

MORTONS RESTAURANT GROUP INC  
Form 10-Q  
August 02, 2011  
Table of Contents

**UNITED STATES**  
**SECURITIES AND EXCHANGE COMMISSION**  
**WASHINGTON, DC 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 July 3, 2011

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 number 1-12692

**MORTON S RESTAURANT GROUP, INC.**

(Exact name of registrant as specified in its charter)

**Delaware**  
(State or other jurisdiction of incorporation or organization)

**13-3490149**  
(I.R.S. employer identification no.)

**325 North LaSalle Street, Suite 500, Chicago, Illinois**  
(Address of principal executive offices)

**60654**  
(Zip code)

**312-923-0030**  
(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  or No .

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Indicate by check mark whether the registrant has submitted electronically and posted on its corporate Web site, if any, every Interactive Data File required to be submitted and posted pursuant to Rule 405 of Regulation S-T during the preceding 12 months (or for such shorter period that the registrant was required to submit and post such files). Yes  or 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 definition of large accelerated filer, accelerated filer and smaller reporting company in Rule 12b-2 of the Exchange Act. (Check one):

Large accelerated filer       Accelerated filer       Non-accelerated filer       Smaller reporting company   
(Do not check if a 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  or No .

As of July 28, 2011, the registrant had 16,901,860 shares of its Common Stock, \$0.01 par value, outstanding.

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**Table of Contents**

MORTON S RESTAURANT GROUP, INC. AND SUBSIDIARIES

INDEX

|  | <b>Page</b> |
|--|-------------|
| <u>Forward-Looking Statements</u>  |             |
| <b><u>Part I - Financial Information</u></b>   |             |
| <u>Item 1. Financial Statements</u>  |             |
| <u>Consolidated Balance Sheets as of July 3, 2011 and January 2, 2011 - unaudited</u>  | 4           |
| <u>Consolidated Statements of Operations for the three and six month periods ended July 3, 2011 and July 4, 2010 - unaudited</u> | 6           |
| <u>Consolidated Statements of Cash Flows for the six month periods ended July 3, 2011 and July 4, 2010 - unaudited</u>           | 7           |
| <u>Notes to Unaudited Consolidated Financial Statements</u>  | 8           |
| <u>Item 2. Management's Discussion and Analysis of Financial Condition and Results of Operations</u>                             | 16          |
| <u>Item 3. Quantitative and Qualitative Disclosures about Market Risk</u>  | 22          |
| <u>Item 4. Controls and Procedures</u>   | 22          |
| <b><u>Part II - Other Information</u></b>  |             |
| <u>Item 1. Legal Proceedings</u>   | 23          |
| <u>Item 1A. Risk Factors</u>   | 23          |
| <u>Item 2. Unregistered Sales of Equity Securities and Use of Proceeds</u>   | 23          |
| <u>Item 6. Exhibits</u>  | 24          |
| <u>Signatures</u>  | 25          |

## Table of Contents

### Forward-Looking Statements

This Form 10-Q contains various forward-looking statements within the meaning of Section 27A of the Securities Act of 1933, as amended, and Section 21E of the Securities Exchange Act of 1934, as amended (the Exchange Act). Forward-looking statements, written, oral or otherwise made, represent the Company's expectation or belief concerning future events. Without limiting the foregoing, the words believes, thinks, anticipates, estimates, plans, expects, and similar expressions are intended to identify forward-looking statements.

The Company cautions that these statements are subject to risks, uncertainties, assumptions and other important factors that could cause actual results to differ materially from those in the forward-looking statements, including, without limitation:

- (i) a reduction in consumer and/or business spending in one or more of the Company's markets due to business layoffs or budget reductions, negative consumer sentiment, access to consumer credit, commodity and other prices, events or occurrences affecting the securities and/or financial markets, occurrences affecting the Company's common stock, housing values, changes in federal, state, foreign and/or local tax levels or other factors;
- (ii) risks relating to the restaurant industry and the Company's business, including competition, changes in consumer tastes and preferences, risks associated with opening new locations, increases in food and other raw materials costs, increases in energy costs, demographic trends, traffic patterns, weather conditions, employee availability, benefits and cost increases, perceived product safety issues, supply interruptions, litigation judgments or settlements in pending litigation, government regulation, the Company's ability to maintain adequate financing facilities, the Company's liquidity and capital resources, prevailing interest rates and legal and regulatory matters;
- (iii) public health issues, including, without limitation risks relating to the spread of pandemic diseases;
- (iv) risks regarding the timing or whether the Company will elect to pursue any of the strategic alternatives it may consider, or that any such alternatives will result in changes to the Company's business plan or a sale of the Company; and
- (v) other risks detailed in Item 1A. Risk Factors herein, in the Company's most recent Form 10-K and in the Company's other reports filed from time to time with the Securities and Exchange Commission.

In addition, the Company's ability to open new restaurants is dependent upon various factors, such as the availability of attractive sites for new restaurants, the ability to negotiate suitable lease terms, the ability to generate or borrow funds to develop new restaurants, the ability to obtain various government permits and licenses, limitations on permitted capital expenditures under the Company's Senior Credit Facility (as defined in Note 8 Long Term Debt in the Notes to Consolidated Financial Statements in Part I, Item 1 of this report) and the recruitment and training of skilled management and restaurant employees. Other unknown or unpredictable factors also could harm the Company's business, financial condition and results. Consequently, there can be no assurance that actual results or developments anticipated by the Company will be realized or, even if substantially realized, that they will have the expected consequences to, or effects on, the Company. The Company undertakes no obligation to update or revise any forward-looking statements, whether as a result of new information, future events or otherwise, except to the extent required by applicable securities laws.

**Table of Contents****Part I-Financial Information****Item 1. Financial Statements**

## MORTON S RESTAURANT GROUP, INC. AND SUBSIDIARIES

## Consolidated Balance Sheets

(amounts in thousands)

|   | July 3,<br>2011   | January 2,<br>2011 |
|---|-------------------|--------------------|
|   | (unaudited)       |                    |
| <b>Assets</b>                                   |                   |                    |
| Current assets:                                 |                   |                    |
| Cash and cash equivalents                       | \$ 1,151          | \$ 1,214           |
| Restricted cash                                 | 1,532             | 1,435              |
| Accounts receivable                             | 4,456             | 6,407              |
| Inventories                                     | 10,197            | 10,819             |
| Prepaid expenses and other current assets       | 3,307             | 4,180              |
| Income taxes receivable                         | 44                | 96                 |
| <b>Total current assets</b>                     | <b>20,687</b>     | <b>24,151</b>      |
| Property and equipment, at cost:                |                   |                    |
| Furniture, fixtures and equipment               | 31,203            | 29,635             |
| Buildings and leasehold improvements            | 103,491           | 99,330             |
| Land  | 7,300             | 7,300              |
| Construction in progress                        | 198               | 1,320              |
|   | 142,192           | 137,585            |
| Less: accumulated depreciation and amortization | 51,562            | 46,091             |
| <b>Property and equipment, net</b>              | <b>90,630</b>     | <b>91,494</b>      |
| Intangible asset                                | 73,000            | 73,000             |
| Goodwill  | 6,990             | 6,938              |
| Other assets and deferred expenses, net         | 6,096             | 6,231              |
|   | <b>\$ 197,403</b> | <b>\$ 201,814</b>  |

