CHICOS FAS INC
Form 10-Q
November 28, 2006

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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 Quarter Ended:	Commission File Number:
October 28, 2006	0-21258

Chico s FAS, Inc.
(Exact name of registrant as specified in charter)

Florida	59-2389435
(State of Incorporation)	(I.R.S. Employer Identification No.)

11215 Metro Parkway, Fort Myers, Florida 33966
(Address of principal executive offices)
239-277-6200
(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 þ No o

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 þ Accelerated filer o 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 þ

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

At November 22, 2006, there were 175,757,992 shares outstanding of Common Stock, $.01 par value per share.

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CHICO S FAS, Inc. and Subsidiaries
Consolidated Balance Sheets
(In thousands)

	October 28, 2006 (Unaudited)	January 28, 2006
ASSETS		
Current Assets:		
Cash and cash equivalents	$ 2,606	$ 3,035
Marketable securities, at market	251,297	401,445
Receivables	19,313	7,240
Income taxes receivable		5,013
Inventories	137,650	95,421
Prepaid expenses	17,629	13,497
Land held for sale	38,120	
Deferred taxes	16,534	12,327
Total Current Assets	483,149	537,978
Property and Equipment:		
Land and land improvements	14,549	44,893
Building and building improvements	56,102	35,573
Equipment, furniture and fixtures	246,106	187,970
Leasehold improvements	275,843	209,342
Total Property and Equipment	592,600	477,778
Less accumulated depreciation and amortization	(169,885)	(131,846)
Property and Equipment, Net	422,715	345,932
Other Assets:		
Goodwill	69,348	61,796
Other intangible assets	34,063	34,041
Deferred taxes	7,814	
Other assets	20,914	19,666
Total Other Assets	132,139	115,503
	$ 1,038,003	$ 999,413
LIABILITIES AND STOCKHOLDERS EQUITY		
Current Liabilities:		
Accounts payable	$ 77,536	$ 47,434
Accrued liabilities	83,664	74,586
Current portion of deferred liabilities	1,179	648

Total Current Liabilities	162,379	122,668
Noncurrent Liabilities:		
Deferred liabilities	94,091	65,189
Deferred taxes		5,129
Total Noncurrent Liabilities	94,091	70,318
Stockholders Equity:		
Common stock	1,755	1,817
Additional paid-in capital	225,720	202,878
Unearned compensation		(3,710)
Retained earnings	554,059	605,537
Accumulated other comprehensive loss	(1)	(95)
Total Stockholders Equity	781,533	806,427
	$ 1,038,003	$ 999,413

See Accompanying Notes.

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CHICO S FAS, Inc. and Subsidiaries
Consolidated Statements of Income
(Unaudited)
(In thousands, except per share amounts)

	Thirty-Nine Weeks Ended				Thirteen Weeks Ended			
	October 28, 2006		October 29, 2005		October 28, 2006		October 29, 2005	
	Amount	% of Sales	Amount	% of Sales	Amount	% of Sales	Amount	% of Sales
Net sales by Chico s/Soma stores	$ 894,423	**74.5**	$ 816,672	**79.4**	$ 296,820	**73.6**	$ 277,601	**77.4**
Net sales by White House I Black Market stores	257,171	**21.4**	179,545	**17.4**	89,788	**22.2**	68,450	**19.1**
Net sales by catalog & Internet	37,192	**3.1**	24,526	**2.4**	12,659	**3.1**	9,534	**2.6**
Other net sales	11,410	**1.0**	8,102	**0.8**	4,296	**1.1**	3,080	**0.9**
Net sales	1,200,196	**100.0**	1,028,845	**100.0**	403,563	**100.0**	358,665	**100.0**
Cost of goods sold	474,151	**39.5**	394,935	**38.4**	162,826	**40.3**	133,308	**37.2**
Gross profit	726,045	**60.5**	633,910	**61.6**	240,737	**59.7**	225,357	**62.8**
General, administrative and store operating expenses	456,183	**38.0**	371,041	**36.1**	161,373	**40.0**	131,711	**36.7**
Depreciation and amortization	44,007	**3.7**	31,192	**3.0**	15,224	**3.8**	11,339	**3.2**
Income from operations	225,855	**18.8**	231,677	**22.5**	64,140	**15.9**	82,307	**22.9**
Interest income, net	8,303	**0.7**	5,658	**0.5**	2,339	**0.6**	2,154	**0.6**
Income before taxes	234,158	**19.5**	237,335	**23.0**	66,479	**16.5**	84,461	**23.5**
Income tax provision	85,704	**7.1**	87,814	**8.5**	24,332	**6.1**	31,251	**8.7**
Net income	$ 148,454	**12.4**	$ 149,521	**14.5**	$ 42,147	**10.4**	$ 53,210	**14.8**
Per share data:								
Net income per common share basic	$ 0.83		$ 0.83		$ 0.24		$ 0.29	
	$ 0.83		$ 0.82		$ 0.24		$ 0.29	

