

LIFE TIME FITNESS INC
Form 10-Q
October 30, 2009

Table of Contents

**UNITED STATES
SECURITIES AND EXCHANGE COMMISSION
WASHINGTON, D.C. 20549**

FORM 10-Q

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

For the quarterly period ended September 30, 2009

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 No. 001-32230**

Life Time Fitness, Inc.

(Exact name of registrant as specified in its charter)

Minnesota

(State or other jurisdiction of incorporation or organization)

41-1689746

(I.R.S. Employer Identification No.)

**2902 Corporate Place
Chanhassen, Minnesota**

(Address of principal executive offices)

55317

(Zip Code)

Registrant's telephone number, including area code: **952-947-0000**

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 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 or a smaller reporting company. See definitions of large accelerated filer, accelerated filer and smaller reporting company in Rule 12b-2 of the Exchange Act.

Large accelerated filer Accelerated filer Non-accelerated filer Smaller reporting company
(do not check if smaller reporting company)

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 as of October 26, 2009 was 41,392,720 common shares.

TABLE OF CONTENTS

	Page
<u>PART I. FINANCIAL INFORMATION</u>	
<u>Item 1. Financial Statements</u>	
<u>Consolidated Balance Sheets as of September 30, 2009 (unaudited) and December 31, 2008</u>	3
<u>Consolidated Statements of Operations for the Three and Nine Months Ended September 30, 2009 and 2008 (unaudited)</u>	4
<u>Consolidated Statements of Cash Flows for the Nine Months Ended September 30, 2009 and 2008 (unaudited)</u>	5
<u>Notes to Unaudited Consolidated Financial Statements</u>	6
<u>Item 2. Management's Discussion and Analysis of Financial Condition and Results of Operations</u>	12
<u>Item 3. Quantitative and Qualitative Disclosures about Market Risk</u>	21
<u>Item 4. Controls and Procedures</u>	22
<u>PART II. OTHER INFORMATION</u>	
<u>Item 1. Legal Proceedings</u>	22
<u>Item 1A. Risk Factors</u>	22
<u>Item 2. Unregistered Sales of Equity Securities and Use of Proceeds</u>	22
<u>Item 3. Defaults Upon Senior Securities</u>	22
<u>Item 4. Submission of Matters to a Vote of Security Holders</u>	22
<u>Item 5. Other Information</u>	22
<u>Item 6. Exhibits</u>	23
<u>SIGNATURES</u>	24
<u>EX-31.1</u>	
<u>EX-31.2</u>	
<u>EX-32</u>	

Table of Contents**PART I. FINANCIAL INFORMATION****Item 1. Financial Statements**

LIFE TIME FITNESS, INC. AND SUBSIDIARIES
CONSOLIDATED BALANCE SHEETS
(In thousands, except share and per share data)

	September 30, 2009 (Unaudited)	December 31, 2008
ASSETS		
CURRENT ASSETS:		
Cash and cash equivalents	\$ 8,137	\$ 10,829
Accounts receivable, net	3,192	6,114
Inventories and center operating supplies	13,935	14,632
Prepaid expenses and other current assets	14,964	10,994
Deferred membership origination costs	21,497	19,877
Deferred income taxes	1,872	1,365
Total current assets	63,597	63,811
PROPERTY AND EQUIPMENT, net	1,507,073	1,515,957
RESTRICTED CASH	3,785	3,936
DEFERRED MEMBERSHIP ORIGINATION COSTS	11,726	14,210
OTHER ASSETS	49,967	49,789
TOTAL ASSETS	\$ 1,636,148	\$ 1,647,703
LIABILITIES AND SHAREHOLDERS EQUITY		
CURRENT LIABILITIES:		
Current maturities of long-term debt	\$ 12,130	\$ 10,335
Accounts payable	16,926	14,842
Construction accounts payable	10,602	63,418
Accrued expenses	52,323	46,230
Deferred revenue	37,230	36,098
Total current liabilities	129,211	170,923
LONG-TERM DEBT, net of current portion	671,165	702,569
DEFERRED RENT LIABILITY	28,464	27,925
DEFERRED INCOME TAXES	60,252	51,982
DEFERRED REVENUE	10,622	13,719
OTHER LIABILITIES	19,390	27,684
Total liabilities	919,104	994,802
COMMITMENTS AND CONTINGENCIES (Note 6)		
SHAREHOLDERS EQUITY:		
Undesignated preferred stock, 10,000,000 shares authorized; none issued or outstanding		