**Table of Contents**

## MORTON S RESTAURANT GROUP, INC. AND SUBSIDIARIES

## Consolidated Balance Sheets, Continued

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

|   | July 3,<br>2011   | January 2,<br>2011 |
|---|-------------------|--------------------|
|   | (unaudited)       |                    |
| <b>Liabilities and Equity</b>   |                   |                    |
| Current liabilities:  |                   |                    |
| Accounts payable  | \$ 9,692          | \$ 11,703          |
| Accrued expenses  | 18,516            | 20,959             |
| Deferred revenue from gift certificates and gift cards  | 12,030            | 15,542             |
| Current portion of long-term debt   | 3,880             | 3,871              |
| Accrued income taxes  | 425               | 936                |
| <b>Total current liabilities</b>  | <b>44,543</b>     | <b>53,011</b>      |
| Long-term debt, net of current portion  | 64,959            | 63,631             |
| Deferred income taxes, net  | 25,957            | 25,857             |
| Deferred rent and landlord allowances   | 42,455            | 42,520             |
| Other liabilities   | 2,888             | 3,671              |
| <b>Total liabilities</b>  | <b>180,802</b>    | <b>188,690</b>     |
| Commitments and contingencies   |                   |                    |
| Equity:   |                   |                    |
| Morton s Restaurant Group, Inc. and Subsidiaries:   |                   |                    |
| Preferred stock, \$0.01 par value per share. 30,000,000 shares authorized, 1,200,000 issued and outstanding at July 3, 2011 and at January 2, 2011  | 12                | 12                 |
| Common stock, \$0.01 par value per share. 100,000,000 shares authorized, 17,413,739 and 17,267,571 issued and 16,181,739 and 16,035,571 outstanding at July 3, 2011 and January 2, 2011, respectively | 175               | 173                |
| Additional paid-in capital  | 175,183           | 174,828            |
| Treasury stock, 1,232,000 shares at a weighted average cost of \$7.63 per share at July 3, 2011 and January 2, 2011   | (9,395)           | (9,395)            |
| Accumulated other comprehensive income  | 1,164             | 961                |
| Accumulated deficit   | (149,980)         | (152,790)          |
| <b>Total stockholders' equity of controlling interest</b>   | <b>17,159</b>     | <b>13,789</b>      |
| Noncontrolling interest   | (558)             | (665)              |
| <b>Total equity</b>   | <b>16,601</b>     | <b>13,124</b>      |
|   | <b>\$ 197,403</b> | <b>\$ 201,814</b>  |

See accompanying notes to unaudited consolidated financial statements.

**Table of Contents**

## MORTON S RESTAURANT GROUP, INC. AND SUBSIDIARIES

## Consolidated Statements of Operations

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

|   | Three month periods ended |                 | Six month periods ended |                 |
|---|---------------------------|-----------------|-------------------------|-----------------|
|   | July 3,<br>2011           | July 4,<br>2010 | July 3,<br>2011         | July 4,<br>2010 |
|   |                           |                 | (unaudited)             |                 |
| Revenues  | \$ 77,963                 | \$ 70,457       | \$ 160,486              | \$ 145,779      |
| Food and beverage costs                                   | 23,958                    | 21,481          | 49,575                  | 44,142          |
| Restaurant operating expenses                             | 42,389                    | 39,326          | 85,251                  | 80,559          |
| Pre-opening costs   | 82                        | 325             | 354                     | 429             |
| Depreciation and amortization                             | 2,734                     | 2,543           | 5,395                   | 5,042           |
| General and administrative expenses                       | 4,767                     | 3,838           | 9,778                   | 8,088           |
| Marketing and promotional expenses                        | 1,703                     | 1,889           | 3,229                   | 3,285           |
| Charge related to legal settlements                       |                           |                 | 481                     | 540             |
| Operating income  | 2,330                     | 1,055           | 6,423                   | 3,694           |
| Interest expense, net                                     | 1,344                     | 923             | 2,686                   | 1,875           |
| Income before income taxes from continuing operations     | 986                       | 132             | 3,737                   | 1,819           |
| Income tax expense  | 248                       | 6               | 824                     | 438             |
| Income from continuing operations                         | 738                       | 126             | 2,913                   | 1,381           |
| Discontinued operations                                   |                           | (789)           |                         | (803)           |
| Net income (loss)   | 738                       | (663)           | 2,913                   | 578             |
| Net income (loss) attributable to noncontrolling interest | 84                        | (147)           | 103                     | (113)           |
| Net income (loss) attributable to controlling interest    | \$ 654                    | \$ (516)        | \$ 2,810                | \$ 691          |
| Amounts attributable to controlling interest:             |                           |                 |                         |                 |
| Income from continuing operations                         | \$ 654                    | \$ 273          | \$ 2,810                | \$ 1,494        |
| Discontinued operations                                   |                           | (789)           |                         | (803)           |
| Net income (loss)   | \$ 654                    | \$ (516)        | \$ 2,810                | \$ 691          |
| Basic income (loss) per share:                            |                           |                 |                         |                 |
| Continuing operations                                     | \$ 0.04                   | \$ 0.02         | \$ 0.17                 | \$ 0.09         |
| Discontinued operations                                   | \$ 0.00                   | \$ (0.05)       | \$ 0.00                 | \$ (0.05)       |
| Net income (loss) per share                               | \$ 0.04                   | \$ (0.03)       | \$ 0.17                 | \$ 0.04         |
| Diluted income (loss) per share:                          |                           |                 |                         |                 |
| Continuing operations                                     | \$ 0.04                   | \$ 0.02         | \$ 0.16                 | \$ 0.09         |
| Discontinued operations                                   | \$ 0.00                   | \$ (0.05)       | \$ 0.00                 | \$ (0.05)       |
| Net income (loss) per share                               | \$ 0.04                   | \$ (0.03)       | \$ 0.16                 | \$ 0.04         |
| Shares used in computing net income (loss) per share:     |                           |                 |                         |                 |
| Basic   | 16,181,045                | 16,032,419      | 16,154,850              | 16,010,087      |
| Diluted   | 17,618,481                | 17,471,550      | 17,673,759              | 17,153,196      |

See accompanying notes to unaudited consolidated financial statements.





**Table of Contents**

## MORTON S RESTAURANT GROUP, INC. AND SUBSIDIARIES

## Consolidated Statements of Cash Flows

(amounts in thousands)

|   | Six month periods ended |                 |
|---|-------------------------|-----------------|
|   | July 3,<br>2011         | July 4,<br>2010 |
|   | (unaudited)             |                 |
| Cash flows from operating activities:   |                         |                 |
| Net income  | \$ 2,913                | \$ 578          |
| Adjustments to reconcile net income to net cash used in operating activities:     |                         |                 |
| Depreciation, amortization and other non-cash charges                             | 6,027                   | 6,633           |
| Non-cash portion of charge related to legal settlements                           |                         | 540             |
| Deferred income taxes   | 416                     | (251)           |
| Change in assets and liabilities:   |                         |                 |
| Accounts receivable   | 1,964                   | 2,266           |
| Inventories   | 651                     | 390             |
| Prepaid expenses and other assets   | 849                     | (1,471)         |
| Income taxes receivable   | 52                      | 488             |
| Accounts payable  | (2,045)                 | (449)           |
| Accrued expenses and deferred revenue   | (5,201)                 | (8,646)         |
| Other liabilities   | (642)                   | 1,879           |
| Accrued income taxes  | (730)                   | (200)           |
| Net cash provided by operating activities   | 4,254                   | 1,757           |
| Cash flows from investing activities:   |                         |                 |
| Purchases of property and equipment   | (5,443)                 | (5,023)         |
| Net cash used in investing activities   | (5,443)                 | (5,023)         |
| Cash flows from financing activities:   |                         |                 |
| Borrowings under senior credit facility   | 7,100                   | 6,300           |
| Payments made on senior credit facility   | (5,862)                 | (5,000)         |
| Principal reduction on obligation to financial institution                        | (86)                    | (80)            |
| Borrowings under non-recourse loan  |                         | 89              |
| Shares vested and surrendered by employees in lieu of paying minimum income taxes | (354)                   | (159)           |
| Increase in restricted cash   | (77)                    | (2,498)         |
| (Payments) proceeds from joint venture loan payable                               | (84)                    | 4,097           |
| JV partners' investment in joint venture  |                         | 171             |
| Payments of deferred financing costs  | (6)                     | (11)            |
| Net cash provided by financing activities   | 631                     | 2,909           |
| Effect of exchange rate changes on cash   | 495                     | (25)            |
| Net decrease in cash and cash equivalents   | (63)                    | (382)           |
| Cash and cash equivalents at beginning of period                                  | 1,214                   | 1,141           |
| Cash and cash equivalents at end of period  | \$ 1,151                | \$ 759          |

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See accompanying notes to unaudited consolidated financial statements.

