BURLINGTON COAT FACTORY WAREHOUSE CORP
Form 10-Q
April 06, 2006

FORM 10-Q

SECURITIES AND EXCHANGE COMMISSION
Washington, D.C. 20549

(MARK ONE)

[X] QUARTERLY REPORT UNDER SECTION 13 OR 15 (d)
OF THE SECURITIES EXCHANGE ACT OF 1934
For the quarterly period ended February 25, 2006

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. 1-8739
Burlington Coat Factory Warehouse Corporation

(Exact name of registrant as specified in its charter)

Delaware	22-1970303
(State or other jurisdiction of incorporation or organization)	(I.R.S. Employer Identification Number)
1830 Route 130 Burlington, New Jersey	08016
(Address of principal executive offices)	(Zip Code)

Registrant's telephone number, including area code (609) 387-7800

Indicate by check mark whether the Registrant (1) has filed all reports required 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 _____

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 o Accelerated filer x Non-accelerated filer o

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

Indicate the number of shares outstanding of each of the issuer's classes of common stock, as of the latest practicable date.

Class	Outstanding at March 8, 2006
Common stock, par value $1.00	44,770,813

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BURLINGTON COAT FACTORY WAREHOUSE CORPORATION
AND SUBSIDIARIES

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PART I - FINANCIAL INFORMATION

Item 1. Financial Statements

BURLINGTON COAT FACTORY WAREHOUSE CORPORATION
AND SUBSIDIARIES
CONDENSED CONSOLIDATED BALANCE SHEETS (unaudited)
(All amounts in thousands)

	February 25, 2006	May 28, 2005
ASSETS		
Current Assets:		
Cash and Cash Equivalents	$ 82,213	$ 47,953
Restricted Cash and Cash Equivalents	13,822	14,957
Investments	167,154	134,664
Accounts Receivable, Net	26,841	24,841
Merchandise Inventories	709,762	720,882
Deferred Tax Assets	23,135	22,187
Prepaid and Other Current Assets	18,203	18,891

Total Current Assets	1,041,130	984,375
Property and Equipment (Net of Accumulated Depreciation)	607,498	621,773
Investments	-	27
Intangible Assets (Net of Accumulated Amortization)	47,246	48,785
Deferred Tax Assets	19,886	16,554
Other Assets	2,066	1,754
Total Assets	$1,717,826	$1,673,268
LIABILITIES AND STOCKHOLDERS' EQUITY		
Current Liabilities:		
Accounts Payable	$ 413,212	$ 390,891
Income Taxes Payable	23,514	5,708
Other Current Liabilities	197,037	179,346
Current Maturities of Long Term Debt and Obligations Under Capital Leases	1,353	1,190
Total Current Liabilities	635,116	577,135
Long Term Debt and Obligations Under Capital Leases	31,575	132,347
Other Liabilities	38,928	37,633
Commitments and Contingencies	-	-
Stockholders' Equity:		
Preferred Stock	-	-
Common Stock	49,895	49,898
Capital in Excess of Par Value	24,838	24,776
Retained Earnings	996,161	910,176

Accumulated Other Comprehensive Income	-	4
Note Receivable from Stock Options Exercised	(27)	(41)
Treasury Stock at Cost	(58,660)	(58,660)
Total Stockholders' Equity	1,012,207	926,153
Total Liabilities and Stockholders' Equity	$1,717,826	$1,673,268

See notes to the condensed consolidated financial statements.

BURLINGTON COAT FACTORY WAREHOUSE CORPORATION
AND SUBSIDIARIES
CONDENSED CONSOLIDATED STATEMENT OF OPERATIONS (unaudited)
(All amounts in thousands, except share data)

	Nine Months Ended		Three Months Ended	
	February 25, 2006	February 26, 2005	February 25, 2006	February 26, 2005
REVENUES:				
Net Sales	$2,619,919	$2,414,314	$1,023,662	$968,109
Other Revenue	24,209	21,832	8,368	7,512
	2,644,128	2,436,146	1,032,030	975,621
COSTS AND EXPENSES:				
Cost of Sales (Exclusive of Depreciation)	1,663,396	1,523,138	649,340	611,010
Selling and Administrative Expenses	766,813	704,320	267,562	236,823
Depreciation	67,979	64,797	22,916	20,625
Interest Expense	3,851	5,352	683	1,780
Other (Income), Net	(1,100)	(9,001)	(3,592)	(3,406)
	2,500,939	2,288,606	936,909	866,832