Net income per common and common equivalent share diluted				
Weighted average common shares outstanding basic	178,036	180,218	175,234	180,639
Weighted average common and common equivalent shares outstanding diluted	179,238	182,115	176,184	182,556

See Accompanying Notes.

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CHICO S FAS, Inc. and Subsidiaries
Consolidated Statements of Cash Flows
(Unaudited)
(In thousands)

	Thirty-Nine Weeks Ended	
	October 28, 2006	**October 29, 2005**
CASH FLOWS FROM OPERATING ACTIVITIES:		
Net income	$ 148,454	$ 149,521
Adjustments to reconcile net income to net cash provided by operating activities		
Depreciation and amortization, cost of goods sold	5,557	3,437
Depreciation and amortization, other	44,007	31,192
Deferred tax benefit	(17,216)	(15,352)
Stock-based compensation expense, cost of goods sold	4,833	317
Stock-based compensation expense, general, administrative and store operating expenses	12,052	854
Excess tax benefit of stock-based compensation	(2,623)	
Tax benefit of stock options exercised		13,301
Deferred rent expense, net	5,133	2,635
Loss on disposal of property and equipment	820	437
(Increase) decrease in assets		
Receivables	(7,091)	(4,528)
Inventories	(41,506)	(28,308)
Prepaid expenses and other, net	(5,403)	(5,135)
Increase in liabilities		
Accounts payable	30,103	30,794
Accrued and other deferred liabilities	36,837	36,089
Total adjustments	65,503	65,733
Net cash provided by operating activities	213,957	215,254
CASH FLOWS FROM INVESTING ACTIVITIES:		
Sales (purchases) of marketable securities, net	150,242	(130,946)
Purchase of Fitigues assets	(7,527)	
Acquisition of franchise store	(811)	
Purchase of equity investment		(10,418)
Purchases of property and equipment	(165,094)	(87,103)
Net cash used in investing activities	(23,190)	(228,467)
CASH FLOWS FROM FINANCING ACTIVITIES:		
Proceeds from issuance of common stock	6,181	16,908
Excess tax benefit of stock-based compensation	2,623	

Repurchase of common stock		(200,000)		
Net cash (used in) provided by financing activities		(191,196)		16,908
Net (decrease) increase in cash and cash equivalents		(429)		3,695
CASH AND CASH EQUIVALENTS Beginning of period		3,035		14,426
CASH AND CASH EQUIVALENTS End of period	$	2,606	$	18,121
SUPPLEMENTAL DISCLOSURES OF CASH FLOW INFORMATION:				
Cash paid for interest	$	73	$	67
Cash paid for income taxes, net	$	86,950	$	78,698

See Accompanying Notes.

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CHICO S FAS, Inc. and Subsidiaries
Notes to Consolidated Financial Statements
October 28, 2006
(Unaudited)
(in thousands, except share and per share amounts)

Note 1. Basis of Presentation

The accompanying unaudited consolidated financial statements of Chico s FAS, Inc. and its wholly-owned subsidiaries (collectively, the Company) have been prepared in accordance with the instructions to Form 10-Q and do not include all of the information and notes required by accounting principles generally accepted in the U.S. for complete financial statements. In the opinion of management, all adjustments (consisting of normal recurring accruals) considered necessary for a fair presentation have been included. All significant intercompany balances and transactions have been eliminated in consolidation. For further information, refer to the consolidated financial statements and notes thereto for the fiscal year ended January 28, 2006, included in the Company s Annual Report on Form 10-K filed with the Securities and Exchange Commission (SEC) on April 7, 2006. The January 28, 2006 balance sheet amounts were derived from audited financial statements included in the Company s Annual Report.