**Table of Contents**

## MORTON S RESTAURANT GROUP, INC. AND SUBSIDIARIES

## Notes to Unaudited Consolidated Financial Statements

July 3, 2011 and July 4, 2010

**1) Basis of Presentation**

The accompanying unaudited consolidated financial statements of Morton s Restaurant Group, Inc. and its subsidiaries ( MRG, the Company, the controlling interest, we, us and our ) have been prepared in accordance with accounting principles generally accepted in the United States of America ( GAAP ) for interim financial information and with the instructions to Form 10-Q. Accordingly, they do not include all information and footnotes required by GAAP for complete financial statements and should be read in conjunction with the Company s Annual Report on Form 10-K for the fiscal year ended January 2, 2011.

The preparation of financial statements in accordance with GAAP requires management of the Company to make estimates and assumptions relating to assets, liabilities, revenues and expenses reported during the period. Actual results could differ from those estimates.

The Company uses a 52/53 week fiscal year which ends on the Sunday closest to January 1. Approximately every six or seven years, a 53rd week is added. Fiscal 2011 and fiscal 2010 are each 52 week years.

MRG was incorporated as a Delaware corporation on October 3, 1988. In February 2006, the Company and certain selling stockholders completed an initial public offering ( IPO ) of shares of common stock. The first Morton s was opened in 1978 in downtown Chicago, where Morton s corporate office is still located. Since then, Morton s has grown to 77 restaurants ( Morton s ) and one Trevi restaurant ( Trevi ) as of July 3, 2011.

**2) Statements of Cash Flows**

For the purposes of the consolidated statements of cash flows, the Company considers all highly liquid instruments purchased with an original maturity of three months or less to be cash equivalents. In addition, accrued purchases of property and equipment are reflected as non-cash transactions in the consolidated statements of cash flows. Furthermore, the issuance of Series A Convertible Preferred Stock ( Preferred Stock ) in connection with the settlement of certain wage and hour litigation during the six month period ended July 4, 2010, is reflected as a non-cash transaction in the consolidated statements of cash flows.

The following table sets forth the amount of interest paid, including capitalized interest, and net income taxes paid for each period presented in the consolidated statements of cash flows (amounts in thousands):

|                                   | Six month periods ended |                 |
|-----------------------------------|-------------------------|-----------------|
|                                   | July 3,<br>2011         | July 4,<br>2010 |
| Interest paid                     | \$ 2,548                | \$ 1,448        |
| Capitalized interest              | 20                      | 7               |
| Income taxes paid, net of refunds | 1,088                   | 407             |

**Table of Contents****3) Income Taxes**

The Company recognized income tax expense of \$0.8 million on pre-tax income related to continuing operations of \$3.7 million for the six month period ended July 3, 2011. The Company's effective tax rate was 22.1% for the six month period ended July 3, 2011 and was primarily attributable to non-U.S. income taxes, as well as current state income taxes. Based on management's evaluation of certain factors, in the fourth quarter of fiscal 2009, the Company established a valuation allowance for all U.S. federal and state deferred tax assets. Management continues to believe that a valuation allowance for all U.S. federal and state deferred tax assets is necessary based on the cumulative loss incurred in the past three years. Consideration is given to all available evidence, both positive and negative, in assessing the need for a valuation allowance. Due to the historical losses recorded in our U.S. operations and the uncertainty of the economic outlook, we continue to maintain a full valuation allowance against our U.S. deferred tax assets.

**4) Net Income (loss) per Share**

The Company computes net income (loss) per common share in accordance with ASC Topic 260, *Earnings per Share*. Basic net income (loss) per share has been computed by dividing net income by the weighted average shares outstanding for the period. Diluted net income (loss) per share is calculated in the same manner, but adjusts shares outstanding to reflect the potential dilution that would occur if unvested restricted stock awards were vested and if the preferred shares outstanding had been converted to common shares. In periods where losses are recorded, inclusion of potentially dilutive securities in the calculation would decrease the loss per common share and, therefore, these securities are not added to the weighted average number of shares outstanding due to their anti-dilutive effect.

The following table sets forth the approximate number of shares that were not included in the calculation of diluted net income (loss) per share because their effect would have been anti-dilutive, if any, and the computation of basic and diluted net income (loss) per share (amounts in thousands, except share and per share amounts):

|  | Three month periods ended |                 | Six month periods ended |                 |
|--|---------------------------|-----------------|-------------------------|-----------------|
|  | July 3,<br>2011           | July 4,<br>2010 | July 3,<br>2011         | July 4,<br>2010 |
| Potentially dilutive shares that are considered anti-dilutive: |                           |                 |                         |                 |
| Restricted stock   | 104,000                   | 240,000         | 122,000                 | 282,000         |
| Income from continuing operations                              | \$ 654                    | \$ 273          | \$ 2,810                | \$ 1,494        |
| Discontinued operations  |                           | (789)           |                         | (803)           |
| Net income (loss) attributable to controlling interest         | \$ 654                    | \$ (516)        | \$ 2,810                | \$ 691          |
| Shares:  |                           |                 |                         |                 |
| Weighted average number of basic common shares outstanding     | 16,181,045                | 16,032,419      | 16,154,850              | 16,010,087      |
| Dilutive potential common shares                               | 1,437,436                 | 1,439,131       | 1,518,909               | 1,143,109       |
| Weighted average number of diluted common shares outstanding   | 17,618,481                | 17,471,550      | 17,673,759              | 17,153,196      |
| Basic income (loss) per share:                                 |                           |                 |                         |                 |
| Continuing operations  | \$ 0.04                   | \$ 0.02         | \$ 0.17                 | \$ 0.09         |
| Discontinued operations  | \$ 0.00                   | \$ (0.05)       | \$ 0.00                 | \$ (0.05)       |
| Net income (loss) per share                                    | \$ 0.04                   | \$ (0.03)       | \$ 0.17                 | \$ 0.04         |
| Diluted income (loss) per share:                               |                           |                 |                         |                 |
| Continuing operations  | \$ 0.04                   | \$ 0.02         | \$ 0.16                 | \$ 0.09         |
| Discontinued operations  | \$ 0.00                   | \$ (0.05)       | \$ 0.00                 | \$ (0.05)       |
| Net income (loss) per share                                    | \$ 0.04                   | \$ (0.03)       | \$ 0.16                 | \$ 0.04         |



**Table of Contents****5) Comprehensive Income (Loss)**

The components of comprehensive income (loss) for the three and six month periods ended July 3, 2011 and July 4, 2010 are as follows (amounts in thousands):

|   | Three month periods ended |                 | Six month periods ended |                 |
|---|---------------------------|-----------------|-------------------------|-----------------|
|   | July 3,<br>2011           | July 4,<br>2010 | July 3,<br>2011         | July 4,<br>2010 |
| Net income (loss) attributable to controlling interest              | \$ 654                    | \$ (516)        | \$ 2,810                | \$ 691          |
| Other comprehensive income (loss):                                  |                           |                 |                         |                 |
| Foreign currency translation  | 44                        | (28)            | 203                     | (28)            |
| Comprehensive income (loss) attributable to controlling interest    | 698                       | (544)           | 3,013                   | 663             |
| Comprehensive income (loss) attributable to noncontrolling interest | 84                        | (147)           | 103                     | (113)           |
| Comprehensive income (loss)   | \$ 782                    | \$ (691)        | \$ 3,116                | \$ 550          |

**6) Stock Based Compensation**

Prior to the IPO, the Company adopted the 2006 MRG Stock Incentive Plan (the "equity incentive plan"). The equity incentive plan provides for the grant of stock options and stock appreciation rights and for awards of shares, restricted shares, restricted stock units and other equity-based awards to employees, officers, directors or consultants. As of July 3, 2011, the aggregate number of shares of the Company's common stock approved for grant under the equity incentive plan was 1,789,000 shares. If an award granted under the equity incentive plan terminates, lapses or is forfeited before the vesting of the related shares, those shares will again be available to be granted. During the six month period ended July 3, 2011, the Company granted and issued the following shares of restricted stock to certain of its employees and directors pursuant to the equity incentive plan:

| Date of Grant    | Number of<br>Shares Granted | Stock Price on<br>Grant Date |
|------------------|-----------------------------|------------------------------|
| January 25, 2011 | 264,850                     | \$ 6.62                      |
| May 19, 2011     | 1,500                       | \$ 7.45                      |

Activity relating to the shares of restricted stock granted pursuant to the equity incentive plan during the six month period ended July 3, 2011 was as follows:

|   | Number of<br>Shares |
|---|---------------------|
| Unvested restricted stock outstanding as of January 2, 2011       | 673,200             |
| Granted at a weighted average price of \$6.62 per share           | 266,350             |
| Vested with 50,212 shares surrendered in lieu of paying taxes (a) | (196,380)           |
| Forfeited by termination  | (15,240)            |
| Unvested restricted stock outstanding as of July 3, 2011          | 727,930             |

(a) In connection with the vesting of shares, certain employees elected to pay the employee minimum income taxes by surrendering shares in lieu of paying the taxes in cash. Such surrendered shares were cancelled by the Company.