Income From Continuing Operations Before Provision for Income Taxes	143,189	147,540	95,121	108,789
Provision for Income Taxes	55,413	57,370	36,811	42,674
Income from Continuing Operations	87,776	90,170	58,310	66,115
(Loss) Income from Discontinued Operations, Net of Tax	-	(439)		603
Net Income	87,776	89,731	58,310	66,718
Net Unrealized Gain on Non-Marketable Securities, Net of Tax	-	1	-	-
Total Comprehensive Income	$ 87,776	$ 89,732	$ 58,310	$ 66,718
Basic Earnings Per Share:				
Basic Income Per Share from Continuing Operations	$ 1.96	$ 2.02	$ 1.30	$ 1.48
Basic (Loss) Income Per Share from Discontinued Operations	-	(0.01)	-	0.01
Basic Net Income Per Share	$ 1.96	$ 2.01	$ 1.30	$ 1.49
Diluted Earnings Per Share:				
Diluted Income Per Share from Continuing Operations	$ 1.95	$ 2.02	$ 1.30	$ 1.48
Diluted (Loss) Income Per Share from Discontinued Operations	-	(0.01)	-	0.01
Diluted Net Income Per Share	$ 1.95	$ 2.01	$ 1.30	$ 1.49
Basic Weighted Average Shares Outstanding	44,773,689	44,653,779	44,774,850	44,679,699
Diluted Weighted Average Shares Outstanding	44,957,085	44,750,045	44,965,772	44,787,991
Dividends Per Share	$ 0.04	$ 0.60	$ -	$ 0.56

See notes to the condensed consolidated financial statements .

BURLINGTON COAT FACTORY WAREHOUSE CORPORATION
AND SUBSIDIARIES
CONDENSED CONSOLIDATED STATEMENT OF CASH FLOWS
(unaudited)
(All amounts in thousands)

	Nine Months Ended	
	February 25, 2006	February 26, 2005
OPERATING ACTIVITIES		
Net Income	$ 87,776	$ 89,731
Loss from Discontinued Operations, Net of Tax	-	439
Income from Continuing Operations	87,776	90,170
Adjustments to Reconcile Net Income from Continuing Operations to Net Cash Provided by Operating Activities:		
Depreciation	67,979	64,797
Provision for Losses on Accounts Receivable	3,448	5,816
Provision for Deferred Income Taxes	(4,280)	311
Loss (Gain) on Disposition of Fixed Assets and Leasehold Purchases	2,645	(953)
Non-Cash Rent Expense and Other	3,774	567
Changes in Operating Assets and Liabilities:		
Investments	(32,490)	(4,614)
Accounts Receivable	(5,406)	(6,895)
Merchandise Inventories	11,120	(104,549)
Prepaids and Other Current Assets	4,510	(166)
Accounts Payable	22,321	83,293
Other Current Liabilities and Income Taxes Payable	38,803	19,085
Net Cash Provided by Continuing Operations	200,200	146,862
Net Cash Used in Discontinued Operations	-	(1,182
	)	
Net Cash Provided by Operating Activities	200,200	145,680
INVESTING ACTIVITIES		

