

SPORTS AUTHORITY INC /DE/
Form 10-Q/A
April 14, 2005

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SECURITIES AND EXCHANGE COMMISSION

Washington, D.C. 20549

FORM 10-Q/A Amendment No. 1

Quarterly Report Pursuant to Section 13 or 15(d) of the
Securities Exchange Act of 1934

For the Quarterly Period Ended: October 30, 2004

Commission File Number: 001-31746

THE SPORTS AUTHORITY, INC.

(Exact name of registrant as specified in its charter)

Delaware
(State or other jurisdiction of
incorporation or organization)

84-1242802
(I.R.S. Employer Identification No.)

1050 West Hampden Avenue, Englewood, Colorado 80110
(Address of principal executive offices, including zip code)

Registrant's telephone number, including area code: (303) 200-5050

Indicate by check mark whether the registrant 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 shorter period that the registrant was required to file such reports). Yes No

Indicate by check mark whether the registrant has been subject to such filing requirements for the past 90 days. Yes No

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

As of November 23, 2004, there were 25,845,023 outstanding shares of the registrant's common stock, \$.01 par value.

EXPLANATORY NOTE

This Amendment to The Sports Authority, Inc. (the "Company") Quarterly Report on Form 10-Q/A for the quarterly period ended October 30, 2004 is being filed in order to correct its previously issued quarterly consolidated financial statements for the thirteen and thirty-nine weeks ended October 30, 2004 and November 1, 2003. The corrections are to change the accounting for leases to be consistent with generally accepted accounting principles in the United States of America ("GAAP") as clarified by the Office of the Chief Accountant of the Securities and Exchange Commission ("SEC") on February 7, 2005 in a letter to the American Institute of Certified Public Accountants ("AICPA"). See Note 2 to the Company's consolidated financial statements for additional discussion.

For the convenience of the reader, this Form 10-Q/A sets forth the Original Filing in its entirety. However, this Form 10-Q/A only amends and restates Items 1, 2 and 4 of Part I of the Original Filing, in each case, solely as a result of, and to reflect, the Restatement, and no other information in the original filing is amended hereby. The foregoing items have not been updated to reflect other events occurring after the Original Filing or to modify or update those disclosures affected by subsequent events. In addition, pursuant to the rules of the SEC, Item 6 of Part II of the Original Filing has been amended to contain currently-dated certifications from our Chief Executive Officer and Chief Financial Officer, as required by Sections 302 and 906 of the Sarbanes-Oxley Act of 2002. The certifications of our Chief Executive Officer and Chief Financial Officer are attached to this Form 10-Q/A as exhibits 31.1, 31.2, 32.1 and 32.2, respectively.

PART I Financial Information

ITEM 1. Financial Statements

THE SPORTS AUTHORITY, INC. AND SUBSIDIARIES

CONSOLIDATED BALANCE SHEETS

(In Thousands, Except Share and Per Share Amounts)

| | October 30, 2004 (as restated, see Note 2) | January 31, 2004 |
|--|--|------------------|
| | (Unaudited) | |
| ASSETS | | |
| Current assets: | | |
| Cash and cash equivalents | \$ 24,340 | \$ 28,009 |
| Accounts receivable, net | 36,653 | 52,717 |
| Inventories | 855,826 | 687,215 |
| Prepaid expenses and other assets | 27,594 | 23,616 |
| Deferred income taxes | 97,978 | 89,066 |
| | <hr/> | <hr/> |
| Total current assets | 1,042,391 | 880,623 |
| Property and equipment, net | 253,805 | 211,411 |
| Favorable leases, net | 20,172 | 22,428 |
| Deferred income taxes | 47,798 | 42,967 |
| Goodwill, net | 152,484 | 132,734 |
| Other assets, net | 70,607 | 75,464 |
| | <hr/> | <hr/> |
| Total assets | \$ 1,587,257 | \$ 1,365,627 |
| | <hr/> | <hr/> |
| LIABILITIES AND STOCKHOLDERS' EQUITY | | |
| Current liabilities: | | |
| Accounts payable | \$ 385,990 | \$ 326,198 |
| Current portion of capital lease obligations | 325 | 302 |
| Accrued expenses and other current liabilities | 176,028 | 175,214 |
| | <hr/> | <hr/> |
| Total current liabilities | 562,343 | 501,714 |
| Long-term debt | 448,458 | 317,321 |
| Capital lease obligations, less current portion | 590 | 837 |
| Store closing reserve, deferred rent and other liabilities | 117,916 | 108,458 |
| | <hr/> | <hr/> |
| Total liabilities | 1,129,307 | 928,330 |
| | <hr/> | <hr/> |
| Commitments and contingencies | | |
| Stockholders' equity: | | |
| Preferred stock, \$.01 par value. 10,000,000 shares authorized; none issued | | |
| Common stock, \$.01 par value. 75,000,000 shares authorized; 27,415,577 and 26,781,727 shares issued; 25,842,823 and 25,208,973 shares outstanding | 274 | 268 |
| Additional paid-in capital | 403,351 | 394,218 |
| Unamortized restricted stock compensation | (11,644) | (15,274) |
| Accumulated other comprehensive loss | (1,042) | (759) |