As of July 3, 2011, there were 395,190 shares available for grant pursuant to the equity incentive plan.



**Table of Contents**

In accordance with ASC Topic 718, *Compensation - Stock Compensation*, stock-based compensation is measured at the grant date based on the calculated fair value of the award, and is recognized as an expense over the requisite employee service period (generally the vesting period of the grant). The Company recognized stock-based compensation for awards issued under the equity incentive plan in the following line items in the consolidated statements of operations (amounts in thousands):

|                                     | Three month periods ended |                 | Six month periods ended |                 |
|-------------------------------------|---------------------------|-----------------|-------------------------|-----------------|
|                                     | July 3,<br>2011           | July 4,<br>2010 | July 3,<br>2011         | July 4,<br>2010 |
| Restaurant operating expenses       | \$ 81                     | \$ 98           | \$ 191                  | \$ 188          |
| General and administrative expenses | 272                       | 415             | 457                     | 799             |
| Marketing and promotional expenses  | 17                        | 16              | 41                      | 33              |
| Net compensation expense            | 370                       | 529             | 689                     | 1,020           |

As of July 3, 2011, total remaining unrecognized compensation expense related to unvested stock-based payment awards, net of estimated forfeitures, was approximately \$3.2 million, which will be recognized over a weighted average period of approximately 3.4 years.

**7) Financial Information about Geographic Areas**

As of July 3, 2011, the Company owned and operated 77 Morton's steakhouses, including 71 domestic restaurants located in 64 cities across 26 states and San Juan, Puerto Rico, and 6 international locations (Toronto, Canada; Hong Kong, China; Macau, China; Shanghai, China; Mexico City, Mexico and Singapore), as well as Trevi, our Italian restaurant, which is located next to the Fountain of the Gods at The Forum Shops at Caesars Palace in Las Vegas, NV.

Income before income taxes from continuing operations for the Company's domestic and foreign operations are as follows (amounts in thousands):

|  | Three month periods ended |                 | Six month periods ended |                 |
|--|---------------------------|-----------------|-------------------------|-----------------|
|  | July 3,<br>2011           | July 4,<br>2010 | July 3,<br>2011         | July 4,<br>2010 |
| Domestic (72 restaurants at July 3, 2011 and July 4, 2010)                   | \$ (510)                  | \$ (412)        | \$ 881                  | \$ 362          |
| Foreign (6 and 5 restaurants at July 3, 2011 and July 4, 2010, respectively) | 1,496                     | 544             | 2,856                   | 1,457           |
| Total  | \$ 986                    | \$ 132          | \$ 3,737                | \$ 1,819        |

Domestic income before income taxes from continuing operations includes certain corporate expenses and other charges that relate to our U.S. based headquarters, and are included in domestic operations but not allocated to the foreign operations. A \$0.2 million charge relating to professional fees associated with the previously announced exploration of strategic alternatives is included in the domestic income before income taxes from continuing operations for the three month period ended July 3, 2011. A \$0.9 million charge relating to the settlement of certain wage and hour and similar labor claims as well as relating to professional fees associated with the previously announced exploration of strategic alternatives is included in the domestic income before income taxes from continuing operations for the six month period ended July 3, 2011. The charge related to the legal settlements of approximately \$0.5 million is included in the domestic income before income taxes from continuing operations for the six month period ended July 4, 2010.



**Table of Contents****8) Long-Term Debt**

Long-term debt as of July 3, 2011 and January 2, 2011 consisted of the following (amounts in thousands):

|   | July 3,<br>2011  | January 2,<br>2011 |
|---|------------------|--------------------|
| Senior credit facility (a)                    | \$ 56,838        | \$ 55,600          |
| Mortgage loan (b)                             | 2,806            | 2,893              |
| Joint venture loans payable (c)               | 7,557            | 7,371              |
| Non-recourse loan (d)                         | 1,638            | 1,638              |
| <b>Total long-term debt</b>                   | <b>68,839</b>    | <b>67,502</b>      |
| Less: Current portion                         | 3,880            | 3,871              |
| <b>Long-term debt, net of current portion</b> | <b>\$ 64,959</b> | <b>\$ 63,631</b>   |

*(a) Senior Credit Facility**Goldman Sachs Bank*

On December 9, 2010, the Company entered into a new five-year \$70.0 million senior credit facility with Goldman Sachs Bank USA ( Goldman Sachs ) which includes a \$60.0 million principal amount senior term loan and \$10.0 million aggregate principal amount of revolving commitments ( Senior Credit Facility ). The Senior Credit Facility matures on December 8, 2015. The Company's wholly-owned subsidiary, Morton's of Chicago, Inc. ( Morton's of Chicago ), is the borrower under the facility and most of its domestic subsidiaries are guarantors. As of July 3, 2011, the Company had outstanding borrowings of approximately \$54.7 million under the senior term loan and \$2.1 million under the revolver, and was in compliance with all of its financial covenants. Management believes that the carrying value of the outstanding borrowings approximate fair value since interest rates vary with market conditions.

Subject to customary conditions, including the absence of default under the Senior Credit Facility, all of the \$10.0 million available under the revolving commitments may be borrowed, repaid and reborrowed, as applicable, until the maturity date thereof. The Company is required to make scheduled installment payments on the senior term loan periodically and any additional voluntary payments reduce these scheduled installment payments on a pro-rata basis. The scheduled payments of \$3.7 million, which are due within 12 months of the most recent balance sheet date, are included in Current portion of long-term debt on the consolidated balance sheet. In addition, we are also subject to certain mandatory prepayments determined by certain conditions of the Senior Credit Facility.

Loans made under the Senior Credit Facility bear interest, at the borrower's option, at a rate per annum equal to either a Base Rate or an Adjusted LIBOR Rate, in each case plus an applicable margin. The applicable margin is 5.50% for Adjusted LIBOR Rate loans and 4.50% for Base Rate loans until delivery of our financial statements for the fiscal year ending January 1, 2012, and after that the applicable margin for Adjusted LIBOR Rate loans ranges from 4.50% to 5.50% and the applicable margin for the Base Rate loans ranges from 3.50% to 4.50%, in each case, based on our senior leverage ratio. The Adjusted LIBOR Rate is subject to a floor of 1.75% and the Base Rate is subject to a floor of 4.75%. The Base Rate is a rate per annum equal to the greater of (i) the rate of interest quoted in *The Wall Street Journal*, Money Rates Section as the Prime Rate as in effect from time-to-time and (ii) the federal funds rate plus 0.50% per annum.

The Senior Credit Facility contains various affirmative and negative covenants customary for similar credit facilities. The affirmative covenants include, but are not limited to: delivery of financial statements, maintenance of existence, payment of taxes, maintenance of properties and insurance, and compliance with laws. The negative covenants include, but are not limited to: limitations on indebtedness, liens, negative pledges, restricted payments, investments, disposition of assets, acquisitions, sales and lease-backs and transactions with affiliates. Notwithstanding the limitation on restricted payments, the Company will be permitted to redeem or repurchase its preferred securities.

## **Table of Contents**

With respect to the Senior Credit Facility, we are required to comply with a minimum fixed charge coverage ratio of 1.15:1.00 and a maximum senior leverage ratio that ranges from 1.75:1.00 to 2.75:1.00 based on the fiscal year, among various other covenants.