Cash Paid for Property and Equipment	(64,759)	(76,135)
Proceeds from Sale of Fixed Assets and Leaseholds	687	4,508
Lease Acquisition Costs	(635)	(4,225)
Receipts Against Long Term Notes Receivable	-	35
Issuance of Notes Receivable	(46)	-
Decrease (Increase) in Restricted Cash and Cash Equivalents	1,135	(1,092)
Minority Interest	20	(210)
Net Cash Used in Investing Activities	(63,598)	(77,119)
FINANCING ACTIVITIES		
Proceeds from Long-Term Debt	470	-
Principal Payments on Long Term Debt	(101,080)	(937)
Issuance of Common Stock Upon Exercise of Stock Options	59	1,404
Treasury Stock Transactions	-	598
Payment of Dividends	(1,791)	(26,783)
Net Cash (Used in) Financing Activities	(102,342)	(25,718)
Increase in Cash and Cash Equivalents	34,260	42,843
Cash and Cash Equivalents at Beginning of Period	47,953	29,817
Cash and Cash Equivalents at End of Period	$ 82,213	$ 72,660
Interest Paid:	$ 4,528	$ 4,158
Income Taxes Paid:	$ 41,887	$ 45,166
Non-Cash Investing Activities:		
Accrued Purchases of Property and Equipment	$ 3,901	$ 2,183

See notes to the condensed consolidated financial statements.

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BURLINGTON COAT FACTORY WAREHOUSE CORPORATION AND SUBSIDIARIES
NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS
NINE AND THREE MONTHS ENDED FEBRUARY 25, 2006 AND
FEBRUARY 26, 2005 (UNAUDITED)

1. The condensed consolidated financial statements include the accounts of Burlington Coat Factory Warehouse Corporation and all its subsidiaries in which it has the controlling financial interest through direct ownership of a majority voting interest or a controlling managerial interest ("the Company"). All subsidiaries are wholly owned except two. The Company maintains a ninety percent interest and a seventy-five percent interest, respectively, in two investments. These investments are consolidated net of their minority interests. All significant intercompany accounts and transactions have been eliminated. Previously, the Company had maintained a fifty percent interest in a third investment in a partnership in which it maintained managerial and financial control. During the third quarter of fiscal 2005, the partnership was dissolved and all assets were distributed to the partners. The accompanying financial statements are unaudited, but in the opinion of management reflect all adjustments (which are of a normal and recurring nature) necessary for a fair presentation of the results of operations for the interim periods. The balance sheet at May 28, 2005 has been derived from the audited financial statements in the Company's Annual Report on Form 10-K for the fiscal year ended May 28, 2005. Because the Company's business is seasonal in nature, the operating results for the nine and three months ended February 25, 2006 and the corresponding periods ended February 26, 2005 are not necessarily indicative of results for the fiscal year.

2. Certain information and footnote disclosures normally included in financial statements prepared in accordance with accounting principles generally accepted in the United States of America have been condensed or omitted. It is suggested that these condensed consolidated financial statements be read in conjunction with the financial statements and notes thereto included in the Company's Annual Report on Form 10-K for the fiscal year ended May 28, 2005.

3. Restricted cash and cash equivalents consist of $11.4 million pledged as collateral for certain insurance contracts and $2.4 million contractually restricted and related to the acquisition and maintenance of a building related to a store operated by the Company.

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4.Merchandise inventories as of February 25, 2006 and May 28, 2005 are valued at the lower of cost, on a First In First Out (FIFO) basis, or market, as determined by the retail inventory method. The Company records its cost of merchandise (net of purchase discounts and certain vendor allowances), certain merchandise acquisition costs (primarily commissions and import fees), inbound freight, warehouse outbound freight, and freight on internally transferred merchandise in the line item "Cost of Sales" in the Company's Condensed Consolidated Statement of Operations. Costs associated with the Company's warehousing, distribution, buying, and store receiving functions are included in the line items "Selling and Administrative Expenses" and "Depreciation" in the Companys Condensed Consolidated Statement of Operations. Warehousing and purchasing costs included in Selling and Administrative Expenses amounted to $36.8 million and $12.2 million for the nine and three months ended February 25, 2006, respectively, and $33.9 million and $11.4 million for the comparative periods of fiscal 2005. Depreciation related to the warehousing and purchasing functions amounted to $6.2 million and $2.0 million for the nine and three month periods ended February 25, 2006, respectively, and $6.6 million and $2.2 million for the comparative periods of fiscal 2005. Also included in Selling and Administrative Expenses are payroll and payroll related expenses, occupancy related expenses, advertising expenses, store operating expenses and corporate overhead expenses. The Company also establishes reserves for inventory levels based on historical analysis of product sales and current market conditions. The reserves are revised, if necessary, on a quarterly basis for adequacy. The Company's reserves against inventory, at cost, were $17.1 million and $15.0 million as of February 25, 2006 and May 28, 2005, respectively.

