

LIFE TIME FITNESS, INC.
Form 10-Q
July 30, 2014

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 June 30, 2014

or

TRANSITION REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT
OF 1934

Commission File Number: 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)

952-947-0000
(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 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.

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

Large accelerated filer Accelerated filer
Non-accelerated filer (Do not check if a smaller reporting company) 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 July 18, 2014 was 39,099,235 common shares.

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)

(Unaudited)

	June 30, 2014	December 31, 2013
ASSETS		
Current assets:		
Cash and cash equivalents	\$ 15,850	\$ 8,334
Accounts receivable, net	11,091	8,298
Center operating supplies and inventories	36,660	32,778
Prepaid expenses and other current assets	28,942	25,802
Deferred membership origination costs	9,455	9,945
Deferred income taxes	4,526	6,881
Income tax receivable	7,614	6,698
Total current assets	114,138	98,736
Property and equipment, net	2,289,876	2,105,077
Restricted cash	588	850
Deferred membership origination costs	6,433	5,210
Goodwill	57,478	49,195
Intangible assets, net	35,175	29,299
Other assets	43,675	42,684
Total assets	\$ 2,547,363	\$ 2,331,051
LIABILITIES AND SHAREHOLDERS' EQUITY		
Current liabilities:		
Current maturities of long-term debt	\$ 27,366	\$ 24,505
Accounts payable	37,688	28,645
Construction accounts payable	43,436	47,342
Accrued expenses	67,327	67,435
Deferred revenue	46,037	35,032
Total current liabilities	221,854	202,959
Long-term debt, net of current portion	1,097,716	824,093
Deferred rent liability	29,149	28,933
Deferred income taxes	94,496	100,504
Deferred revenue	6,499	5,246
Other liabilities	20,938	21,287
Total liabilities	1,470,652	1,183,022
Commitments and contingencies (Note 6)		
Shareholders' equity:		
Undesignated preferred stock, 10,000,000 shares authorized; none issued or outstanding	—	—
Common stock, \$.02 par value, 75,000,000 shares authorized; 39,660,084 and 42,115,549 shares issued and outstanding, respectively	794	843
Additional paid-in capital	272,921	402,147
Retained earnings	808,774	750,654

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

Accumulated other comprehensive loss	(5,778	) (5,615)
Total shareholders' equity	1,076,711	1,148,029	
Total liabilities and shareholders' equity	\$2,547,363	\$2,331,051	

See notes to unaudited consolidated financial statements.

3

LIFE TIME FITNESS, INC. AND SUBSIDIARIES
CONSOLIDATED STATEMENTS OF OPERATIONS

(In thousands, except per share data)

(Unaudited)

	For the Three Months Ended		For the Six Months Ended	
	June 30,		June 30,	
	2014	2013	2014	2013
Revenue:				
Membership dues	\$205,164	\$194,816	\$401,979	\$381,190
Enrollment fees	3,019	3,573	6,142	6,969
In-center revenue	104,359	97,275	202,764	189,246
Total center revenue	312,542	295,664	610,885	577,405
Other revenue	14,022	12,444	27,634	21,450
Total revenue	326,564	308,108	638,519	598,855
Operating expenses:				
Center operations	194,005	176,798	377,123	346,760
Advertising and marketing	9,733	9,629	22,072	20,588
General and administrative	14,496	15,713	30,360	31,069
Other operating	16,377	15,225	30,799	28,059
Depreciation and amortization	34,460	30,017	66,598	59,279
Total operating expenses	269,071	247,382	526,952	485,755
Income from operations	57,493	60,726	111,567	113,100
Other income (expense):				
Interest expense, net of interest income	(8,652)	) (6,434	) (16,503	) (12,563
Equity in earnings of affiliate	270	378	568	724
Total other expense	(8,382)	) (6,056	) (15,935	) (11,839
Income before income taxes	49,111	54,670	95,632	101,261
Provision for income taxes	19,307	21,483	37,512	39,973
Net income	\$29,804	\$33,187	\$58,120	\$61,288
Basic earnings per common share	\$0.76	\$0.80	\$1.46	\$1.48
Diluted earnings per common share	\$0.76	\$0.80	\$1.45	\$1.47
Weighted average number of common shares outstanding – basic	39,128	41,456	39,870	41,376
Weighted average number of common shares outstanding – diluted	39,255	41,659	40,123	41,644

See notes to unaudited consolidated financial statements.