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| | October 30, 2004 (as restated, see Note 2) | January 31, 2004 |
|--|--|------------------|
| Retained earnings | 90,487 | 82,320 |
| Treasury stock, 1,572,754 common shares, at cost | (23,476) | (23,476) |
| Total stockholders' equity | 457,950 | 437,297 |
| Total liabilities and stockholders' equity | \$ 1,587,257 | \$ 1,365,627 |

See accompanying notes to consolidated financial statements.

THE SPORTS AUTHORITY, INC. AND SUBSIDIARIES

CONSOLIDATED STATEMENTS OF INCOME

(Unaudited, in Thousands, Except Share and Per Share Amounts)

| | Thirteen weeks ended | | Thirty-nine weeks ended | |
|--|---|---|---|---|
| | October 30, 2004 (As restated, see Note 2) | November 1, 2003 (As restated, see Note 2) | October 30, 2004 (As restated, see Note 2) | November 1, 2003 (As restated, see Note 2) |
| Net sales | \$ 545,041 | \$ 552,534 | \$ 1,722,107 | \$ 1,048,480 |
| Cost of goods sold, buying, distribution and occupancy | 398,677 | 405,909 | 1,248,120 | 773,355 |
| Gross profit | 146,364 | 146,625 | 473,987 | 275,125 |
| Operating expenses | 139,353 | 135,635 | 422,235 | 247,377 |
| Merger integration costs | 4,774 | 19,677 | 21,750 | 21,354 |
| Pre-opening expenses | 1,562 | 533 | 3,243 | 1,187 |
| Operating income (loss) | 675 | (9,220) | 26,759 | 5,207 |
| Non operating income (expense): | | | | |
| Interest expense | (5,522) | (3,855) | (14,648) | (8,005) |
| Other income, net | 341 | 309 | 1,284 | 2,828 |
| Income (loss) before income taxes | (4,506) | (12,766) | 13,395 | 30 |
| Income tax benefit (expense) | 1,753 | 4,978 | (5,228) | 1,691 |
| Net income (loss) | \$ (2,753) | \$ (7,788) | \$ 8,167 | \$ 1,721 |
| Earnings (loss) per share: | | | | |
| Basic | \$ (0.11) | \$ (0.32) | \$ 0.32 | \$ 0.11 |
| Diluted | \$ (0.11) | \$ (0.32) | \$ 0.31 | \$ 0.10 |
| Weighted average shares of common stock outstanding: | | | | |
| Basic | 25,821,965 | 24,408,686 | 25,639,714 | 16,059,729 |
| Diluted | 25,821,965 | 24,408,686 | 26,375,278 | 17,189,259 |

See accompanying notes to consolidated financial statements.