5. The Company classifies its investments in debt and equity securities into held-to-maturity, available-for-sale or trading categories in accordance with the provisions of Statement of Financial Accounting Standards ("SFAS") No. 115, *Accounting For Certain Investments in Debt and Equity Securities.* Debt securities are classified as held-to-maturity when the Company has the positive intent and ability to hold the securities to maturity. Held-to-maturity securities are stated at amortized cost. Securities that the Company intends to sell in the near term are classified as trading securities and are carried at fair market value, with unrealized gains and losses included in net income. Investments not classified as held-to-maturity or trading securities are classified as available-for-sale and are carried at fair market value, with unrealized gains and losses, net of tax, reported as a separate component of stockholders' equity. During the three month period ended February 25, 2006, investment securities previously classified as available-for-sale were reclassified as trading securities as the Company intends to sell these securities within the next two months. At the balance sheet dates presented, investments consisted of (in thousands):

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February 25, 2006

	Cost	Unrealized Gains (Losses)	Fair Market Value
Trading Securities (Current):			
Short Term Municipal Bond Fund	$166,460	$ -	$166,460
Equity Investments	664	30	694
	$167,124	$30	$167,154

May 28, 2005

	Cost	Unrealized Gains (Losses)	Fair Market Value
Trading Securities (Current):			
Short Term Municipal Bond Investments	$134,772	($ 108)	$134,664
Available-for-Sale Investments (Long Term):			
Equity Investments	$ 23	$ 4	$ 27

6. The Company records revenue at the time of sale and delivery of merchandise. The Company records revenue net of allowances for estimated future returns. The Company accounts for layaway sales and leased department revenue in compliance with Staff Accounting Bulletin ("SAB") No. 101, *Revenue Recognition in Financial Statements.* Layaway sales are recognized upon delivery of merchandise to the customer. The amount of cash received upon initiation of the layaway is recorded as a deposit liability within other current liabilities. Gift cards are recorded as a liability at the time of issuance, and upon redemption the related sale is recorded.

7. Other (Income) Loss, Net consists of investment income, gains (losses) from disposition of fixed assets and other miscellaneous income (loss) items. Losses from disposition of fixed assets amounted to $2.6 million and $0.5 million for the nine and three month periods ended February 25, 2006, respectively. For the comparative nine and three month periods ended February 26, 2005, the Company realized net gains on dispositions of fixed assets of $1.0 million and $1.6 million, respectively. During fiscal 2006, losses from dispositions of fixed assets were offset in part by increases in investment income during the nine and three month periods compared with the comparative periods ended February 26, 2005. Interest income increased $3.0 million to $5.9 million and $1.4 million to $3.1 million for the nine and

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three month periods ended February 25, 2006, respectively. The Company recorded miscellaneous losses of $3.5 million during the second quarter of fiscal 2006 related to the write-off of the net book value of assets damaged during Hurricanes Katrina and Wilma (see note 33 in the notes to the condensed consolidated financial statements). During the nine month period ended February 26, 2005, the Company recorded miscellaneous income of $4.2 million in settlement of claims the Company had filed in the bankruptcy proceeding of K-Mart Corporation in connection with the rejection by K-Mart of leases for four locations that had been subleased to the Company. During the third quarter of fiscal 2006, the Company recorded an additional $0.6 million in miscellaneous income related to the settlement of these claims.

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8. As of February 25, 2006, the Company had a current deferred tax asset of $23.1 million and a non-current deferred tax asset, net of valuation allowances, of $19.9 million. As of May 28, 2005, the Company had a current deferred tax asset of $22.2 million and a non-current deferred tax asset of $16.6 million. Income taxes are provided on an interim basis based upon the Company's estimate of the effective annual income tax rate. The Company is in the process of restructuring the corporate structure of its subsidiaries as it relates to state operations. The Company expects to substantially complete the restructuring in April 2006. The impact of the restructuring on the Company's net operating losses and its valuation allowances has not yet been determined.