The Company s fiscal years end on the Saturday closest to January 31 and are designated by the calendar year in which the fiscal year commences. Operating results for the thirty-nine weeks ended October 28, 2006 are not necessarily indicative of the results that may be expected for the entire year.

Other net sales for the current period consist of net sales to franchisees and net sales related to the Company s recently acquired Fitigues stores. Other net sales for the prior period consist of net sales to franchisees.

Note 2. Recent Accounting Pronouncements

In October 2006, the Financial Accounting Standards Board (the FASB) issued FASB Interpretation No. 48, Accounting for Uncertainty in Income Taxes-an interpretation of FASB Statement No. 109 (FIN 48). FIN 48 clarifies the accounting for income taxes by prescribing the minimum recognition threshold a tax position is required to meet before being recognized in the financial statements. Additionally, FIN 48 provides guidance on derecognition, classification, interest, penalties, accounting in interim periods and disclosure related to uncertain income tax positions. FIN 48 is effective for fiscal years beginning after December 15, 2006. The Company is currently evaluating the impact of adopting FIN 48; however, the Company does not expect the adoption of FIN 48 to have a material effect on its financial position, results of operations or cash flows.

Note 3. Land Held for Sale

During the third quarter of fiscal 2006, the Company reclassified a parcel of land located in south Fort Myers, Florida with a book value of $38.1 million from a long-term asset to a current asset held for sale. The Company anticipates that the land will be sold within the next 12 months, and the Company does not expect that any such sale will have any material impact on its statements of operations or overall financial position.

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Note 4. Goodwill and Intangible Assets

The Company s goodwill and its indefinite-lived intangible asset are reviewed annually for impairment or more frequently if impairment indicators arise. The annual valuation will be performed during the fourth quarter of each year. The change in the carrying amount of goodwill for the thirty-nine weeks ended October 28, 2006 is as follows:

Balance as of January 28, 2006	$ 61,796
Goodwill related to the acquisition of Fitigues	6,752
Goodwill related to the acquisition of franchise store	800
Total	$ 69,348

Note 5. Stock-Based Compensation

General

Effective January 29, 2006, the Company adopted the provisions of Statement of Financial Accounting Standard (SFAS) No. 123R, Share-Based Payment (SFAS 123R) using the modified prospective transition method. Under this transition method, stock-based compensation expense recognized for share-based awards during the thirteen and thirty-nine weeks ended October 29, 2006 includes: (a) compensation expense for all stock-based compensation awards granted prior to, but not yet vested as of, January 29, 2006, based on the grant date fair value estimated in accordance with the original provisions of SFAS No. 123, Accounting for Stock-Based Compensation (SFAS 123), and (b) compensation expense for all stock-based compensation awards granted subsequent to January 29, 2006, based on the grant date fair value estimated in accordance with the provisions of SFAS 123R. In accordance with the modified prospective transition method, results for the prior period have not been restated. Prior to the adoption of SFAS 123R, the Company recognized stock-based compensation expense in accordance with Accounting Principles Board (APB) Opinion No. 25, Accounting for Stock Issued to Employees (APB 25) and related Interpretations, as permitted by SFAS 123.

At October 28, 2006, the Company had stock-based compensation plans as more particularly described below. The total compensation expense related to stock-based awards granted under these plans during the thirteen and thirty-nine weeks ended October 28, 2006, reflecting the impact of the implementation of the modified prospective transition method in accordance with SFAS 123R, was $6.0 million and $16.9 million, respectively. The total compensation expense related to stock-based awards granted under these plans during the thirteen and thirty-nine weeks ended October 29, 2005, reflecting compensation expense recognized in accordance with APB 25, was $0.4 million and $1.2 million, respectively. Effective January 29, 2006 and subsequent thereto, the Company recognizes stock-based compensation costs net of a forfeiture rate for only those shares expected to vest on a straight-line basis over the requisite service period of the award. The Company estimated the forfeiture rate for each quarter of fiscal 2006 based on its historical experience during the preceding four fiscal years.