THE SPORTS AUTHORITY, INC. AND SUBSIDIARIES

CONSOLIDATED STATEMENTS OF STOCKHOLDERS' EQUITY AND COMPREHENSIVE INCOME

(Unaudited, in Thousands, Except Share Amounts)

| | Common stock | | Additional paid- in capital | Unamortized restricted stock compensation | Accumulated other comprehensive loss | Retained earnings | Comprehensive income | Treasury stock | | Total stockholders' equity |
|---|--------------|--------|--------------------------------------|--|---|----------------------|-------------------------|----------------|-------------|----------------------------------|
| | Shares | Amount | | | | | | Shares | Amount | |
| BALANCES AT JANUARY 31, 2004 | 25,208,973 | \$ 268 | \$ 394,218 | \$ (15,274) | \$ (759) | \$ 82,320 | | 1,572,754 | \$ (23,476) | \$ 437,297 |
| Net income (as restated, see Note 2) | | | | | | 8,167 | \$ 8,167 | | | 8,167 |
| Unrealized loss on interest rate swaps | | | | | (283) | | (283) | | | (283) |
| Comprehensive income (as restated, see Note 2) | | | | | | | \$ 7,884 | | | |
| Exercise of stock options, including tax benefit of \$2,138 | 332,905 | 3 | 8,636 | | | | | | | 8,639 |
| Restricted stock grant | | | 2,509 | (2,509) | | | | | | |
| Cancellation of Restricted Stock | | | (1,161) | 1,161 | | | | | | |
| Restricted stock vesting and repurchase | 300,945 | 3 | (851) | | | | | | | (848) |
| Amortization of restricted stock | | | | 4,978 | | | | | | 4,978 |
| BALANCES AT OCTOBER 30, 2004 (as restated, see Note 2) | 25,842,823 | \$ 274 | \$ 403,351 | \$ (11,644) | \$ (1,042) | \$ 90,487 | | 1,572,754 | \$ (23,476) | \$ 457,950 |

See accompanying notes to consolidated financial statements.

THE SPORTS AUTHORITY, INC. AND SUBSIDIARIES

CONSOLIDATED STATEMENTS OF CASH FLOWS

(Unaudited, in Thousands)

| | Thirty-nine weeks ended | |
|---|---|---|
| | October 30, 2004 (As restated, see Note 2) | November 1, 2003 (As restated, see Note 2) |
| CASH FLOWS FROM OPERATING ACTIVITIES: | | |
| Net income | \$ 8,167 | \$ 1,721 |
| Adjustments to reconcile net income to net cash used in operating activities: | | |
| Depreciation and amortization | 43,562 | 25,498 |
| Amortization of loan acquisition costs | 1,609 | 938 |
| Impairment of long-lived assets | 1,074 | |
| Gain on sale of marketable securities | | (100) |
| Deferred income taxes | 5,228 | (1,690) |
| (Gain)/Loss on disposition of assets | (14) | 558 |
| Change in operating assets and liabilities: | | |
| Accounts receivable, net | 2,123 | (2,755) |
| Inventories | (170,268) | (118,679) |
| Prepaid expenses and other current assets | (4,042) | (2,373) |
| Other assets | (794) | 1,835 |
| Accounts payable | 59,633 | 81,237 |
| Accrued expenses and other current liabilities | (18,587) | (15,668) |
| Other long term liabilities | (5,509) | 10,223 |
| | <u>(77,818)</u> | <u>(19,255)</u> |
| CASH FLOWS FROM INVESTING ACTIVITIES: | | |
| Purchases of property and equipment | (85,850) | (58,197) |
| Proceeds from sale of property and equipment | 20,246 | |
| Proceeds from sale of marketable securities | | 192 |
| Proceeds from mortgage notes | 3,088 | |
| Direct merger costs with The Sports Authority, Inc., net of cash acquired | | (38,799) |
| Other investing activities, net | 462 | 39 |
| | <u>(62,054)</u> | <u>(96,765)</u> |
| CASH FLOWS FROM FINANCING ACTIVITIES: | | |
| Proceeds from long-term debt | 880,099 | 487,082 |
| Principal payments on long-term debt | (748,962) | (357,465) |
| Payment of financing fees | (1,211) | (6,000) |
| Principal payments on capital lease obligations | (224) | (549) |
| Proceeds from the sale of common stock under option plans | 6,501 | 6,070 |
| | <u>136,203</u> | <u>129,138</u> |
| Increase (decrease) in cash and cash equivalents | (3,669) | 13,118 |
| Cash and cash equivalents at beginning of period | 28,009 | 10,156 |
| | <u>\$ 24,340</u> | <u>\$ 23,274</u> |

Thirty-nine weeks ended

Supplemental disclosures of cash flow information:

| | | | | |
|--|----|--------|----|-------|
| Cash paid during the period for interest | \$ | 10,666 | \$ | 6,096 |
| Cash paid during the period for income taxes | \$ | 586 | \$ | 759 |

See accompanying notes to consolidated financial statements.