Edgar Filing: LIFE TIME FITNESS INC - Form 10-Q

Common stock, \$.02 par value, 75,000,000 and 50,000,000 shares authorized, respectively; 41,391,895 and 39,612,775 shares issued and outstanding, respectively	828	793
Additional paid-in capital	393,864	385,095
Retained earnings	325,718	271,711
Accumulated other comprehensive loss	(3,366)	(4,698)
Total shareholders' equity	717,044	652,901
TOTAL LIABILITIES AND SHAREHOLDERS' EQUITY	\$ 1,636,148	\$ 1,647,703

See notes to unaudited consolidated financial statements.

3

Table of Contents

LIFE TIME FITNESS, INC. AND SUBSIDIARIES
CONSOLIDATED STATEMENTS OF OPERATIONS
(In thousands, except per share data)
(Unaudited)

	For the Three Months Ended September 30,		For the Nine Months Ended September 30,	
	2009	2008	2009	2008
REVENUE:				
Membership dues	\$ 144,832	\$ 131,232	\$ 425,070	\$ 377,001
Enrollment fees	6,617	6,818	19,630	19,991
In-center revenue	59,129	56,151	178,681	167,385
Total center revenue	210,578	194,201	623,381	564,377
Other revenue	3,742	4,608	9,922	11,290
Total revenue	214,320	198,809	633,303	575,667
OPERATING EXPENSES:				
Center operations	127,468	116,300	383,313	337,139
Advertising and marketing	5,756	7,287	20,145	23,608
General and administrative	9,669	9,453	33,172	30,707
Other operating	8,017	4,926	17,791	13,696
Depreciation and amortization	23,428	18,720	68,127	52,500
Total operating expenses	174,338	156,686	522,548	457,650
Income from operations	39,982	42,123	110,755	118,017
OTHER INCOME (EXPENSE):				
Interest expense, net of interest income of \$208, \$30, \$370 and \$119, respectively	(7,651)	(7,185)	(23,005)	(21,301)
Equity in earnings of affiliate	316	336	985	985
Total other income (expense)	(7,335)	(6,849)	(22,020)	(20,316)
INCOME BEFORE INCOME TAXES	32,647	35,274	88,735	97,701
PROVISION FOR INCOME TAXES	12,014	13,700	34,728	38,895
NET INCOME	\$ 20,633	\$ 21,574	\$ 54,007	\$ 58,806
BASIC EARNINGS PER COMMON SHARE	\$ 0.52	\$ 0.55	\$ 1.38	\$ 1.51
DILUTED EARNINGS PER COMMON SHARE	\$ 0.51	\$ 0.55	\$ 1.36	\$ 1.49
WEIGHTED AVERAGE NUMBER OF COMMON SHARES OUTSTANDING BASIC	39,410	39,025	39,221	38,946

WEIGHTED AVERAGE NUMBER OF
COMMON SHARES OUTSTANDING
DILUTED

40,255	39,370	39,687	39,350
--------	--------	--------	--------

See notes to unaudited consolidated financial statements.

4

Table of Contents

LIFE TIME FITNESS, INC. AND SUBSIDIARIES
CONSOLIDATED STATEMENTS OF CASH FLOWS
(In thousands)
(Unaudited)

	For the Nine Months Ended September 30,	
	2009	2008
CASH FLOWS FROM OPERATING ACTIVITIES:		
Net income	\$ 54,007	\$ 58,806
Adjustments to reconcile net income to net cash provided by operating activities:		
Depreciation and amortization	68,127	52,500
Deferred income taxes	6,957	8,094
Provision for doubtful accounts	(8)	15
Loss on disposal of property and equipment, net	818	1,159
Gain on sale of land held for sale	(873)	
Amortization of deferred financing costs	1,925	1,078
Share-based compensation	5,907	5,989
Excess tax benefit related to share-based payment arrangements	(433)	(38)
Equity in earnings of affiliate	(985)	(985)
Changes in operating assets and liabilities	2,000	16,840
Other	1,109	54
Net cash provided by operating activities	138,551	143,512
CASH FLOWS FROM INVESTING ACTIVITIES:		
Purchases of property and equipment	(116,853)	(360,551)
Proceeds from sale of property and equipment	8	161,885
Proceeds from sale of land held for sale	1,327	
Proceeds from property insurance settlements		317
Increase in other assets	(213)	(6,443)
Decrease (increase) in restricted cash	151	(2,518)
Net cash used in investing activities	(115,580)	(207,310)
CASH FLOWS FROM FINANCING ACTIVITIES:		
Proceeds from long-term borrowings	7,813	39,188
Repayments of long-term borrowings	(7,755)	(13,043)
Proceeds from (repayments of) revolving credit facility, net	(27,600)	42,500
Increase in deferred financing costs	(745)	(6,113)
Excess tax benefit related to share-based payment arrangements	433	38
Proceeds from stock option exercises	2,191	2,993
Net cash provided by (used in) financing activities	(25,663)	65,563
INCREASE (DECREASE) IN CASH AND CASH EQUIVALENTS	(2,692)	1,765
CASH AND CASH EQUIVALENTS Beginning of period	10,829	5,354
CASH AND CASH EQUIVALENTS End of period	\$ 8,137	\$ 7,119

