

STEAK & SHAKE CO  
Form 10-K  
December 11, 2006

UNITED STATES  
SECURITIES AND EXCHANGE COMMISSION  
Washington, D. C. 20549

FORM 10-K

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

For the fiscal year ended September 27, 2006

Commission file number 0-8445

THE STEAK N SHAKE COMPANY  
(Exact name of registrant as specified in its charter)

INDIANA (State or other jurisdiction of incorporation or organization)	37-0684070 (I.R.S. Employer Identification No.)
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36 S. Pennsylvania Street, Suite 500  
Indianapolis, Indiana 46204  
(317) 633-4100  
(Address and telephone number  
of registrant's principal executive offices)  
Securities registered pursuant to Sec. 12(b) of the Act:

Title of Each Class	Name of Exchange on Which Registered
Common Stock, stated value \$.50 per share	New York Stock Exchange

Securities registered pursuant to Sec. 12(g) of the Act: None.

Indicate by check mark if the registrant is a well-known seasoned issuer, as defined in Rule 405 of the Securities Act.  
Yes  No

Indicate by check mark if the registrant is not required to file reports pursuant to Section 13 or Section 15(d) of the Act. Yes  No

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 if disclosure of delinquent filers pursuant to Rule 405 of Regulation S-K is not contained herein, and will not be contained, to the best of registrant's knowledge, in definitive proxy or information statements incorporated by reference in Part III of this Form 10-K or any amendment to this Form 10-K.

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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).

Large accelerated filer  Accelerated Filer  Non Accelerated filer

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

The aggregate market value of Common Stock held by persons not "affiliated" with the registrant, based on the closing price of the Common Stock at April 12, 2006, was approximately \$445,658,513 based on the closing stock price of \$17.03 per share on that day.

The number of shares of Common Stock outstanding at December 4, 2006 was 28,203,032.

DOCUMENTS INCORPORATED BY REFERENCE

Portions of the Proxy Statement for the 2007 Annual Meeting of Shareholders of Registrant are incorporated by reference into Part III.

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Form 10-K  
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## **PART I.**

### **ITEM 1. BUSINESS**

#### *General*

The Steak n Shake Company ("Steak n Shake" or the "Company") is engaged primarily in the ownership, operation and franchising of Steak n Shake restaurants. Founded in 1934 in Normal, Illinois, Steak n Shake is one of the oldest restaurant chains in the country. As of September 27, 2006, we had 429 Company-owned restaurants and 48 franchised restaurants, located in 19 states. Steak n Shake restaurants are generally open 24 hours a day, seven days a week, and in addition to the core menu, offer a breakfast menu during breakfast hours. Lunch and dinner sales account for approximately 37% and 46% of sales, respectively, while breakfast and late night sales account for 6% and 11% of sales, respectively.

Our fiscal year ends on the last Wednesday in September. Accordingly, every five or six years, our fiscal year contains fifty-three weeks. Fiscal years 2006 and 2005 contained fifty-two weeks, while fiscal year 2004 contained fifty-three weeks. Our first, third, and fourth quarters contain twelve weeks and the second quarter contains sixteen weeks (except in fiscal years when there are fifty-three weeks, in which case the fourth quarter contains thirteen weeks).

#### *The Steak n Shake Concept*

We strive to be the best restaurant in the world at providing guests a genuine, classic community diner experience with STEAKBURGER™ sandwiches and hand-dipped milk shakes. We occupy a distinct niche in the restaurant industry by offering full-service dining with counter and dining room seating, as well as drive-thru and carryout service. Counter and dining room sales represent approximately sixty-percent of the sales mix, while sales for off-premises dining represent approximately forty-percent of the sales mix. Unlike some fast-food restaurants, all Steak n Shake food is freshly prepared, cooked-to-order in view of the guest, and served promptly on china with flatware and glassware by a friendly team of wait staff. Our prices are generally less than most casual dining and family-style concepts, with an average check of approximately \$6.90 per person. The average check during the peak lunch and dinner hours is approximately \$6.90 and \$7.20, respectively.

We believe that Steak n Shake offers more compelling value and core menu items with a higher level of quality than competing fast food chains. Our menu continues to feature core items that include STEAKBURGER™ sandwiches, thin and crispy french fries and hand-dipped milk shakes. We believe that our focus on certain menu items has allowed us to serve consistent, high-quality food that has built brand loyalty with our guests. Menu items are prepared in accordance with our strict specifications using high-quality ingredients including 100% pure U.S. beef, with cuts of T-bone, strip and sirloin steak, in our STEAKBURGER™ sandwiches.