THE SPORTS AUTHORITY, INC. AND SUBSIDIARIES

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (As restated, see Note 2)

1. Company

On August 4, 2003, a wholly owned subsidiary of Gart Sports Company completed a merger with The Sports Authority, Inc. In connection with the merger, Gart Sports Company ("Gart") was renamed The Sports Authority, Inc. The references made to the entities herein refer to The Sports Authority, Inc. (formerly Gart Sports Company, which is also referred to as "Sports Authority" or "Company"). "TSA" refers to TSA Stores, Inc., (formerly known as The Sports Authority, Inc.). The statements of income for the thirteen and the thirty-nine weeks ended October 30, 2004 reflect the results of the combined company, while results for the thirteen and thirty-nine weeks ended November 1, 2003 include the combined company only for the thirteen weeks ended November 1, 2003 and the former Gart Sports Company on a stand-alone basis for the first twenty-six weeks of fiscal 2003. In the merger, the TSA shareholders received 0.37 shares of Sports Authority common stock for each share of TSA stock they owned. The combined company operated 390 retail sporting goods stores in 45 states as of October 30, 2004.

Under license and e-commerce agreements with GSI Commerce Inc. ("GSI"), GSI operates sporting goods retail websites at www.thesportsauthority.com, www.gartsports.com, www.sportmart.com, and www.oshmans.com. Under these agreements, GSI owns certain content and technology related to the website, purchases and owns the merchandise sold on the websites, and hosts, maintains, fulfills orders and furnishes all other "back-end" operations required to operate the websites. GSI receives all revenue generated from the websites and pays the Company a royalty based on sales from these sites.

Mega Sports Co., Ltd. ("Mega Sports"), a joint venture between the Company and AEON Co., Ltd. ("AEON"), operates *The Sports Authority* stores in Japan pursuant to a license agreement with the Company. Under the agreement, Mega Sports pays a royalty based on its gross sales, in exchange for use of trademarks and other intangible property owned by the Company and for merchandising assistance provided by the Company. In April 2004, the license agreement was amended to, among other things, extend the term of the agreement from 2005 to 2014 and to revise the royalty payable by Mega Sports. TSA Stores has a 19.9% ownership interest in Mega Sports, which is accounted for under the cost method. AEON is a major Japanese retailer that owns 4.5% of the Company's outstanding stock.

2. Restatement of Financial Statements

On February 7, 2005, the Office of the Chief Accountant of the Securities and Exchange Commission ("SEC") issued a letter to the American Institute of Certified Public Accountants regarding certain operating lease-related accounting issues and their application under generally accepted accounting principles in the United States of America ("GAAP"). As a result of this letter, the Company's management initiated a thorough review of its accounting for leases and has concluded that its accounting was not in accordance with generally accepted accounting principles. The Company has corrected its accounting for tenant improvement allowances and to reflect the recognition of rent expense on a straight-line basis, including consideration of rent holidays and applicable rent escalations. For purposes of determination of the term of the lease, the Company considers the commencement date of the lease term to be the earlier of the date when the Company becomes legally obligated for the rent payments or the date when it takes possession of the building for purposes of constructing the build-out. As a result, the Company restated its consolidated financial statements for each of the fiscal years ended January 31, 2004, February 1, 2003 and February 2, 2002 and for the first three quarters of fiscal 2004. The consolidated financial statements included in this Form 10-Q/A have been restated to reflect the adjustments described above.

The Company had historically accounted for tenant improvement allowances as reductions to the related leasehold improvement asset on the consolidated balance sheets and capital expenditures in investing activities on the consolidated statements of cash flows. Management has determined that these allowances should be recorded as deferred rent liabilities on the consolidated balance sheets and as a component of operating activities on the consolidated statements of cash flows.

