting Pronouncements:

On July 13, 2006, FASB Interpretation No. 48, *Accounting for Uncertainty in Income Taxes - An Interpretation of FASB Statement No. 109 (FIN 48)*, was issued. FIN 48 clarifies the accounting for uncertainty in income taxes recognized in an enterprise s financial statements in accordance with FASB Statement No. 109, *Accounting for Income Taxes*. FIN 48 also prescribes a recognition threshold and measurement attribute for the financial statement recognition and measurement of a tax position taken or expected to be taken in a tax return. The new FASB standard provides guidance on derecognition, classification, interest and penalties, accounting in interim periods, disclosure, and transition. The provisions of FIN 48 are effective for fiscal years beginning after December 15, 2006 (i.e., the beginning of the Company s fiscal year 2008), and the provisions are to be applied to all tax positions upon initial adoption of this standard. Only tax positions that meet the more-likely-than-not recognition threshold at the effective date may be recognized or continue to be recognized upon adoption of FIN 48. The cumulative effect of applying the provisions of FIN 48 must be reported as an adjustment to the opening balance of retained earnings for that fiscal year. The Company is currently evaluating the impact of FIN 48 on its Consolidated Financial Statements.

In September 2006, the FASB issued SFAS No. 157, *Fair Value Measures* (SFAS No. 157). SFAS No. 157 defines fair value, establishes a framework for measuring fair value and enhances disclosures about fair value measures required under other accounting pronouncements, but does not change existing guidance as to whether or not an instrument is carried at fair value. SFAS No. 157 is effective for fiscal years beginning after November 15, 2007 (i.e., the beginning of the Company s fiscal year 2009). The Company is currently evaluating the impact of SFAS No. 157 on its Consolidated Financial Statements.

In September 2006, the FASB issued SFAS No. 158, *Employers Accounting for Defined Benefit Pension and Other Postretirement Plans* (SFAS No. 158). SFAS No. 158 amends SFAS No. 87, *Employers Accounting for Pensions* (SFAS No. 87), SFAS No. 88, *Employers Accounting for Settlements and Curtailments of Defined Benefit Plans and for Termination Benefits* (SFAS No. 88), SFAS No. 106, *Employers Accounting for Postretirement Benefits Other Than Pensions* (SFAS No. 106) and SFAS No. 132(R), *Employers Disclosures about Pensions and Other Postretirement Benefits* (SFAS No. 132(R)). SFAS No. 158 requires balance sheet recognition of the funded status for all pension and postretirement benefit plans as of the end of the Company s current fiscal year (i.e., in the Company s fiscal year 2007 Annual Report on Form 10-K). The impact of initial adjustment will be recorded as an adjustment of the ending balance of other comprehensive income. Subsequent changes in funded status must also be recognized as a component of other comprehensive income to the extent they have not yet been recognized as a component of net periodic benefit cost pursuant to SFAS No. 87, SFAS No. 88 or SFAS No. 106. The Company has

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unfunded deferred compensation contracts covering key executives based on their accomplishments within the Company which will be subject to the provisions of SFAS No. 158. The Company intends to fund its future obligations under these contracts through company-owned life insurance policies on the participants. The Company is currently evaluating the impact of SFAS No. 158 on its Consolidated Financial Statements.

2. SHAREHOLDERS EQUITY AND COMPREHENSIVE INCOME:

Additional Paid-In Capital

The decrease in additional paid-in capital during the three months ended September 30, 2006 was due to the following:

(Dollars in thousands)	
Balance, June 30, 2006	$ 232,284
Exercise of stock options	3,845
Tax benefit realized upon exercise of stock options	1,730
Stock-based compensation	1,146
Stock repurchase	(25,023)
Balance, September 30, 2006	$ 213,982

Comprehensive Income

Components of comprehensive income for the Company include net income, changes in fair market value of financial instruments designated as hedges of interest rate or foreign currency exposure and foreign currency translation charged or credited to the cumulative translation account within shareholders equity. Comprehensive income for the three months ended September 30, 2006 and 2005 were as follows:

	Components of Comprehensive Income For the Three Months Ended September 30,	
(Dollars in thousands)	**2006**	**2005**
Net income	$ 23,093	$ 22,159
Other comprehensive income (loss):		
Changes in fair market value of financial instruments designated as cash flow hedges of interest rate exposure, net of taxes	(1,046)	1
Change in cumulative foreign currency translation, net of taxes	4,268	2,508
Total comprehensive income	$ 26,315	$ 24,668

3. NET INCOME PER SHARE:

The following table sets forth a reconciliation of shares used in the computation of basic and diluted earnings per share:

	For the Three Months Ended September 30,	
(Shares in thousands)	**2006**	**2005**
Weighted average shares for basic earnings per share	45,044	44,964
Effect of dilutive securities:		
Dilutive effect of stock-based compensation	1,024	1,232
Contingent shares issuable under contingent stock agreements (see Note 5).	64	140
Weighted average shares for diluted earnings per share	46,132	46,336

Stock options, SARs and restricted stock representing 675,052 and 437,750 shares were excluded from the shares used in the computation of diluted earnings per share for the three months ended September 30, 2006 and 2005, respectively, as they were anti-dilutive.

Restricted stock awards of 187,445 and 141,650 shares for the three months ended September 30, 2006 and 2005, respectively, were excluded from the computation of basic weighted average shares outstanding as such shares were not yet vested at these dates.

4. GOODWILL AND OTHER INTANGIBLES:

The tables below contain detail related to our recorded goodwill and other intangibles as of September 30, 2006 and June 30, 2006.

(Dollars in thousands)	Salons North America	International	Beauty Schools	Hair Restoration Centers	Consolidated
Balance at June 30, 2006	$ 520,314	$ 41,224	$ 81,886	$ 134,804	$ 778,228
Goodwill acquired	14,524	456	2,147	(1,316)	15,811
Translation rateadjustments	329	930	100		1,359
Balance at September 30, 2006	$ 535,167	$ 42,610	$ 84,133	$ 133,488	$ 795,398

Goodwill acquired includes adjustments to prior year acquisitions, including the finalization of the purchase price allocation to identifiable intangible assets of the hair restoration centers which resulted in the decrease to the recorded goodwill for that segment during the quarter.

The table below presents other intangible assets as of September 30, 2006 and June 30, 2006:

	September 30, 2006			June 30, 2006		
(Dollars in thousands)	Cost	Accumulated Amortization	Net	Cost	Accumulated Amortization	Net
Amortized intangible assets:						
Brand assets and trade names	$ 110,467	$ (7,779)	$ 102,688	$ 110,087	$ (7,019)	$ 103,068
Customer list	48,743	(10,035)	38,708	48,743	(7,598)	41,145
Franchise agreements	26,301	(6,320)	19,981	24,907	(5,967)	18,940
Product license agreements	15,985	(2,381)	13,604	15,784	(2,221)	13,563