The Senior Credit Facility contains events of default (subject to exceptions, thresholds and grace periods), including, without limitation, for: (i) nonpayment of principal or interest; (ii) failure to perform or comply with covenants; (iii) breaches of representations and warranties; (iv) cross-defaults with certain other indebtedness; (v) certain bankruptcy related events (subject to limited exceptions for certain inactive subsidiaries or operating subsidiaries which cease operations); (vi) impairment of security interests in collateral; (vii) invalidity of guarantees; (viii) monetary judgment defaults; and (ix) certain ERISA matters. Other than in respect of a bankruptcy related event of default, which would result in the automatic and immediate requirement to repay all borrowings and other amounts due, if an event of default occurs the lenders would be entitled to require the immediate repayment of all borrowings and other amounts due under the facility and to seize and sell the collateral pledged to secure the borrowings and other obligations under the facility.

### *(b) Mortgage loan*

During fiscal 2011, one of the Company's subsidiaries entered into a mortgage loan with GE Capital Franchise Finance aggregating \$4.0 million with an interest rate of 8.98% per annum, the proceeds of which were used to fund the purchase of land and construction of a restaurant. On both July 3, 2011 and January 2, 2011, the aggregate outstanding principal balance due on this mortgage loan was approximately \$2.8 million, of which approximately \$0.2 million of principal is included in Current portion of long-term debt in the accompanying consolidated balance sheets. The mortgage loan is scheduled to mature in March 2021. As of July 3, 2011, the Company was in compliance with all of the financial covenants of this mortgage loan.

### *(c) Joint Venture Loans Payable*

Also included in the consolidated balance sheets as of July 3, 2011 and January 2, 2011, are liabilities related to variable interest entities (See Note 9) consisting of loans for the Company's Mexico City and Shanghai restaurants totaling \$7.6 million and \$7.4 million, respectively. The proceeds of the loans were used to fund construction of the respective restaurants, pre-opening costs and initial operating expenses. These loans are treated as debt of the joint ventures. The loan related to Mexico City is repayable without interest while the loan related to Shanghai requires simple interest to be accrued at an annual interest rate of 2%.

### *(d) Non-recourse loan*

On April 13, 2009, one of the Company's subsidiaries entered into an agreement with Crown at Miami Beach, LTD, pursuant to which that subsidiary borrowed \$1.6 million, which is still outstanding as of July 3, 2011. Loan proceeds were used solely for costs incurred in connection with the construction and opening of the restaurant located in Miami Beach, FL, including for the acquisition and installation of furniture, fixtures and equipment. The loan bears interest at 8.0% and matures on October 1, 2014 at which time a balloon payment of the total principal outstanding is due.

**Table of Contents****9) Consolidation of Variable Interest Entities (Joint Ventures)**

The Company operates Morton's steakhouses in Mexico City, Mexico and in Shanghai, China in which the Company has variable interests. The accounts of these variable interest entities (VIEs) have been included in the Company's consolidated financial statements due to the fact that the Company is the primary beneficiary in the VIEs. The liabilities recognized as a result of consolidating the VIEs do not represent an additional claim on the Company's general assets but rather each loan represents a claim against the specific assets of each consolidated VIE. Conversely, assets recognized as a result of consolidating the VIEs do not represent additional assets that could be used to satisfy claims against the Company's general assets.

The Company determined it is the primary beneficiary of the two VIEs as the Company is responsible for the day-to-day management and operation of the restaurants, including new menu selection and pricing. These activities were determined to most significantly impact the economic performance of the VIEs. Upon repayment of the outstanding loans, profits from the VIEs will be distributed to the owners in proportion to their ownership interests. The Company is not involved in any VIEs other than those discussed above. The amounts set forth in the table below were included in the Company's consolidated balance sheets related to the VIEs (amounts in thousands):

|                             | July 3,<br>2011 | January 2,<br>2011 |
|-----------------------------|-----------------|--------------------|
| Restricted cash             | \$ 615          | \$ 805             |
| Total assets                | 6,839           | 6,942              |
| Joint venture loans payable | 7,557           | 7,371              |

**10) Restaurant Activity**

During the six month period ended July 3, 2011, the Company opened a new Morton's steakhouse in the Uptown area of Dallas, TX, which also includes a Bar 12-21 and have entered into a lease to open a new Morton's steakhouse in the Tyson's Corner area of Vienna, VA.

**11) Discontinued Operations**

The Company accounts for closed restaurants as discontinued operations in accordance with ASC Topic 360, *Property, Plant and Equipment*, due to the fact that the Company does not expect any further direct or indirect cash flows from these restaurants. Accordingly, the results of closed restaurants are included in discontinued operations for all periods presented in the accompanying consolidated financial statements. The results of discontinued operations were as follows (amounts in thousands):

|                          | Three month periods ended |                 | Six month periods ended |                 |
|--------------------------|---------------------------|-----------------|-------------------------|-----------------|
|                          | July 3,<br>2011           | July 4,<br>2010 | July 3,<br>2011         | July 4,<br>2010 |
| Revenues                 | \$                        | \$              | \$                      | \$              |
| Loss before income taxes |                           | (789)           |                         | (803)           |
| Income tax benefit       |                           |                 |                         |                 |
| Net loss                 | \$                        | \$ (789)        | \$                      | \$ (803)        |

**12) Legal Matters and Contingencies**

The Company records legal fees and accruals in accordance with ASC Topic 450, *Contingencies*. A liability is recorded when it is probable and the amount can be reasonably estimated. The Company's accounting policy is to accrue estimated legal defense costs under ASC Topic 450.

## **Table of Contents**

In February 2010, two former employees of the San Diego Morton's steakhouse filed a class action complaint against Morton's of Chicago/San Diego, Inc. in the Superior Court of the State of California for the County of San Diego, alleging certain violations of the California Labor Code and the California Unfair Competition Law for failure to provide meal and rest breaks, failure to pay overtime and failure to provide employees with accurate wage statements. The plaintiffs were seeking recovery of statutory penalties, unpaid wages and overtime, as well as injunctive and declaratory relief and attorneys' fees and costs. On January 7, 2011, the Company's partial motion for summary judgment was granted and the plaintiffs' claims for failure to provide rest periods and failure to provide employees with accurate wage statements were dismissed. In addition, on February 18, 2011, the court denied plaintiffs' motion for class certification. In May 2011, a settlement and release agreement was entered into by the parties resolving this matter.

In August 2010, a former employee of the Costa Mesa Morton's steakhouse filed a state-wide class action complaint against Morton's of Chicago in the Superior Court of the State of California for the County of Los Angeles, alleging certain violations of the California Labor Code and the California Unfair Competition Law for failure to provide meal and rest breaks, failure to pay overtime and failure to provide employees with accurate wage statements as a result of the classification of California-based Assistant Managers and Day Managers as salaried exempt. The plaintiff is seeking recovery of statutory penalties, unpaid wages and overtime, as well as injunctive and declaratory relief and attorneys' fees and costs. The Company is contesting this matter vigorously. In September 2010, the Company removed the case to Federal court and the plaintiff subsequently filed a motion to remand. On January 26, 2011, the plaintiff's motion to remand was denied. In addition, on June 13, 2011, the court denied plaintiffs' motion for class certification. A jury trial is scheduled for January 2012. The plaintiff in this matter has not stated the amount of damages sought and, at this stage of the proceedings, it is not possible to state the estimated damages sought by the plaintiff.

The Company is involved in various other claims and legal actions, including claims and legal actions by landlords, arising in the ordinary course of business. The Company does not believe that the ultimate resolution of these actions will have a material adverse effect on the Company's financial condition.

### **13) Subsequent Events**

We evaluated all of our activity through the issue date of these financial statements and concluded that no subsequent events have occurred that would require recognition in the financial statements or disclosure in the Notes to Unaudited Consolidated Financial Statements.

## Table of Contents

### **Item 2. Management's Discussion and Analysis of Financial Condition and Results of Operations**

This discussion should be read in conjunction with the Consolidated Financial Statements and accompanying notes in Item 1 of this Quarterly Report on Form 10-Q and with our Annual Report on Form 10-K for the fiscal year ended January 2, 2011.