The Company had historically recognized straight-line rent expense for leases beginning on the earlier of the store opening date or lease commencement date, which had the effect of excluding the build-out period (or rent holiday period) of its stores from the calculation of the period over which it expensed rent. The Company has determined that it should have included the build-out period in its calculation of straight line rent expense in accordance with Financial Accounting Standards Board Technical Bulletin No. 85-3, "Accounting for Operating Leases with Scheduled Rent Increases" and has corrected its straight line rent accrual and deferred lease credits accordingly. Straight-line rent recorded during the build-out period is capitalized as a component of the historical cost of leasehold improvements included in property and equipment. The capitalized rent is amortized over the useful life of the related asset or the lease term, whichever is shorter. Straight-line rent recorded during our pre-opening period (completion of build-out through store open date) is recorded as a pre-opening expense. The correction of this accounting requires the Company to record additional deferred rent in "Other long-term liabilities", increase "Property and equipment, net" and to adjust "Retained earnings" on the consolidated balance sheets. This restatement to previously issued consolidated financial statements does not have an effect on total net cash flows during any of the periods restated. Certain reclassifications have been reflected in the statement of cash flows to include tenant improvement allowances within operating activities and exclude them as a component of capital expenditures within investing activities.

Following is a summary of the significant effects of these corrections on the Company's consolidated balance sheet as of October 30, 2004, as well as the effects of these corrections on the Company's consolidated statements of income and cash flows for the thirteen weeks and thirty-nine weeks ended October 30, 2004 and November 1, 2003 (in thousands, except share data):

| | Consolidated Statements of Income | | |
|--|--|--------------------|--------------------|
| | As previously reported | Adjustments | As restated |
| Thirteen weeks ended October 30, 2004 | | | |
| Cost of goods sold, buying, distribution and occupancy | 398,306 | 371 | 398,677 |
| Gross profit | 146,735 | (371) | 146,364 |
| Operating expenses | 139,344 | 9 | 139,353 |
| Pre-opening expenses | 1,075 | 487 | 1,562 |
| Operating income | 1,542 | (867) | 675 |
| Income before income taxes | (3,639) | (867) | (4,506) |
| Income tax expense | 1,419 | 334 | 1,753 |
| Net income | (2,220) | (533) | (2,753) |
| Earnings per common share basic | (0.09) | (0.02) | (0.11) |
| Earnings per common share diluted | (0.09) | (0.02) | (0.11) |

Thirteen weeks ended November 1, 2003

| | | | |
|--|----------|--------|----------|
| Cost of goods sold, buying, distribution and occupancy | 405,818 | 91 | 405,909 |
| Gross profit | 146,716 | (91) | 146,625 |
| Operating Expenses | 135,610 | 25 | 135,635 |
| Pre-opening expenses | 426 | 107 | 533 |
| Operating income | (8,997) | (223) | (9,220) |
| Income before income taxes | (12,543) | (223) | (12,766) |
| Income tax expense | 4,892 | 86 | 4,978 |
| Net income | (7,651) | (137) | (7,788) |
| Earnings per common share basic | (0.31) | (0.01) | (0.32) |
| Earnings per common share diluted | (0.31) | (0.01) | (0.32) |

| | <u>As previously reported</u> | <u>Adjustments</u> | <u>As restated</u> |
|--|-----------------------------------|--------------------|--------------------|
| Thirty-nine weeks ended October 30, 2004 | | | |
| Cost of goods sold, buying, distribution and occupancy | 1,248,231 | (111) | 1,248,120 |
| Gross profit | 473,876 | 111 | 473,987 |
| Operating Expenses | 422,208 | 27 | 422,235 |
| Pre-opening expenses | 2,461 | 782 | 3,243 |
| Operating income | 27,457 | (698) | 26,759 |
| Income before income taxes | 14,093 | (698) | 13,395 |
| Income tax expense | (5,497) | 269 | (5,228) |
| Net income | 8,596 | (429) | 8,167 |
| Earnings per common share basic | 0.34 | (0.02) | |