Over the years, we have responded to changing guest tastes by providing greater menu variety without losing our focus or guest appeal. During the current year, new menu offerings included five varieties of Premium Topping Steakburger™ Sandwiches. These new steakburgers have provided more choices than our traditional Steakburger™ sandwiches. We have also added new Bits n Pieces™ Milk Shakes in the current year. These included bits and pieces of candies mixed into our traditional hand-dipped milkshakes. Candy choices include M&M®'s, chocolate peanut butter candies, cookie dough, and cookies and cream pieces. In addition to these new menu items that we have been launching Company wide, we are also testing other new items including Frozen Yogurt and Fruit n Frozen Yogurt Milk Shakes in select markets.

#### *Expanding the Concept*

Accelerating the Company's growth into both new and existing trade areas has been a focus in recent years. During fiscal year 2006, we opened twenty-six new Company-owned units and six new franchise units. The new

Company-owned units were built in existing markets, with franchise openings aiding in growth in current markets and new markets as well. This level of expansion has allowed us to build field organizational quality and stability while focusing on improving each and every guest experience through hospitality initiatives; improving depth in the field organization through improved recruitment and higher retention; enhancing training and staff development; and aggressively marketing the brand through differentiation. We currently expects to expand our growth by opening approximately fifteen Company-owned Steak n Shake restaurants in fiscal year 2007. The actual number of openings will depend on many factors, including the ability to locate appropriate sites, negotiate acceptable purchase or lease terms, obtain necessary local governmental permits, complete construction, and recruit and train restaurant management and hourly associates.

During our current fiscal fourth quarter, we acquired eight franchised restaurants from Creative Restaurants, Inc. ("CRI") a former franchisee. These restaurants were all well established restaurants primarily in the Louisville, Kentucky area. Similarly, we purchased 17 restaurants owned by Kelley Restaurants, Inc. ("KRI") in fiscal 2005. These restaurants were located in the Atlanta, Georgia and Charlotte, North Carolina markets. The purchase of franchised restaurants allows us to build on the success achieved by our franchisees while giving us the opportunity to further develop the markets in which these restaurants are located.

Because the site selection process is critical to the success of our restaurants, our senior management devotes significant time and resources to analyzing each prospective site. We consider a variety of factors in the site selection process, including local market demographics, site visibility and accessibility, highway interchanges and proximity to significant generators of potential guests, such as major retailers, housing communities and businesses. During fiscal 2006, we have begun utilizing a new site selection tool. Thompson MapInfo allows us to be much more analytic in our real estate site selections. This site selection tool provides a more sophisticated view of the sales potential for each prospective site as well as insight into markets around the country. In 2007 and beyond, we will continue to prioritize and select markets and individual sites for both Company-owned and franchise expansion.

***Our Strategic Plan***

During fiscal 2006, we unveiled our strategic plan for growth. While our growth plan is divided into 3 phases that build upon the previous phase, the strategic plan is centered around five key goals: Inspired Associates, Delighted Guests, Empowering Leaders, Process Excellence and Market Expansion. During 2007, the major focus of resources will be on Delighted Guests, with the goal of improving guest counts. As it relates to Delighted Guests, the first major initiative is called "The Guest Winning Promise." This initiative will explore a series of options for optimizing each element of the Steak 'n Shake guest experience including: building exterior design, interior atmosphere, dine-in & drive-thru menu, service execution, and point of sale system optimization. The intent is to be deliberate about every aspect of the Steak n Shake concept at a level of detail and understanding we have never completed before. We believe it is essential to ensure that our concept continues to have great consumer relevance while operating in the most efficient and effective manner possible.

While Delighted Guests will be our main focus in fiscal 2007, other initiatives will receive attention as well. For example, relative to Inspired Associates, we will begin a project called "The Associate Winning Promise." The goal of this project is to further understand the characteristics of those associates who most consistently delight our guests and find great satisfaction working at Steak 'n Shake. This will provide important insights about how best to attract, develop and retain these valued associates. We plan to begin testing and implementing the best ideas that arise from this research during 2007.

***Strengthening the Foundation***

In 2007, we expect to accelerate progress on field execution in a systematic manner. During 2006, we identified three key measures which correlate most highly with our same store sales success: change in drive-through speed, guest satisfaction in the dining room, and associate turnover. We have classified all restaurants into five quintiles based on their performance against these measures which we have labeled A (best) to E (worst). During 2007, we intend to make significant progress moving every "E-B" restaurant up at least one tier by working to address the issues affecting these under-performing units.