LIFE TIME FITNESS, INC. AND SUBSIDIARIES
 CONSOLIDATED STATEMENTS OF COMPREHENSIVE INCOME

(In thousands)

(Unaudited)

	For the Three Months Ended		For the Six Months Ended	
	June 30, 2014	2013	June 30, 2014	2013
Net income	\$29,804	\$33,187	\$58,120	\$61,288
Other comprehensive income (loss), net of income tax:				
Foreign currency translation adjustments, net of income tax benefit of \$(337), \$738, \$272 and \$1,123, respectively	\$493	\$(1,123)	(391)	(1,707)
Unrealized gains on cash flow hedges, net of income taxes of \$(9), \$(711), \$(152) and \$(925), respectively	13	1,067	228	1,388
Other comprehensive income (loss), net of income tax:	506	(56)	(163)	(319)
Comprehensive income	\$30,310	\$33,131	\$57,957	\$60,969

See notes to unaudited consolidated financial statements.

LIFE TIME FITNESS, INC. AND SUBSIDIARIES
CONSOLIDATED STATEMENTS OF CASH FLOWS

(In thousands)

(Unaudited)

	For the Six Months Ended	
	June 30,	
	2014	2013
Cash flows from operating activities:		
Net income	\$58,120	\$61,288
Adjustments to reconcile net income to net cash provided by operating activities:		
Depreciation and amortization	66,598	59,279
Deferred income taxes	(3,715)	) 671
Gain on disposal of property and equipment, net	(459)	) (216)
Gain on land held for sale	(17)) —
Amortization of deferred financing costs	1,245	1,100
Share-based compensation	6,777	6,286
Excess tax benefit related to share-based compensation	(917)	) (4,564)
Changes in operating assets and liabilities	6,508	1,726
Other	(478)	) (1,116)
Net cash provided by operating activities	133,662	124,454
Cash flows from investing activities:		
Purchases of property and equipment	(253,411)	) (137,433)
Acquisitions, net of cash acquired	(12,400)	) (437)
Proceeds from sale of property and equipment	691	763
Proceeds from sale of land held for sale	785	—
Proceeds from property insurance settlements	—	175
Decrease (increase) in other assets	2,333	(736)
Decrease in restricted cash	262	1,640
Net cash used in investing activities	(261,740)	) (136,028)
Cash flows from financing activities:		
Proceeds from long-term borrowings	83,750	75,000
Repayments of long-term borrowings	(10,772)	) (28,272)
Proceeds from (repayments of) credit facility, net	203,400	(13,500)
Increase in deferred financing costs	(4,470)	) (976)
Excess tax benefit related to share-based compensation	917	4,564
Proceeds from stock option exercises	2,662	1,108
Proceeds from employee stock purchase plan	775	607
Stock purchased for employee stock purchase plan	(701)	) (569)
Repurchases of common stock	(139,994)	) (28,157)
Net cash provided by financing activities	135,567	9,805
Effect of exchange rates on cash and cash equivalents	27	(1,604)
Increase (decrease) in cash and cash equivalents	7,516	(3,373)
Cash and cash equivalents – beginning of period	8,334	16,499
Cash and cash equivalents – end of period	\$15,850	\$13,126
See notes to unaudited consolidated financial statements.		

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 our consolidated 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, 2013.

2. Share-Based Compensation

Stock Option and Incentive Plans

We have three share-based compensation plans: the Amended and Restated Life Time Fitness, Inc. 2004 Long-Term Incentive Plan (the "2004 Plan"); the Life Time Fitness, Inc. 2011 Long-Term Incentive Plan (the "2011 Plan") and an Employee Stock Purchase Plan (the "ESPP"), collectively, the share-based compensation plans. We no longer make grants under the 2004 Plan. There are 2,500,000 shares of common stock reserved for grant under the 2011 Plan and, as of June 30, 2014, there were 911,408 shares available for grant. The types of awards that may be granted under the 2011 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 June 30, 2014, we had granted a total of 1,929,665 options to purchase common stock under all of the share-based compensation plans, of which options to purchase 78,277 shares were outstanding and vested, and a total of 5,173,039 restricted shares were granted, of which 1,427,549 restricted shares were outstanding and unvested. We use the term "restricted shares" to define unvested shares granted to employees and non-employee directors. We use the term "vest" to define the lapse of vesting restrictions on restricted shares.