See notes to unaudited consolidated financial statements.

Table of Contents

LIFE TIME FITNESS, INC. AND SUBSIDIARIES
NOTES TO UNAUDITED CONSOLIDATED FINANCIAL STATEMENTS
(Table amounts in thousands, except share and per share data)

1. Basis of Presentation

The accompanying unaudited consolidated financial statements have been prepared in accordance with accounting principles generally accepted in the United States for interim financial information and with the instructions to Form 10-Q and Article 10 of Regulation S-X. Accordingly, they do not include all of the information and notes required by accounting principles generally accepted in the United States for complete financial statements. In the opinion of management, all adjustments (consisting of normal recurring adjustments) considered necessary to fairly present financial position, results of operations and cash flows for the periods have been included.

These interim consolidated financial statements and the related notes should be read in conjunction with the annual consolidated financial statements and notes included in the latest Form 10-K, as filed with the Securities and Exchange Commission (SEC), which includes audited consolidated financial statements for the three fiscal years ended December 31, 2008. We evaluated the impact of events occurring after September 30, 2009 up to October 30, 2009, which is the date of issuance of these consolidated financial statements. These statements contain all necessary adjustments and disclosures resulting from that evaluation.

2. Share-Based Compensation

We have four share-based compensation plans, the FCA, Ltd. 1996 Stock Option Plan (the 1996 Plan), the Life Time Fitness, Inc. 1998 Stock Option Plan (the 1998 Plan), the Amended and Restated Life Time Fitness, Inc. 2004 Long-Term Incentive Plan (the 2004 Plan) and an Employee Stock Purchase Plan (the ESPP), collectively, the share-based compensation plans. In connection with approval for the 2004 Plan, our Board of Directors approved a resolution to cease making additional grants under the 1996 Plan and the 1998 Plan. The types of awards that may be granted under the 2004 Plan include incentive and non-qualified options to purchase shares of common stock, stock appreciation rights, restricted shares, restricted share units, performance awards and other types of share-based awards.

As of September 30, 2009, we had granted a total of 5,587,165 options to purchase common stock under all of the share-based compensation plans, of which options to purchase 827,578 shares were outstanding, and a total of 2,525,837 restricted shares were granted, of which 1,981,757 restricted shares were outstanding and unvested. We use the term restricted shares to define nonvested shares granted to employees and non-employee directors, whereas applicable accounting guidance reserves that term for fully vested and outstanding shares whose sale is contractually or governmentally prohibited for a specified period of time.

Total share-based compensation expense included in our consolidated statements of operations for the three and nine months ended September 30, 2009 and 2008, was as follows:

	For the Three Months Ended September 30,		For the Nine Months Ended September 30,	
	2009	2008	2009	2008
Share-based compensation expense related to stock options	\$ 98	\$ 533	\$ 730	\$ 1,852
Share-based compensation expense related to restricted shares	1,752	1,531	5,087	4,039
Share-based compensation expense related to ESPP	30	30	90	98
Total share-based compensation expense	\$ 1,880	\$ 2,094	\$ 5,907	\$ 5,989

Table of Contents

LIFE TIME FITNESS, INC. AND SUBSIDIARIES
NOTES TO UNAUDITED CONSOLIDATED FINANCIAL STATEMENTS
(Table amounts in thousands, except share and per share data)

The following table summarizes the stock option transactions for the three month periods ended March 31, 2009, June 30, 2009 and September 30, 2009:

	Stock Options	Weighted Average Exercise Price	Weighted Average Remaining Contractual Term (in years)	Aggregate Intrinsic Value
Outstanding at December 31, 2008	980,929	\$ 21.65	5.6	
Granted				
Exercised				
Canceled	(2,354)	\$ 31.06		
Outstanding at March 31, 2009	978,575	\$ 21.63	5.4	\$ 632
Granted				
Exercised	(24,100)	\$ 8.00		
Canceled	(3,947)	\$ 29.85		
Outstanding at June 30, 2009	950,528	\$ 21.94	5.2	\$ 2,439
Granted				
Exercised	(121,950)	\$ 16.38		
Canceled	(1,000)	\$ 25.47		
Outstanding at September 30, 2009	827,578	\$ 22.76	5.0	\$ 5,800
Vested or Expected to Vest at September 30, 2009	825,702	\$ 22.71	5.0	\$ 5,800
Exercisable at September 30, 2009	806,963	\$ 22.22	5.0	\$ 5,800

No options were granted during the nine months ended September 30, 2009 or the nine months ended September 30, 2008. As of September 30, 2009, there was \$0.1 million of unrecognized compensation expense related to stock options that is expected to be recognized over a weighted average period of 0.3 years.

The aggregate intrinsic value in the table above represents the total pretax intrinsic value (the difference between our closing stock price at September 30, 2009 and the exercise price, multiplied by the number of in-the-money options) that would have been received by the option holders, had all option holders exercised their options on September 30, 2009. This amount changes based on the fair market value of our stock. Total intrinsic value of options exercised during the nine months ended September 30, 2009 and 2008 was \$1.8 million and \$3.7 million, respectively.

Net cash proceeds from the exercise of stock options were \$2.2 million and \$3.0 million for the nine months ended September 30, 2009, and 2008, respectively. The actual income tax benefit realized from stock option exercises total \$0.4 million and less than \$0.1 million, respectively, for those same periods.

Table of Contents

LIFE TIME FITNESS, INC. AND SUBSIDIARIES
NOTES TO UNAUDITED CONSOLIDATED FINANCIAL STATEMENTS
(Table amounts in thousands, except share and per share data)

The following table summarizes the unvested restricted shares activity for the three month periods ended March 31, 2009, June 30, 2009 and September 30, 2009:

	Restricted Shares	Range of Market Price Per Share on Grant Date
Outstanding at December 31, 2008	487,203	\$ 14.31-53.95
Granted	657,315	\$ 9.72
Canceled	(2,253)	\$ 14.31-49.06
Vested	(100,136)	\$ 14.31-53.95
Outstanding at March 31, 2009	1,042,129	\$ 9.72-53.95
Granted	1,028,514	\$ 16.39-20.44
Canceled	(50,366)	\$ 9.72-50.82
Vested	(35,206)	\$ 14.31-50.82
Outstanding at June 30, 2009	1,985,071	\$ 9.72-53.95
Granted		\$
Canceled	(140)	\$ 20.44-46.51
Vested	(3,174)	\$ 9.72-51.15
Outstanding at September 30, 2009	1,981,757	\$ 9.72-53.95

During the nine months ended September 30, 2009 and 2008, we issued 1,685,829 and 404,638 shares of restricted stock, respectively, with an aggregate fair value of \$27.3 million and \$11.1 million, respectively. The grant date fair market value of restricted shares that vested during the nine months ended September 30, 2009 was \$5.2 million. The total value of each restricted stock grant, based on the fair market value of the stock on the date of grant, is amortized to compensation expense on a straight-line basis over the related vesting period. As of September 30, 2009, there was \$17.7 million of unrecognized compensation expense related to restricted stock that is expected to be recognized over a weighted average period of 2.9 years.

In June 2009, the Compensation Committee of our Board of Directors approved the grant of 996,000 shares of long-term performance-based restricted stock to serve as an incentive to our senior management team to achieve certain diluted earnings per share (EPS) targets in 2011 and 2012. If a specified EPS target is achieved for fiscal 2011, 50% of the restricted shares will vest. If a higher EPS target is achieved for fiscal 2011, 100% of the restricted shares will vest. If the grant has not fully vested after fiscal 2011, 50% of the shares will vest if a specified EPS target is achieved for fiscal 2012. If none of the shares vested after fiscal 2011, 100% of the shares will vest if a higher EPS target is achieved for fiscal 2012. In the event that we do not achieve the required EPS targets, the restricted stock will be forfeited. A maximum of \$20.4 million could be recognized as compensation expense under this grant if all EPS targets are met.