***Restaurant Locations***

The following table lists the locations of the 477 Steak n Shake restaurants, including 48 franchised units, as of September 27, 2006:

	<b>Company-Owned</b>	<b>Franchised</b>	<b>Total</b>
Alabama	6	-	6
Arkansas	-	1	1
Florida	83	-	83
Georgia	23	3	26
Illinois	62	6	68
Indiana	67	3	70
Iowa	4	-	4
Kansas	4	-	4
Kentucky	15	-	15
Michigan	21	-	21
Mississippi	-	1	1
Missouri	44	14	58
North Carolina	4	6	10

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Ohio	63	-	63
Oklahoma	-	4	4
Pennsylvania	5	-	5
South Carolina	2	1	3
Tennessee	8	9	17
Texas	18	-	18
Total	<u>429</u>	<u>48</u>	<u>477</u>



### ***Restaurant Operations***

The key to growing our customer base is ensuring our guests have an enjoyable dine-in, carry-out or drive-thru experience. To ensure a positive guest experience, we must have competent and skilled restaurant management at each of our locations. A typical Steak n Shake restaurant's management team consists of a general manager, a restaurant manager and from one to four managers. The number of managers varies depending upon the sales volume of the unit. Each restaurant's General Manager has primary responsibility for the day-to-day operations of the restaurant and is responsible for maintaining Company-established operating standards and procedures. The General Manager holds the responsibility for his/her unit's profitability and his/her bonus is partially based on exceeding the financial plan's expected store profitability. In addition to day-to-day operations, the General Manager is involved in the planning and budgeting process for his/her restaurant. An experienced, well-trained General Manager promotes compliance with our high standards for food quality and guest service, ensures that all health and safety requirements are met and ensures compliance with applicable state labor laws. We seek to employ managers who focus on guest service and who manage the restaurant from the dining room.

We foster a "promote from within" approach. To develop the talented bench strength needed for continued internal promotions, developing our associates into outstanding managers is one of our highest priorities. As part of our commitment to improving our standards of execution, we emphasize strengthening each management team's skills and capabilities through innovative selection, development, evaluation, and reward systems. Associates are encouraged to learn new skills to foster their professional growth and to create greater opportunities for advancement. The management development process is designed to not only meet our current management needs, but to provide the foundation for our future growth needs as well.

### ***Guest Satisfaction and Quality Control***

Our reputation and guest loyalty have been earned through the consistent quality of the dining experience we provide to our guests. Our future success depends on our associates' consistent commitment to exceeding the guests' expectations. This commitment is monitored at Company-owned units through the use of guest comment cards, guest satisfaction surveys, a mystery shopping program, frequent on-site visits and formal inspections by management and training personnel. Franchised restaurants are monitored through periodic inspections by the Company's franchise field operations personnel, guest satisfaction surveys, and a mystery shopping program, in addition to their own internal management oversight procedures. These guest satisfaction measurement tools provide data for both continuing and improving our excellence in customer service.

### ***Purchasing and Distribution Center Operations***

We operate one distribution center in Bloomington, Illinois from which food products (except for items purchased by the restaurants locally such as bakery goods, produce and dairy products) and restaurant supplies are delivered to 108 Company-owned and 9 franchised restaurants. The restaurants served by the distribution center are located in parts of the Midwest (primarily in Illinois, Missouri, Iowa and Wisconsin). Our semi-trailers handle refrigerated products, frozen products and dry goods in the same delivery trip. The restaurants that are not serviced by the distribution center obtain Company-approved food products and supplies from two separate independent distributors; one with locations in Orlando, Florida and Pryor, Oklahoma, and the other with a location in Zanesville, Ohio.

Purchases are negotiated centrally for most food and beverage products and supplies to ensure uniform quality, adequate quantities and competitive prices. Short-term forward buying contracts are utilized to facilitate the availability of products that meet our specifications and to lessen our exposure to fluctuating prices. Food and supply items undergo ongoing research, development and testing in an effort to maintain the highest quality products and to

be responsive to changing consumer tastes.

***Branding***

Our marketing thrust is driven by new product news and is directed towards building brand loyalty and increasing purchase frequency. Marketing platforms are product benefit directed and explain why Steak n Shake is superior to fast food alternatives by using a fun, irreverent, tongue-in-cheek approach in our advertising campaigns. This "voice of the restaurant" defines our brand personality. By coupling this branding approach with real consumer benefits, existing guests are encouraged to visit more often and new guests are encouraged to give our concept a try. Television and radio, outdoor billboards, and coupon inserts are our key areas of focus in advertising.

***Franchising***

We designed our franchising program to extend the Company's brand name recognition to areas where we have no current development plans, and to derive additional revenues without substantial investment. Our expansion plans include selectively seeking new franchisees to help grow the Steak n Shake brand, along with expanding relationships with current franchisees.

Franchisees undergo a selection process supervised by the Vice President, Franchising, and require final approval by senior management. We typically seek franchisees with the financial resources necessary to fund successful development and significant experience in the restaurant/retail business. We assist franchisees with both the development and ongoing operation of their restaurants. Our management personnel assist with site selection, approve all restaurant sites and provide franchisees with prototype plans and construction support and specifications for their restaurants. Our staff provides both on-site and off-site instruction to franchised restaurant management associates.