As of February 25, 2006 and May 28, 2005, valuation allowances amounted to $10.6 million and related primarily to state tax net operating losses. The Company believes it is unlikely that it will be able to utilize the benefit of these losses in the future. Current deferred tax assets consisted primarily of certain operating costs, provisions for uncollectible receivables, and certain inventory related costs not currently deductible for tax purposes. Non-current deferred tax assets primarily reflected rent expense and pre-opening costs not currently deductible for tax purposes.

9. The Company accounts for intangible assets in compliance with SFAS No. 142, *Goodwill and Other Intangible Assets*. The Company's intangible assets primarily represent costs incurred to acquire long term store leases. These leasehold purchases are recorded at cost, which approximates fair value, and, in accordance with SFAS No. 142, are amortized over the minimum lease term, including option periods where the exercise of the option period can be reasonably assured, which approximates the leasehold's useful life. Amortization of intangibles is included in Selling and Administrative Expenses in the Company's Condensed Consolidated Statement of Operations. Intangible assets as of February 25, 2006 and May 28, 2005 are as follows (in thousands):

	February 25, 2006			May 28, 2005		
	Gross Carrying Amount	Accumulated Amortization	Net Amount	Gross Carrying Amount	Accumulated Amortization	Net Amount
Leasehold Purchases	$63,879	$16,770	$47,109	$63,245	$15,087	$48,158
Other	463	326	137	1,042	415	627
	$64,342	$17,096	$47,246	$64,287	$15,502	$48,785

Amortization expense amounted to $3.1 million and $0.8 million for the nine and three months ended February 25, 2006, respectively, compared with $3.2 million and $0.9 million for the nine and three months ended February 26, 2005, respectively. Amortization expense for each of the next five fiscal years is estimated to be as follows: fiscal 2007 - $3.7 million; fiscal 2008 - $3.7 million; fiscal 2009 - $3.7 million; fiscal 2010 - $3.5 million; and fiscal 2011 - $3.4 million. Amortization for the remainder of fiscal 2006 is expected to be approximately $1.0 million.

10. Other assets consist primarily of notes receivable and the net accumulation of excess rent income, accounted for on a straight line basis, over actual rental income receipts.

11. Other current liabilities primarily consists of sales tax payable, unredeemed store credits and gift certificates, accrued payroll costs, accrued insurance costs, accrued operating expenses, layaway deposits, payroll taxes payable, current portion of deferred rents and other miscellaneous items.

12. Other liabilities primarily consist of deferred lease incentives, the net accumulation of excess straight line rent expense over actual rental expenditures, and minority interest in investments. Deferred lease incentives are funds received from landlords used primarily to offset the costs of store remodelings. These deferred lease incentives are amortized over the expected lease term including rent holiday periods and option periods where the exercise of the option can be reasonably assured. Minority interest in the two consolidated investments, which are not wholly owned by the Company, amounted to $0.7 million and $0.7 million at February 25, 2006 and May 28, 2005, respectively.

13. The Company establishes reserves to cover contractual lease payments and other ancillary costs associated with store closings that extend beyond the store's closing date. Established reserves by fiscal year and related payments are as follows (in millions):

	Fiscal Year 2003	Fiscal Year 2004	Fiscal Year 2005	Fiscal Year 2006 (nine months)	Total Reserve as of February 25, 2006
Reserves Established	$0.4	$1.5	$0.3	$0.6	
Payments Applied to Reserve					

Fiscal 2004	(0.1)	(0.4)	-	-	
Fiscal 2005	(0.2)	(0.6)	-	-	
Fiscal 2006 (nine months)	(0.1)	(0.1)	(0.3)	(0.2)	
	$ -	$0.4	$ -	$0.4	$0.8

The Company believes that these reserves are adequate to cover the expected contractual lease payments and other ancillary costs associated with these closings.