#### Overview

Many parts of the world including the United States have been in, or are recovering from, a recession and despite the recent increases in comparable sales we have experienced, we believe that weak general economic conditions could continue through the rest of 2011 and possibly beyond. The ongoing impact of the housing crisis and high unemployment may further exacerbate current economic conditions. We continue to experience many of the same challenges our partners and competitors in the industry are facing. As a result of these economic conditions, our guests may become more apprehensive about the economy and/or related factors, and may reduce their level of discretionary spending. A decrease in spending due to lower consumer discretionary income or consumer confidence caused by uncertainty in the current state of the global economy could impact the frequency with which our guests choose to dine out or the amount they spend on meals while dining out, thereby decreasing our revenues and negatively affecting our operating results.

#### Results of Operations

##### ***Three Month Period Ended July 3, 2011 (13 weeks) compared to Three Month Period Ended July 4, 2010 (13 weeks)***

Our income from continuing operations attributable to controlling interest for the three month period ended July 3, 2011 was \$0.7 million compared to \$0.3 million for the three month period ended July 4, 2010. The change is primarily due to an increase in comparable restaurant revenues, net of related food and beverage and restaurant operating costs. For purposes of this discussion, comparable restaurants refer to Morton's steakhouses open for all of fiscal 2010 and the six month period ended July 3, 2011.

Revenues increased \$7.5 million, or 10.7%, to \$78.0 million for the three month period ended July 3, 2011, from \$70.5 million for the three month period ended July 4, 2010. Revenues increased \$5.6 million, or 8.2%, due to an increase in revenues from comparable restaurants. Revenues increased \$1.8 million due to the opening of our Shanghai restaurant in fiscal 2010. Revenues increased \$0.1 million due to a net increase in revenues from our Trevi restaurant and other revenues.

Average revenue per restaurant open all of either period being compared increased 9.6%. Revenues for the three month period ended July 3, 2011 also reflect the impact of menu price increases of 1.2% in June 2010, 1.0% in July 2010, 2.7% in December 2010 and 0.9% in January 2011 at our Morton's steakhouses.

Food and beverage costs increased \$2.5 million, or 11.5%, to \$24.0 million for the three month period ended July 3, 2011, from \$21.5 million for the three month period ended July 4, 2010. The increase was directly related to the increase in sales as well as higher beef and other food costs as compared to the prior year period. Food and beverage costs as a percentage of revenues increased to 30.7% for the three month period ended July 3, 2011, from 30.5% for the three month period ended July 4, 2010. This increase was primarily due to the impact of higher beef and other food costs, partially offset by menu price increases when compared to the three month period ended July 4, 2010.

## Table of Contents

Restaurant operating expenses, which include labor, occupancy and other operating expenses, increased \$3.1 million, or 7.8%, to \$42.4 million for the three month period ended July 3, 2011, from \$39.3 million for the three month period ended July 4, 2010. This increase was primarily due to an increase in salaries, wages and other benefits, increased credit card commissions related to increased sales volume and costs due to the opening of our Shanghai restaurant in October of 2010. Included in the three month periods ended July 3, 2011 and July 4, 2010 is a non-cash straight line rent expense (income) of \$(0.1) million and \$0.1 million, respectively. Restaurant operating expenses as a percentage of revenues decreased to 54.4% for the three month period ended July 3, 2011, from 55.8% for the three month period ended July 4, 2010. This decrease was primarily due to the leveraging effect on the fixed cost base caused by positive comparable restaurant revenues.

Pre-opening costs decreased \$0.2 million to \$0.1 million for the three month period ended July 3, 2011, from \$0.3 million for the three month period ended July 4, 2010. We expense all costs incurred during restaurant start-up activities, including training, travel and legal, among other costs. The number of restaurants opened, the timing of restaurant openings and the costs per restaurant opened affected the amount of these costs.

Depreciation and amortization increased \$0.2 million, or 7.5%, to \$2.7 million for the three month period ended July 3, 2011, from \$2.5 million for the three month period ended July 4, 2010. This increase was due to depreciation and amortization relating to our Shanghai restaurant, which opened in October 2010, and capital expenditures related to renovations to existing restaurants.

General and administrative expenses increased \$0.9 million, or 24.2%, to \$4.8 million for the three month period ended July 3, 2011, from \$3.8 million for the three month period ended July 4, 2010. General and administrative expenses as a percentage of revenues increased to 6.1% for the three month period ended July 3, 2011, from 5.4% for the three month period ended July 4, 2010. These increases were primarily due to increased legal costs associated with various matters and professional fees associated with the previously announced exploration of strategic alternatives.

Marketing and promotional expenses decreased \$0.2 million, or 9.8%, to \$1.7 million for the three month period ended July 3, 2011, from \$1.9 million for the three month period ended July 4, 2010. Marketing and promotional expenses as a percentage of revenues decreased 0.5% to 2.2% for the three month period ended July 3, 2011, from 2.7% during the three month period ended July 4, 2010.

Interest expense, net increased \$0.4 million, or 45.6%, to \$1.3 million for the three month period ended July 3, 2011, from \$0.9 million for the three month period ended July 4, 2010. This increase was primarily due to the higher interest rates charged on the Company's new credit facility that was entered into on December 9, 2010, when compared to the rates on the prior credit facility that were effective during the three month period ended July 4, 2010. Interest income for the three month periods ended July 3, 2011 and July 4, 2010 was insignificant.

Provision for income taxes consisted of income tax expense of \$0.2 million and \$6,000 for the three month periods ended July 3, 2011 and July 4, 2010, respectively. Our effective tax rate was 25.2% and 4.5% for the three month periods ended July 3, 2011 and July 4, 2010, respectively.

Net income attributable to noncontrolling interest of \$0.1 million for the three month period ended July 3, 2011 consists of our partners' 49.99% share of the net income (loss) of the Morton's steakhouses located in Mexico City, Mexico and Shanghai, China. This compares to a net loss attributable to noncontrolling interest of \$0.1 million for the three month period ended July 4, 2010, consisting of our partners' 49.99% share of the net income (loss) of the Morton's steakhouse located in Mexico City, Mexico and the startup costs for our Shanghai restaurant which opened in October of 2010.

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**Table of Contents**

***Six Month Period Ended July 3, 2011 (26 weeks) compared to Six Month Period Ended July 4, 2010 (26 weeks)***

Our income from continuing operations attributable to controlling interest for the six month period ended July 3, 2011 was \$2.8 million compared to \$1.5 million for the six month period ended July 4, 2010. The change is primarily due to an increase in comparable restaurant revenues, net of related food and beverage and restaurant operating costs. For purposes of this discussion, comparable restaurants refer to Morton's steakhouses open for all of fiscal 2010 and the six month period ended July 3, 2011.

Revenues increased \$14.7 million, or 10.1%, to \$160.5 million for the six month period ended July 3, 2011, from \$145.8 million for the six month period ended July 4, 2010. Revenues increased \$11.0 million, or 7.8%, due to an increase in revenues from comparable restaurants. Revenues increased \$3.2 million due to the opening of our Shanghai restaurant in fiscal 2010. Revenues increased \$0.5 million due to a net increase in revenues from our Trevi restaurant and other revenues.

Average revenue per restaurant open all of either period being compared increased 8.9%. Revenues for the six month period ended July 3, 2011 also reflect the impact of menu price increases of 1.2% in June 2010, 1.0% in July 2010, 2.7% in December 2010 and 0.9% in January 2011 at our Morton's steakhouses.

Food and beverage costs increased \$5.4 million, or 12.3%, to \$49.6 million for the six month period ended July 3, 2011, from \$44.1 million for the six month period ended July 4, 2010. The increase was directly related to the increase in sales as well as higher beef and other food costs as compared to the prior year period. Food and beverage costs as a percentage of revenues increased to 30.9% for the six month period ended July 3, 2011, from 30.3% for the six month period ended July 4, 2010. This increase was primarily due to the impact of higher beef and other food costs, partially offset by menu price increases when compared to the six month period ended July 4, 2010.