Total share-based compensation expense included in our consolidated statements of operations for the three and six months ended June 30, 2014 and 2013, was as follows:

	For the Three Months Ended		For the Six Months Ended	
	June 30, 2014	2013	June 30, 2014	2013
Share-based compensation expense related to restricted shares	\$3,461	\$3,426	\$6,717	\$6,226
Share-based compensation expense related to ESPP	30	30	60	60
Total share-based compensation expense	\$3,491	\$3,456	\$6,777	\$6,286

LIFE TIME FITNESS, INC. AND SUBSIDIARIES
 NOTES TO UNAUDITED CONSOLIDATED FINANCIAL STATEMENTS

(Table amounts in thousands, except share and per share data)

Summary of Restricted Stock Activity

	Shares	Weighted Average Grant Date Fair Value
Outstanding at December 31, 2013	1,429,730	\$44.19
Granted	432,468	\$45.07
Canceled	(109,339)	\$45.37
Vested	(325,310)	\$40.54
Outstanding at June 30, 2014	1,427,549	\$45.20

During the six months ended June 30, 2014 and 2013, we issued 432,468 and 353,956 shares of restricted stock, respectively, with an aggregate grant date fair value of \$19.5 million and \$15.0 million, respectively. The grant date fair value of restricted shares that vested during the six months ended June 30, 2014 and 2013 was \$13.2 million and \$21.3 million, respectively. The total value of each restricted stock grant, based on the fair 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 June 30, 2014, there was \$33.3 million of unrecognized compensation expense related to restricted stock that is expected to vest. We plan to recognize this amount over a weighted average period of 2.8 years.

Special 2012 Long-Term Performance-Based Restricted Stock Grant

In May, July and August 2012, the Compensation Committee of our Board of Directors approved the grant of a total of 658,500 shares of long-term performance-based restricted stock to serve as an incentive to our senior management team to achieve certain cumulative diluted earnings per share ("EPS") and return on invested capital ("ROIC") targets during performance periods that end on December 31, 2015 and December 31, 2016. On June 30, 2014, 568,500 shares remained outstanding under this grant.

The Compensation Committee set the cumulative diluted EPS targets at 1.5 times the compound annual growth rate under our then-current long range plan and the ROIC targets at 1.1 times the ROIC under our then-current long range plan. The following are the performance metrics underlying the targets:

	Cumulative Diluted EPS Measurement Period	EPS Target	ROIC Measurement Period	ROIC Target	
2015 Performance Period	4/1/2012		1/1/2015		
50% vest if we achieve both performance targets	through 12/31/2015	\$ 13.68	through 12/31/2015	8.9	%
2016 Performance Period	4/1/2012		1/1/2016		
All/remaining vest if we achieve both performance targets	through 12/31/2016	\$ 18.96	through 12/31/2016	9.0	%

A maximum of \$26.1 million could be recognized as compensation expense under this grant if all cumulative diluted EPS and ROIC targets are met. We do not believe that achievement of either the cumulative diluted EPS or the ROIC targets is currently probable, and, therefore, we have not recognized any compensation expense associated with the grant.

If it becomes probable that the cumulative diluted EPS and ROIC performance targets will be achieved, a cumulative adjustment will be recorded and the remaining compensation expense will be recognized over the remaining performance period. If all of the targets had been considered probable at June 30, 2014, we would have recognized \$13.7 million of non-cash performance share-based compensation expense during the period ended June 30, 2014. The probability of reaching the targets is evaluated each reporting period. If we later determined that

LIFE TIME FITNESS, INC. AND SUBSIDIARIES
 NOTES TO UNAUDITED CONSOLIDATED FINANCIAL STATEMENTS

(Table amounts in thousands, except share and per share data)

it is no longer probable that the minimum cumulative diluted EPS and ROIC performance targets for the grants will be met, no further compensation expense would be recognized and any previously recognized compensation expense would be reversed. In the event that we do not achieve the specified cumulative diluted EPS and ROIC targets for the performance period ending December 31, 2016, the restricted shares will be forfeited. None of these shares were included in our diluted common shares outstanding at June 30, 2014 or 2013.

Summary of Stock Option Activity

	Shares	Weighted Average Exercise Price	Weighted Average Remaining Contractual Term (Years)	Aggregate Intrinsic Value
Outstanding at December 31, 2013	215,668	\$25.64	1.1	\$4,616
Exercised	(132,352)	) \$20.12		
Canceled	(5,039)	) \$44.66		
Outstanding at June 30, 2014	78,277	\$33.76	1.2	\$1,208
Vested at June 30, 2014	78,277	\$33.76	1.2	\$1,208

No stock options have been granted since 2007. As of June 30, 2014, there was no unrecognized compensation expense related to stock options.