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Note 5. Stock-Based Compensation (continued)

As a result of adopting SFAS 123R, the impact to the consolidated statements of income for the thirteen weeks ended October 28, 2006 on income before income taxes and net income was a reduction of $4.8 million and $3.1 million, respectively, from what would have been presented if the Company had continued to account for stock option awards under APB 25. The impact on basic and diluted earnings per share for the thirteen weeks ended October 28, 2006 was a reduction of $0.02 per share.

As a result of adopting SFAS 123R, the impact to the consolidated statements of income for the thirty-nine weeks ended October 28, 2006 on income before income taxes and net income was a reduction of $13.8 million and $8.9 million, respectively, from what would have been presented if the Company had continued to account for stock option awards under APB 25. The impact on basic and diluted earnings per share for the thirty-nine weeks ended October 28, 2006 was a reduction of $0.05 per share.

In addition, prior to the adoption of SFAS 123R, the Company presented all tax benefits related to deductions resulting from the exercise of stock options as operating activities in the consolidated statement of cash flows. SFAS 123R requires that cash flows resulting from tax benefits attributable to tax deductions in excess of the compensation expense recognized for those options (excess tax benefits) be classified as financing cash flows. As a result, the Company classified $2.6 million of excess tax benefits as financing cash flows for the thirty-nine weeks ended October 28, 2006. The total income tax benefit recognized in the consolidated statement of operations for share-based awards during the thirteen and thirty-nine weeks ended October 28, 2006 (in accordance with the provisions of SFAS 123R) was $2.1 million and $6.1 million, respectively. During the thirteen and thirty-nine weeks ended October 29, 2005, the total income tax benefit recognized in the consolidated statement of operations for share-based awards (in accordance with the provisions of APB 25) was $0.1 million and $0.4 million, respectively.

The pro forma table below illustrates the effect on net income and earnings per share as if the Company had applied the fair value recognition provisions of SFAS No. 123, as amended by SFAS No. 148, Accounting for Stock-Based Compensation- Transition and Disclosure , to all stock-based employee compensation for the thirty-nine and thirteen weeks ended October 29, 2005:

	Thirty-Nine Weeks Ended October 29, 2005	Thirteen Weeks Ended October 29, 2005
Net income, as reported	$ 149,521	$ 53,210
Add: Stock-based compensation expense included in reported net income, net of taxes	738	244
Deduct: Total stock-based employee compensation expense determined under fair value based method for all awards, net of taxes	(9,104)	(3,122)
Net income, pro forma	$ 141,155	$ 50,332
Net income per common share:		
Basic as reported	$ 0.83	$ 0.29
Basic pro forma	$ 0.78	$ 0.28
Diluted as reported	$ 0.82	$ 0.29

Diluted pro forma	$	0.78	$	0.28

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Note 5. Stock-Based Compensation (continued)

Stock Option Plans

The Company has share-based awards outstanding under three different plans: (1) the 1993 Stock Option Plan, (2) the Independent Directors Plan and (3) the 2002 Omnibus Stock and Incentive Plan (the Omnibus Plan). Stock options granted and outstanding under each of the plans generally vest evenly over three years (except for the Independent Directors Plan, whose options generally vest after 6 months) and have a 10-year contractual term. The exercise price of a stock option generally is equal to the fair market value of the Company s common stock on the option grant date. No new grants will be made under the Company s existing 1993 Plan or Independent Directors Plan, and such existing plans remain in effect only for purposes of administering options that were outstanding on the date the Omnibus Plan was approved by the Company s shareholders. The Omnibus Plan provides for awards of nonqualified stock options, incentive stock options, restricted stock awards and restricted stock units. Restricted stock awards are stock awards that are not vested when received. The Omnibus Plan initially reserved 9,710,280 shares of common stock for future issuance. As of October 28, 2006, 2,064,378 shares of common stock remain available for issuance under the Omnibus Plan.