Restaurant operating expenses, which include labor, occupancy and other operating expenses, increased \$4.7 million, or 5.8%, to \$85.3 million for the six month period ended July 3, 2011, from \$80.6 million for the six month period ended July 4, 2010. This increase was primarily due to an increase in salaries, wages and other benefits, increased credit card commissions and increased costs due to the opening of our Shanghai restaurant during fiscal 2010. Included in the six month periods ended July 3, 2011 and July 4, 2010 is non-cash straight line rent expense (income) of \$(0.2) million and \$0.2 million, respectively. Restaurant operating expenses as a percentage of revenues decreased to 53.1% for the six month period ended July 3, 2011, from 55.3% for the six month period ended July 4, 2010. This decrease was primarily due to the leveraging effect on the fixed cost base caused by positive comparable restaurant revenues.

Pre-opening costs remained consistent with the prior year at \$0.4 million for the six month periods ended July 3, 2011 and July 4, 2010. We expense all costs incurred during restaurant start-up activities, including training, travel and legal, among other costs. The number of restaurants opened, the timing of restaurant openings and the costs per restaurant opened affected the amount of these costs.

Depreciation and amortization increased \$0.4 million, or 7.0%, to \$5.4 million for the six month period ended July 3, 2011, from \$5.0 million for the six month period ended July 4, 2010. This increase was due to depreciation and amortization relating to our Shanghai restaurant, which opened in October 2010, and capital expenditures related to renovations to existing restaurants.

General and administrative expenses increased \$1.7 million, or 20.9%, to \$9.8 million for the six month period ended July 3, 2011, from \$8.1 million for the six month period ended July 4, 2010. General and administrative expenses as a percentage of revenues increased to 6.1% for the six month period ended July 3, 2011, from 5.5% for the six month period ended July 4, 2010. These increases were primarily due to increased legal costs associated with various matters and professional fees associated with the previously announced exploration of strategic alternatives.

## Table of Contents

Marketing and promotional expenses decreased \$0.1 million, or 1.7%, to \$3.2 million for the six month period ended July 3, 2011, from \$3.3 million for the six month period ended July 4, 2010. Marketing and promotional expenses as a percentage of revenues decreased 0.3% to 2.0% for the six month period ended July 3, 2011, from 2.3% during the six month period ended July 4, 2010.

Charge related to legal settlements of \$0.5 million for the six month period ended July 3, 2011 relates to the settlement of certain wage and hour and similar labor claims. Charge related to legal settlements of \$0.5 million for the six month period ended July 4, 2010 relates to the change in the fair value of the Company's Preferred Stock issued in February 2010 in connection with the fiscal 2009 settlement of certain wage and hour litigation. The charge represents the final adjustment to the fair value of the Preferred Stock as of the January 28, 2010 court approval date. The fair value of the Preferred Stock issued in the settlement was calculated based on market conditions at the time of issuance using a Black-Scholes option pricing model.

Interest expense, net increased \$0.8 million, or 43.3%, to \$2.7 million for the six month period ended July 3, 2011, from \$1.9 million for the six month period ended July 4, 2010. This increase was primarily due to the higher interest rates charged on the Company's new credit facility that was entered into on December 9, 2010, when compared to the rates on the prior credit facility that was effective during the six month period ended July 4, 2010. Interest income for the six month periods ended July 3, 2011 and July 4, 2010 was insignificant.

Provision for income taxes consisted of income tax expense of \$0.8 million and \$0.4 million for the six month periods ended July 3, 2011 and July 4, 2010, respectively. Our effective tax rate was 22.1% and 24.1% for the six month periods ended July 3, 2011 and July 4, 2010, respectively.

Net income attributable to noncontrolling interest of \$0.1 million for the six month period ended July 3, 2011 consists of our partners' 49.99% share of the net income (loss) of the Morton's steakhouses located in Mexico City, Mexico and Shanghai, China. This compares to a net loss attributable to noncontrolling interest of \$0.1 million for the six month period ended July 4, 2010, consisting of our partners' 49.99% share of the net income (loss) of the Morton's steakhouse located in Mexico City, Mexico and the startup costs for our Shanghai Steakhouse which opened later in fiscal 2010.

## Liquidity and Capital Resources

Our principal liquidity requirements are to meet our lease obligations and our working capital and capital expenditure needs and to pay principal and interest on our debt. Subject to our operating performance, which, if significantly adversely affected, would negatively affect the availability of funds, we expect to finance our operations for fiscal 2011 through cash provided by operations and borrowings available under our Senior Credit Facility. In addition, we rely to a significant degree on landlord development allowances and/or loans as a means of financing the costs of opening new restaurants, and any substantial reduction in the amount of those landlord development allowances and/or loans could adversely affect our liquidity. We had cash and cash equivalents of \$1.2 million as of July 3, 2011 and January 2, 2011.

Based on our current projections, we believe that our cash and cash equivalents and cash flow from operations will be sufficient to meet our working capital and investment requirements and our debt service obligations for the next twelve months. If available liquidity is not sufficient to meet these requirements and obligations as they come due, our plans include reducing expenditures as necessary in order to meet our cash requirements. However, there can be no assurance that any such reductions in expenditures would be sufficient to enable us to meet our cash requirement needs.



## **Table of Contents**

### *Working Capital and Cash Flows*

As of July 3, 2011, we had, and in the future we may have, negative working capital balances. Our operations have not required significant working capital and, like many restaurant companies, we have been able to operate with negative working capital since our restaurant guests pay for their food and beverage purchases in cash or by credit card at the time of sale, and we are able to sell many of our food inventory items before payment is due to our suppliers. Our receivables primarily represent amounts due from credit card processors, which arise when customers pay by credit card, and are included in Accounts Receivable in our consolidated balance sheets. We receive trade credit based upon negotiated terms in purchasing food and supplies. Funds available from cash sales not needed immediately to pay for food and supplies or to finance receivables or inventories have typically been used for capital expenditures and/or to repay debt.

### *Operating Activities*

Cash provided by operating activities for the six month period ended July 3, 2011 was \$4.3 million and primarily consisted of net income of \$2.9 million that included non-cash depreciation, amortization and other non-cash charges of \$6.4 million, which was offset by cash outflows primarily for the payment of accounts payable and accrued expenses, as well as other changes in assets and liabilities, of \$5.0 million. The improvement in cash flow from operations over the prior year period was due to higher net income and lower cash required for working capital items.

### *Investing Activities*

Cash used in investing activities for the six month period ended July 3, 2011 was \$5.4 million and consisted of purchases of property and equipment.

### *Financing Activities*

Cash provided by financing activities for the six month period ended July 3, 2011 was \$0.6 million and primarily consisted of proceeds from net borrowings under our Senior Credit Facility of \$1.2 million, partially offset by cash used for the payment of minimum income taxes relating to shares vested and surrendered by employees and other financing uses of cash of \$0.6 million.

### *Contractual Commitments*

#### *Restaurant Operating Leases*

Our lease obligations include certain restaurant operating leases for which we, or one of our subsidiaries, guarantee for a portion of the lease term, the performance of the lease by the subsidiary operating company that is a party thereto.