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14. Long-term debt consists of (in thousands):

	February 25, 2006	May 28, 2005
Promissory Notes, 4.38% due in monthly payments of $8 through December 23, 2011	$ 465	$ -
Senior Notes, 4.06% due in annual payments of various amounts from September 30, 2006 to September 30, 2010	-	36,000
Senior Notes, 4.67% due in annual payments of various amounts from September 30, 2007 to September 30, 2013	-	64,000
Industrial Revenue Bonds, 6.0% due in semi-annual payments of various amounts from September 1, 2004 to September 1, 2010	5,000	5,735
Promissory Note, non-interest bearing, due in monthly payments of $17 through January 1, 2012	1,183	1,333
Capital Lease Obligations	26,280	26,469
Subtotal	32,928	133,537
Less Current Portion	(1,353)	(1,190)
Long-Term Debt and Obligations Under Capital Leases	$ 31,575	$132,347

On November 2, 2005, the Company prepaid in full $100 million of the Company's senior notes without any prepayment premium. The Company used existing unrestricted cash generated from operating activities, as well as cash from the sale of short-term investments, to pay off the senior notes. The Company did not borrow any amounts in order to pay off the senior notes. In connection with the prepayment of the senior notes, the Company wrote off approximately $0.5 million in unamortized deferred debt charges during the second quarter of fiscal 2006, which was recorded in Selling and Administrative Expenses on the Company's Condensed Consolidated Statement of Operations.

In January 2006, the Company purchased the groundlease and sublease related to one of its store locations. The Company financed this purchase partially through the issuance of a promissory note in the principal amount of $0.5 million. The note bears interest at 4.38% per annum and matures on December 23, 2011. The loan evidenced by the note is to be repaid in equal monthly installments of $7,539 which began on February 23, 2006.

15. During the second quarter of fiscal 2006, the Company entered into a death benefit agreement with three of its executive officers, Andrew R. Milstein, Stephen E. Milstein and Mark A. Nesci. Each of Andrew R. Milstein and Stephen E. Milstein beneficially own more than 5% of the outstanding shares of the Company's common stock. In addition, Andrew R. Milstein and Stephen E. Milstein are parties to a Voting Agreement, pursuant to which the other parties thereto have granted Andrew R. Milstein and Stephen E. Milstein an irrevocable proxy to vote the shares of Common Stock owned by such parties. The shares of Common Stock subject to the Voting Agreement represent a majority interest of the issued and outstanding shares of Common Stock of the Company. The agreement provides that, subject to certain conditions set forth in the agreement, the Company will pay a death benefit of $1,000,000 to the executive's estate or designated beneficiary after the death of the executive. The Company recorded, in Selling and Administrative Expenses on its Condensed Consolidated Statement of Operations, $0.6 million of expense related to these agreements during the nine month period ended February 25, 2006 using the net present value of the expected benefit payouts based on the executives' life expectancies.

16. On November 14, 2005, the Board of Directors of the Company declared a cash dividend in the amount of four cents ($0.04) per share payable on January 9, 2006 to stockholders of record on November 28, 2005. The paid dividend amounted to $1.8 million.

17. The Company presents comprehensive income as a component of stockholders' equity in accordance with SFAS No. 130, *Reporting Comprehensive Income.* For the nine and three months ended February 26, 2005, comprehensive income consisted of net income and net unrealized gains (loss) on available-for-sale investments. During the three month period ended February 25, 2006, investment securities previously classified as available-for-sale were reclassified as trading securities. The related unrealized gains on these securities were recognized in net income during the three months ended February 25, 2006.

18. The Company has one reportable segment, which operates within the United States. Sales by major product categories are as follows (in thousands):

	Nine months Ended		Three Months Ended	
	February 25, 2006	February 26, 2005	February 25, 2006	February 26, 2005
Apparel	$2,102,335	$1,928,039	$835,615	$790,255
Home Products	517,584	486,275	188,047	177,854

$2,619,919	$2,414,314	$1,023,662	$968,109

Apparel includes all clothing items for men, women and children and apparel accessories, such as jewelry, perfumes and watches. Home Products includes linens, home furnishings, gifts, baby furniture and baby furnishings.