The aggregate intrinsic values in the table above represent the total pretax intrinsic values (the differences between our closing stock price 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 that date. This amount changes based on the fair market value of our stock. Total intrinsic value of options exercised during the six months ended June 30, 2014 and 2013 was \$3.7 million and \$1.1 million, respectively.

Our net cash proceeds from the exercise of stock options were \$2.7 million and \$1.1 million for the six months ended June 30, 2014 and 2013, respectively. The excess income tax benefit realized from stock option exercises and restricted stock vesting was \$0.9 million and \$4.6 million, respectively, for those same periods. In accordance with the related accounting guidance, this tax benefit is presented as a financing cash inflow. There is a corresponding cash outflow included in cash flows from operating activities.

Employee Stock Purchase Plan

Our ESPP provides for the sale of up to 1,500,000 shares 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, 2014 and ends December 31, 2014. Compensation expense under the ESPP is estimated based on the discount of 10% at the end of the purchase period. During the six months ended June 30, 2014, \$0.8 million was withheld from employees for the purpose of purchasing shares under the ESPP. There were 1,245,581 shares of common stock available for purchase under the ESPP as of June 30, 2014.

Share Repurchase Plans

In June 2006, our Board of Directors authorized the repurchase of up to 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 issued under our ESPP. During the six months ended June 30, 2014, we repurchased 15,146 shares under this authorization for approximately \$0.7 million. As of June 30, 2014, there were 245,581 remaining shares authorized to be repurchased for this purpose.

In August 2013, our Board of Directors authorized the repurchase of up to \$200.0 million of our outstanding common stock from time to time through open market or privately negotiated transactions. The authorization to repurchase shares terminates when the aggregate repurchase amount totals \$200.0 million or at the close of business on August

16, 2015, whichever occurs first. The share repurchase program does not obligate us to repurchase any

LIFE TIME FITNESS, INC. AND SUBSIDIARIES
 NOTES TO UNAUDITED CONSOLIDATED FINANCIAL STATEMENTS

(Table amounts in thousands, except share and per share data)

dollar amount or number of shares of our common stock and the program may be extended, modified, suspended or discontinued at any time. During the six months ended June 30, 2014, we repurchased 2,910,946 shares under this program for approximately \$140.0 million. As of June 30, 2014, \$29.0 million remained authorized under this program.

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 year. Diluted EPS is computed similarly to basic EPS, except that the denominator is increased for the conversion of any dilutive common stock equivalents, the assumed exercise of dilutive stock options using the treasury stock method and unvested restricted stock awards using the treasury stock method. Stock options excluded from the calculation of diluted EPS because the option exercise price was greater than the average market price of the common share were 2,477 and 2,477 for the three months ended June 30, 2014 and 2013, respectively and 2,477 and 15,540 for the six months ended June 30, 2014 and 2013, respectively.

The basic and diluted EPS calculations are shown below:

	For the Three Months Ended		For the Six Months Ended	
	June 30, 2014	2013	June 30, 2014	2013
Net income	\$29,804	\$33,187	\$58,120	\$61,288
Weighted average number of common shares outstanding – basic	39,128	41,456	39,870	41,376
Effect of dilutive stock options	22	94	16	91
Effect of dilutive restricted stock awards	105	109	237	177
Weighted average number of common shares outstanding – diluted	39,255	41,659	40,123	41,644
Basic earnings per common share	\$0.76	\$0.80	\$1.46	\$1.48
Diluted earnings per common share	\$0.76	\$0.80	\$1.45	\$1.47

4. Operating Segment

Our operations are conducted mainly through our distinctive and large, multi-use sports and athletic, professional fitness, family recreation and spa centers in a resort-like environment. We aggregate the activities of our centers and other ancillary products and services into one reportable segment. Each of the centers has similar economic characteristics, services, product offerings and customers, and in-center revenues are derived primarily from services to our members. 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 as the primary measure of operating segment performance. Our chief operating decision maker is our Chief Executive Officer.

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 six months ended June 30, 2014 and 2013:

	For the Three Months Ended		For the Six Months Ended	
	June 30, 2014	2013	June 30, 2014	2013
Membership dues	\$205,164	\$194,816	\$401,979	\$381,190
Enrollment fees	3,019	3,573	6,142	6,969
Personal training	49,664	46,794	98,548	92,808
Other in-center revenue	54,695	50,481	104,216	96,438
Total center revenue	312,542	295,664	610,885	577,405
Other revenue	14,022	12,444		