Beginning in the first quarter of fiscal 2005, certain of the Company s officers and non-officers, its two non-officer inside directors, and each of its independent directors have been granted restricted stock awards, pursuant to restricted stock agreements. A restricted stock award is an award of common shares that is subject to certain restrictions during a specified period. Restricted stock awards are independent of option grants and are generally subject to forfeiture if employment terminates prior to the release of the restrictions. The Company holds the certificates for such shares in safekeeping during the vesting period, and the grantee cannot transfer the shares before the respective shares vest. Shares of nonvested restricted stock have the same voting rights as common stock, are entitled to receive dividends and other distributions thereon and are considered to be currently issued and outstanding. Restricted stock awarded to officers and non-officer employees in fiscal 2005 vests 100% at the end of three years from the date of grant. In early fiscal 2006, the Company decided to change the vesting for future restricted stock awards awarded to officers and non-officer employees such that substantially all restricted stock vests pro-rata over a period of three years from the date of grant. The restricted stock awarded to non-officer directors in both fiscal 2005 and 2006 vests pro-rata over a period of three years from the date of grant. The Company expenses the cost of the restricted stock awards, which is determined to be the fair market value of the shares at the date of grant, straight-line over the period during which the restrictions lapse. For these purposes, the fair market value of the restricted stock is determined based on the closing price of the Company s common stock on the grant date.

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Note 5. Stock-Based Compensation (continued)

Employee Stock Purchase Plan

The Company sponsors an employee stock purchase plan (the ESPP) under which substantially all full-time employees are given the right to purchase up to 800 shares of the common stock of the Company two times a year at a price equal to 85 percent of the value of the stock immediately prior to the beginning of each purchase period. Prior to January 29, 2006, the Company recognized no compensation expense for the issuance of shares under the ESPP. As of January 29, 2006 and in accordance with the provisions of SFAS 123R, the Company recognizes compensation expense based on the 15% discount at purchase. For the thirty-nine weeks of fiscal 2006, ESPP compensation expense was $0.3 million.

Methodology Assumptions

As part of its SFAS 123R adoption, the Company examined its historical pattern of option exercises in an effort to determine if there were any discernable activity patterns based on certain employee populations. From this analysis, the Company identified two employee populations. The Company uses the Black-Scholes option-pricing model to value the Company s stock options for each of the employee populations. Using this option-pricing model, the fair value of each stock option award is estimated on the date of grant. The fair value of the Company s stock option awards, which are subject to pro-rata vesting generally over 3 years, is expensed on a straight-line basis over the vesting period of the stock options. The expected volatility assumption is based on the historical volatility of the Company s stock over a term equal to the expected term of the option granted. The expected term of stock option awards granted is derived from historical exercise experience for each of the employee populations under the Company s stock option plans and represents the period of time that stock option awards granted are expected to be outstanding for each of the two identified employee populations. The expected term assumption incorporates the contractual term of an option grant, which is ten years, as well as the vesting period of an award, which is generally pro-rata vesting over three years. The risk-free interest rate is based on the implied yield on a U.S. Treasury constant maturity with a remaining term equal to the expected term of the option granted.

The weighted average assumptions relating to the valuation of the Company s stock options for the thirty-nine and thirteen weeks ended October 28, 2006 and October 29, 2005 were as follows:

	Thirty-Nine Weeks Ended		**Thirteen Weeks Ended**	
	October 28, 2006	**October 29, 2005**	**October 28, 2006**	**October 29, 2005**
Weighted average fair value of grants	$15.37	$ 14.13	$9.32	$ 16.31
Expected volatility	46%	57%	46%	49%
Expected term (years)	4.5	4.6	4.5	4.4
Risk-free interest rate	4.6%	3.9%	4.6%	4.2%
Expected dividend yield	N/A	N/A	N/A	N/A

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Note 5. Stock-Based Compensation (continued)

Stock Based Compensation Activity

The following table presents a summary of the Company s stock options activity for the thirty-nine weeks ended October 28, 2006:

	Weighted Average