19. Other Revenue consists of rental income received from leased departments, subleased rental income, layaway and alteration service charges and other miscellaneous items. Layaway and alteration service fees amounted to $6.6 million and $1.3 million for the nine and three month periods ended February 25, 2006 compared with $6.5 million and $1.3 million in the comparative periods of the prior year. Rental income from leased departments amounted to $8.7 million and $3.8 million for the nine and three month periods ended February 25, 2006, respectively, compared with $7.2 million and $2.9 million in the comparative periods of fiscal 2005. Subleased rental income and other miscellaneous revenue items amounted to $8.9 million and $3.2 million for the nine and three month periods ended February 25, 2006, respectively. Subleased rental income and other miscellaneous revenue items were $8.2 million and $3.2 million for the comparative periods of fiscal 2005.

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20. Rebates and allowances received from vendors are accounted for in compliance with Emerging Issues Task Force ("EITF") Issue No. 02-16, *Accounting by a Customer (including a Reseller) for Certain Consideration Received from a Vendor*. EITF Issue No. 02-16 specifically addresses whether a reseller should account for cash consideration received from a vendor as an adjustment of cost of sales, revenue, or as a reduction to a cost incurred by the reseller. Rebates and allowances received from vendors that are dependent on purchases of inventories are recognized as a reduction of cost of goods sold when the related inventory is sold or marked down. Rebates and allowances that are reimbursements of specific expenses are recognized as a reduction of selling and administrative expenses when earned, up to the amount of the incurred cost. Any vendor reimbursement in excess of the related incurred cost is recorded as a reduction of cost of sales. Rebates and allowances that were reimbursements of specific expenses, which were recognized as a reduction of selling and administrative expenses, amounted to $0.7 million and $0.2 million for the nine and three month periods ended February 25, 2006, respectively. Reimbursement of expenses for the nine and three month periods ended February 26, 2005 amounted to $0.6 million and $0.2 million, respectively.

21. In March 1998, the American Institute of Certified Public Accountants ("AICPA") issued Statement of Position ("SOP") 98-1, *Accounting For the Costs of Computer Software Developed For or Obtained for Internal-Use*. The SOP requires the capitalization of certain costs incurred in connection with developing or obtaining software for internal use. The Company capitalized $3.6 million and $1.0 million relating to these costs during the nine and three month periods ended February 25, 2006, respectively. For the comparative nine and three month periods of fiscal 2005, the Company capitalized $2.4 million

and $1.1 million, respectively.

22. SFAS No. 123, Accounting for Stock Based Compensation, as amended by SFAS No. 148, Accounting for Stock Based Compensation - Transition and Disclosure, an Amendment of FASB Statement No. 123, encourages, but does not require companies to record compensation cost for stock-based employee compensation plans at fair value. The Company has chosen to continue to account for stock-based compensation using the intrinsic method prescribed in Accounting Principles Board ("APB") Opinion No. 25, Accounting for Stock Issued to Employees, and related interpretations. Accordingly, compensation cost for stock options is measured as the excess, if any, of the quoted market price of the Company's stock at the date of the grant over the amount an employee must pay to acquire the stock. The Company issued options to purchase 161,300 shares of common stock during fiscal 2005. No compensation expense was recorded during the nine and three month periods ending February 26, 2005 because the quoted market price of the Company's stock at the date of the grant did not exceed the amount grantees must pay to acquire the stock. The Company did not issue, and there was no compensation expense related to, the issuance of any stock options during the nine and three month periods ended February 25, 2006. The following table illustrates the effect on net income and net income per share for the nine and three month periods ended February 25, 2006 and February 26, 2005 if the Company had applied the fair value recognition provisions of SFAS No. 123 (in thousands, except per share data):

	Nine months Ended February 25, 2006	Nine months Ended February 26, 2005	Three Months Ended February 25, 2006	Three Months Ended February 26, 2005
Net income as reported	$87,776	$89,731	$58,310	$66,718
Expense under fair value method, net of tax effect	(388)	(214)	(52)	(121)
Pro forma net income	$87,388	$89,517	$58,258	$66,597
Income per share:				
Basic - as reported	$1.96	$2.01	$1.30	$1.49
Diluted - as reported	$1.95	$2.01	$1.30	$1.49
Basic - pro forma	$1.95	$2.00	$1.30	$1.49