**Table of Contents**

See Note 8 Long-Term Debt in the Notes to Consolidated Financial Statements in Part I, Item 1 of this report for a discussion of our debt obligations. The following table represents our contractual commitments associated with our debt, lease and other obligations as of July 3, 2011 (amounts in thousands):

|  | 2011             | 2012             | 2013             | 2014             | 2015             | Thereafter        | Total             |
|--|------------------|------------------|------------------|------------------|------------------|-------------------|-------------------|
| Senior credit facility                 | \$ 2,831         | \$ 4,892         | \$ 5,538         | \$ 5,538         | \$ 38,039        | \$                | \$ 56,838         |
| Interest on senior credit facility (a) | 2,053            | 3,535            | 3,190            | 2,823            | 2,336            |                   | 13,937            |
| Mortgage loan                          | 92               | 196              | 215              | 235              | 257              | 1,811             | 2,806             |
| Interest on mortgage loan (a)          | 126              | 239              | 220              | 200              | 178              | 474               | 1,437             |
| JV Loans Payable                       | 1,165            | 1,885            | 1,900            | 938              | 440              | 1,229             | 7,557             |
| Interest on JV loans payable (a)       | 79               | 55               | 25               | 5                |                  |                   | 164               |
| Non-recourse loan                      |                  |                  |                  | 1,638            |                  |                   | 1,638             |
| Interest on non-recourse loan (a)      | 66               | 131              | 131              | 98               |                  |                   | 426               |
| <b>Subtotal</b>                        | <b>6,412</b>     | <b>10,933</b>    | <b>11,219</b>    | <b>11,475</b>    | <b>41,250</b>    | <b>3,514</b>      | <b>84,803</b>     |
| Operating leases                       | 13,764           | 29,259           | 30,097           | 29,757           | 27,916           | 143,364           | 274,157           |
| Legal settlements                      | 1,190            | 1,883            | 1,600            |                  |                  |                   | 4,673             |
| Purchase commitments                   | 11,094           |                  |                  |                  |                  |                   | 11,094            |
| <b>Total</b>                           | <b>\$ 32,460</b> | <b>\$ 42,075</b> | <b>\$ 42,916</b> | <b>\$ 41,232</b> | <b>\$ 69,166</b> | <b>\$ 146,878</b> | <b>\$ 374,727</b> |

(a) Interest is based on borrowings as of July 3, 2011 and interest rates as of July 28, 2011.

*Capital Expenditures*

During the first six months of fiscal 2011, our expenditures for fixed assets and related investment costs, plus pre-opening costs, approximated \$5.8 million. We estimate that we will expend up to an aggregate of \$7.9 million in fiscal 2011 for fixed assets and related investment costs, including pre-opening costs of approximately \$0.4 million, for the relocation of one restaurant, ordinary refurbishment of existing restaurants and to remodel the bar area in selected restaurants to include our Bar 12 21 concept. Cash capital expenditures in fiscal 2011 are expected to be reduced by landlord contributions of approximately \$0.1 million. We anticipate that funds generated through operations and through borrowings under our Senior Credit Facility, together with landlord contributions, will be sufficient to fund these currently planned expenditures through the end of fiscal 2011. We cannot be sure, however, that this will be the case.

## **Table of Contents**

### **Item 3. Quantitative and Qualitative Disclosures about Market Risk**

The inherent risk in market risk sensitive instruments and positions primarily relates to the potential for losses arising from adverse changes in foreign currency exchange rates, interest rates and beef and other food product prices.

As of July 3, 2011, we owned and operated six international restaurants, one each in Hong Kong, China; Macau, China; Shanghai, China; Mexico City, Mexico; Singapore; and Toronto, Canada. As a result, we are subject to risk from changes in foreign exchange rates. The cash flow risk associated with these rate changes is largely mitigated by the fact that both revenues and expenses of these locations are denominated in the local currency, which is also the functional currency. However, these changes result in cumulative translation adjustments, which are included in accumulated other comprehensive income. We do not consider the potential loss resulting from a hypothetical 10% adverse change in quoted foreign currency exchange rates, as of July 3, 2011, to be material.

We also are subject to market risk from exposure to changes in interest rates based on our financing activities. This exposure relates to borrowings under our Senior Credit Facility that are payable at floating rates of interest. Our other indebtedness, including our mortgage, non-recourse loan and joint venture loans, are payable at fixed rates of interest. As of July 3, 2011, there were borrowings outstanding under our floating rate Senior Credit Facility of \$56.8 million. As a result, a hypothetical 10% fluctuation in interest rates would have an impact of approximately \$0.4 million on pre-tax earnings for the six month period ended July 3, 2011.

We are exposed to market price fluctuations in beef and other food product prices. Given the historical volatility of beef and other food product prices, this exposure can impact our food and beverage costs. Since we typically set our menu prices in advance of our beef and other food product purchases, we cannot quickly take into account changing costs of beef and other food items. To the extent that we are unable to pass the increased costs on to our guests through price increases, our results of operations would be adversely affected. To manage this risk in part, we attempt to enter into fixed price purchase commitments. We currently do not use financial instruments to hedge our risk to market price fluctuations in beef or other food product prices. As a result, a hypothetical 10% fluctuation in beef costs would have an impact of approximately \$2.2 million on pre-tax earnings for the six month period ended July 3, 2011.

### **Item 4. Controls and Procedures**

The Company maintains disclosure controls and procedures (as defined in Rule 13a-15(e) of the Securities Exchange Act) designed to provide reasonable assurance that the information required to be disclosed by the Company in the reports that it files or submits under the Exchange Act is recorded, processed, summarized, and reported within the time periods specified in the Securities and Exchange Commission's rules and forms. These include, without limitation, controls and procedures designed to ensure that this information is accumulated and communicated to the Company's management, including its Chief Executive Officer and Chief Financial Officer, as appropriate to allow timely decisions regarding required disclosure. Management, with the participation of the Chief Executive and Chief Financial Officers, conducted an evaluation of the effectiveness of the design and operation of the Company's disclosure controls and procedures as of July 3, 2011. Based on this evaluation, the Company's Chief Executive Officer and Chief Financial Officer have concluded that the Company's disclosure controls and procedures were effective as of July 3, 2011 at the reasonable assurance level. No changes were made in our internal controls or in other factors that could significantly affect these controls subsequent to the date of their evaluation.

**Table of Contents**

**Part II - Other Information**

**Item 1. Legal Proceedings**

See Note 12 "Legal Matters and Contingencies" in the Notes to Consolidated Financial Statements in Part I, Item 1 of this report for a summary of legal proceedings.

**Item 1A. Risk Factors**

There are no material changes to the risk factors disclosed in the Company's Annual Report on Form 10-K for the fiscal year ended January 2, 2011, except as set forth in the Company's Quarterly Report on Form 10-Q for the fiscal quarter ended April 3, 2011.

**Item 2. Unregistered Sales of Equity Securities and Use of Proceeds**

During the six month period ended July 3, 2011, the Company did not purchase shares of its common stock.

**Table of Contents**

**Item 6. Exhibits**

| <b>Exhibit No.</b> | <b>Description</b>  |
|--------------------|---|
| 31.1*              | Certification of Chief Executive Officer Pursuant to Section 302 of the Sarbanes-Oxley Act of 2002  |
| 31.2*              | Certification of Chief Financial Officer Pursuant to Section 302 of the Sarbanes-Oxley Act of 2002  |
| 32.1*              | Certification of Chief Executive Officer Pursuant to 18 U.S.C. Section 1350, as Adopted Pursuant to Section 906 of the Sarbanes-Oxley Act of 2002   |
| 32.2*              | Certification of Chief Financial Officer Pursuant to 18 U.S.C. Section 1350, as Adopted Pursuant to Section 906 of the Sarbanes-Oxley Act of 2002   |
| 101                | The following materials from Morton's Restaurant Group Inc.'s Quarterly Report on Form 10-Q for the quarter ended July 3, 2011 are furnished herewith, formatted in XBRL (eXtensible Business Reporting Language): (i) the Consolidated Balance Sheets as of July 3, 2011 and January 2, 2011 - unaudited, (ii) the Consolidated Statements of Operations for the Three- and Six-Months Ended July 3, 2011 and July 4, 2010 - unaudited, (iii) the Consolidated Statements of Cash Flows for the Six-Months Ended July 3, 2011 and July 4, 2010 - unaudited, and (iv) the Notes to Unaudited Consolidated Financial Statements, tagged as blocks of text. |

\* Filed herewith.

**Table of Contents**

SIGNATURES

Pursuant to the requirements of the Securities Exchange Act of 1934, as amended, the Registrant has duly caused this report to be signed on its behalf by the undersigned thereunto duly authorized.

MORTON S RESTAURANT GROUP, INC.  
(Registrant)

Date: August 2, 2011

By: /s/ CHRISTOPHER J. ARTINIAN  
Christopher J. Artinian  
Chief Executive Officer, President and Director  
(Principal Executive Officer)

Date: August 2, 2011

By: /s/ RONALD M. DINELLA  
Ronald M. DiNella  
Senior Vice President,  
  
Chief Financial Officer and Treasurer  
(Principal Financial and Accounting Officer)