We consider the specific EPS targets to be competitively sensitive information during the performance period. We believe these targets, inclusive of compensation expense under this grant, to be aggressive goals in excess of our current baseline expectations, and therefore, we did not recognize any compensation expense associated with the grant during the nine months ended September 30, 2009, nor has any share amount been included in our total diluted shares. If all of the targets had been considered probable at September 30, 2009, we would have recognized \$2.3 million of

compensation cost during the nine months ended September 30, 2009. If it becomes probable that certain of the EPS performance targets will be achieved, the corresponding estimated cost of the grant will be recorded as compensation expense over the performance period. The probability of reaching the targets is revaluated each reporting period. If it becomes probable that certain of the target performance levels will be achieved, a cumulative adjustment will be recorded and future compensation expense will increase based on the currently projected performance levels. If we later determine that it is not probable that the minimum EPS performance threshold for the grants will be met, no further compensation cost will be recognized and any previously recognized compensation cost will be reversed.

Table of Contents

LIFE TIME FITNESS, INC. AND SUBSIDIARIES
NOTES TO UNAUDITED CONSOLIDATED FINANCIAL STATEMENTS
(Table amounts in thousands, except share and per share data)

Our ESPP provides for the sale of our common stock to our employees at discounted purchase prices. The cost per share under this plan is 90% of the fair market value of our common stock on the last day of the purchase period, as defined. The current purchase period for employees under the ESPP began July 1, 2009 and ends December 31, 2009. Compensation expense under the ESPP is estimated based on the discount of 10% at the end of the purchase period. In June 2006, our Board of Directors authorized the repurchase of 500,000 shares of our common stock from time to time in the open market or otherwise for the primary purpose of offsetting the dilutive effect of shares pursuant to our ESPP. During the first nine months of 2009, we repurchased 67,268 shares for approximately \$1.0 million. As of September 30, 2009, there were 375,388 remaining shares authorized to be repurchased for this purpose. The shares repurchased to date have been purchased in the open market and, upon repurchase, became authorized, but unissued shares of our common stock.

3. Earnings per Share

Basic EPS is computed by dividing net income applicable to common shareholders by the weighted average number of shares of common stock outstanding for each period. Diluted EPS is computed based on the weighted-average number of common shares and common equivalent shares. Common equivalent shares represent the effect of dilutive stock options and restricted stock awards during each period presented. Stock options excluded from the calculation of diluted EPS because the option exercise or award price was greater than the average market price of the common share were 435,128 and 75,552 for the nine months ended September 30, 2009 and 2008, respectively. Long-term performance-based restricted shares excluded from the calculation of diluted EPS because vesting of the shares was not probable were 996,000 and 0 for the nine months ended September 30, 2009 and 2008, respectively.

The basic and diluted earnings per share calculations are shown below:

	For the Three Months Ended September 30,		For the Nine Months Ended September 30,	
	2009	2008	2009	2008
Net income	\$ 20,633	\$ 21,574	\$ 54,007	\$ 58,806
Weighted average number of common shares outstanding basic	39,410	39,025	39,221	38,946
Effect of dilutive stock options	141	215	55	215
Effect of dilutive restricted stock awards	704	130	411	189
Weighted average number of common shares outstanding diluted	40,255	39,370	39,687	39,350
Basic earnings per common share	\$ 0.52	\$ 0.55	\$ 1.38	\$ 1.51
Diluted earnings per common share	\$ 0.51	\$ 0.55	\$ 1.36	\$ 1.49

4. Operating Segments

Our operations are conducted mainly through our large, multi-use sports, fitness and family recreation centers. We aggregate the activities of our centers and other ancillary products and services into one reportable segment as none of the centers or other ancillary products or services meet the quantitative thresholds for separate disclosure under the applicable accounting guidance. Each of the centers has similar expected economic characteristics, service and product offerings, customers and design. Each of the other ancillary products and services either directly or indirectly, through advertising or branding, complement the operations of the centers. Our chief operating decision maker uses EBITDA, which consists of net income plus interest expense, net, provision for income taxes and depreciation and

amortization, as the primary measure of operating segment performance.

Table of Contents

**LIFE TIME FITNESS, INC. AND SUBSIDIARIES
NOTES TO UNAUDITED CONSOLIDATED FINANCIAL STATEMENTS
(Table amounts in thousands, except share and per share data)**

The following table presents revenue for the three and nine months ended September 30, 2009 and 2008:

For the Three Months