Diluted - pro forma	$1.94	$2.00	$1.30	$1.49

The fair value of each stock option granted is estimated on the date of grant using the Black-Scholes option pricing model with the following weighted average assumptions used for grants in fiscal 2005:

	Options Granted September 2004	Options Granted January 2005
Number of Shares	87,700	73,600
Risk-free interest rate	4.10%	4.10%
Expected volatility	37.65%	38.00%
Expected life	5.5 years	5.5 years
Contractual life	10 years	10 years
Expected dividend yield	0.20%	0.20%
Fair value of options granted	$6.79	$9.85

23. The Company accounts for impaired long-lived assets in accordance with SFAS No. 144, *Accounting for the Impairment or Disposal of Long-Lived Assets*. This statement requires that long-lived assets and certain identifiable intangibles to be held and used by an entity be reviewed for impairment whenever events or changes in circumstances indicate that the carrying amount of an asset may not be recoverable. Also, in general, long-lived assets and certain intangibles to be disposed of should be reported at the lower of the carrying amount or fair value less cost to sell. The Company considers historical performance and future estimated results in its evaluation of potential impairment and then compares the carrying amount of the asset to the estimated future cash flows expected to result from the use of the asset. If the carrying amount of the asset exceeds the estimated expected undiscounted future cash flows, the Company measures the amount of the impairment by comparing the carrying amount of the asset to its fair value. The estimation of fair value is generally measured by discounting expected future cash flows at the rate the Company utilizes to evaluate potential

investments. During the nine month period ended February 25, 2006, the Company incurred impairment charges of $1.3 million. There were no impairment charges recorded during the three month period ended February 25, 2006. These impairment charges do not include any asset write-downs related to the stores impacted by Hurricanes Katrina or Wilma that are described in note 33.

24. The Company continuously monitors and evaluates store profitability. Based upon these evaluations, the decision to permanently close a store or to relocate a store within its same trading market is made. The only stores included in the Company's calculation of discontinued operations are permanently closed stores where sales by another store will not absorb a significant amount of the closed store's sales. In accordance with SFAS No. 144, the Company's discontinued operations reflect the operating results for the three stores and one investment closed during fiscal 2005.

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	Nine Months Ended (all amounts in thousands)		Three Months Ended (all amounts in thousands)	
	February 25, 2006	February 26, 2005	February 25, 2006	February 26, 2005
Revenues	-	$9,984	-	$3,583

Gross Margin	-	3,049	-	1,277
Selling and Administrative Expenses	-	3,367	-	484
Depreciation	-	301	-	89
Income (Loss) from Discontinued Operations Before Income Tax Provision (Benefit)	-	(198)	-	764
Income (Loss) from Discontinued Operations, Net of Tax	-	($439)	-	$603

25. The Company's net advertising costs consist primarily of newspaper and television costs. The production costs of net advertising are charged to expenses as incurred. Net advertising expenses for the nine and three month periods ended February 25, 2006 were $55.1 million and $17.9 million, respectively. For the comparative periods of last year, net advertising costs were $47.8 million and $12.8 million, respectively. The Company nets certain cooperative advertising reimbursements received from vendors against specific, incremental, identifiable costs incurred in connection with selling the vendors' products. Any excess reimbursement is characterized as a reduction of inventory and is recognized as a reduction to cost of sales as inventories are sold. Vendor rebates netted against advertising expense were $0.8 million and $0.4 million for the nine and three months ended February 26, 2005, respectively. For the nine and three months ended February 26, 2005, vendor rebates amounted to $0.8 million and $0.4 million, respectively.

26. Basic and diluted income per share is based on the weighted average number of shares outstanding during each period. The amounts used in the calculation of basic and diluted income per share are as follows (in thousands):

	Nine Months Ended February 25, 2006			Nine Months Ended February 26, 2005		
	Income	Shares	Per Share	Income	Shares	Per Share
Basic Income Per Share:						
Income from Continuing Operations	$87,776	44,774	$1.96	$90,170	44,654	$2.02
Dilutive Effect of Stock Options	-					