

JACK IN THE BOX INC /NEW/

Form 10-Q

May 14, 2008

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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 quarterly period ended April 13, 2008  
Commission File Number: 1-9390  
JACK IN THE BOX INC.**

(Exact name of registrant as specified in its charter)

DELAWARE

95-2698708

(State of Incorporation)

(I.R.S. Employer Identification No.)

9330 BALBOA AVENUE, SAN DIEGO, CA

92123

(Address of principal executive offices)

(Zip Code)

Registrant's telephone number, including area code (858) 571-2121

Indicate by check mark whether the registrant (1) has filed all reports required to be filed by Section 13 or 15(d) of the Securities Exchange Act of 1934 during the preceding 12 months (or for such shorter period that the registrant was required to file such reports), and (2) has been subject to such filing requirements for the past 90 days.

Yes  No

Indicate by check mark whether the registrant is a large accelerated filer, an accelerated filer, a non-accelerated filer, or a smaller reporting company. See the definitions 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  No

Number of shares of common stock, \$.01 par value, outstanding as of the close of business  
May 12, 2008 58,759,137.

**JACK IN THE BOX INC. AND SUBSIDIARIES  
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PART I. FINANCIAL INFORMATION  
ITEM 1. CONDENSED CONSOLIDATED FINANCIAL STATEMENTS  
JACK IN THE BOX INC. AND SUBSIDIARIES  
CONDENSED CONSOLIDATED BALANCE SHEETS  
(Dollars in thousands, except per share data)  
(Unaudited)

	<b>April 13, 2008</b>	<b>September 30, 2007</b>
<b>ASSETS</b>		
Current assets:		
Cash and cash equivalents	\$ 16,400	\$ 15,702
Accounts and other receivables, net	50,124	41,091
Inventories	46,805	46,933
Prepaid expenses	24,831	29,311
Deferred income taxes	47,063	47,063
Assets held for sale and leaseback	43,398	42,583
Other current assets	5,859	5,383
<b>Total current assets</b>	<b>234,480</b>	<b>228,066</b>
Property and equipment, at cost	1,608,266	1,586,577
Less accumulated depreciation and amortization	(658,035)	(634,409)
<b>Property and equipment, net</b>	<b>950,231</b>	<b>952,168</b>
Other assets, net	201,516	202,588
	<b>\$ 1,386,227</b>	<b>\$ 1,382,822</b>
 <b>LIABILITIES AND STOCKHOLDERS EQUITY</b>		
Current liabilities:		
Current maturities of long-term debt	\$ 3,925	\$ 5,787
Accounts payable	67,918	97,489
Accrued liabilities	234,018	223,540
<b>Total current liabilities</b>	<b>305,861</b>	<b>326,816</b>
Long-term debt, net of current maturities	425,970	427,516
Other long-term liabilities	172,156	168,722
Deferred income taxes	41,530	45,211

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Stockholders' equity:

Preferred stock \$.01 par value, 15,000,000 authorized, none issued		
Common stock \$.01 par value, 175,000,000 authorized, 73,348,119 and 72,515,171 issued, respectively	733	725
Capital in excess of par value	149,506	132,081
Retained earnings	744,318	681,350
Accumulated other comprehensive loss, net	(29,388)	(25,140)
Treasury stock, at cost, 14,635,109 and 12,779,609 shares, respectively	(424,459)	(374,459)
Total stockholders' equity	440,710	414,557
	\$ 1,386,227	\$ 1,382,822

See accompanying notes to condensed consolidated financial statements.

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JACK IN THE BOX INC. AND SUBSIDIARIES  
CONDENSED CONSOLIDATED STATEMENTS OF EARNINGS  
(In thousands, except per share data)  
(Unaudited)

	<b>Twelve Weeks Ended</b>		<b>Twenty-Eight Weeks Ended</b>	
	<b>April 13, 2008</b>	<b>April 15, 2007</b>	<b>April 13, 2008</b>	<b>April 15, 2007</b>
Revenues:				
Restaurant sales	\$ 490,810	\$ 500,445	\$ 1,138,525	\$ 1,151,853
Distribution and other sales	167,126	129,807	375,462	293,557
Franchised restaurant revenues	35,578	30,415	84,469	71,949
	693,514	660,667	1,598,456	1,517,359
Operating costs and expenses:				
Restaurant costs of sales	161,971	155,509	374,734	358,066
Restaurant operating costs	247,790	253,446	572,302	582,653
Distribution and other costs of sales	166,660	128,359	374,063	291,154
Franchised restaurant costs	14,892	12,923	33,840	29,343
Selling, general and administrative expenses	65,760	69,552	156,359	158,904
Gains on sale of company-operated restaurants	(11,942)	(7,244)	(28,747)	(14,401)
	645,131	612,545	1,482,551	1,405,719
Earnings from operations	48,383	48,122	115,905	111,640
Interest expense	6,783	8,337	15,870	18,115
Interest income	(42)	(3,056)	(293)	(7,340)
Interest expense, net	6,741	5,281	15,577	10,775
Earnings before income tax expense	41,642	42,841	100,328	100,865
Income tax expense	15,213	15,632	37,360	36,302
Net earnings	\$ 26,429	\$ 27,209	\$ 62,968	\$ 64,563
Net earnings per share:				
Basic	\$ .45	\$ .41	\$ 1.06	\$ .94
Diluted	\$ .44	\$ .40	\$ 1.04	\$ .92

Weighted-average shares outstanding:

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Basic	58,833	66,121	59,229	68,498
Diluted	59,953	67,888	60,488	70,426

See accompanying notes to condensed consolidated financial statements.

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JACK IN THE BOX INC. AND SUBSIDIARIES  
CONDENSED CONSOLIDATED STATEMENTS OF CASH FLOWS  
(Dollars in thousands)  
(Unaudited)

	<b>Twenty-Eight Weeks Ended</b>	
	<b>April 13, 2008</b>	<b>April 15, 2007</b>
Cash flows from operating activities:		
Net earnings	\$ 62,968	\$ 64,563
Adjustments to reconcile net income to net cash provided by operating activities:		
Depreciation and amortization	53,908	49,736
Deferred finance cost amortization	837	726
Provision for deferred income taxes	(1,182)	(8,353)
Share-based compensation expense for equity classified awards	5,385	6,270
Pension and postretirement expense	7,797	9,030
Losses (gains) on cash surrender value of company-owned life insurance	3,883	(4,793)
Gains on the sale of company-operated restaurants	(28,747)	(14,401)
Losses on the disposition of property and equipment, net	8,967	6,065
Loss on early retirement of debt		1,939
Impairment charges and other	1,461	383
Changes in assets and liabilities:		
Increase in receivables	(9,032)	(12,067)
Decrease (increase) in inventories	128	(4,293)
Decrease (increase) in prepaid expenses and other current assets	5,491	(1,098)
Decrease in accounts payable	(13,986)	(2,026)
Pension and postretirement contributions	(9,201)	(7,329)
Increase (decrease) in other liabilities	17,563	(753)
Cash flows provided by operating activities	106,240	83,599
Cash flows from investing activities:		
Purchases of property and equipment	(91,322)	(68,697)
Proceeds from the sale of company-operated restaurants	36,053	19,292
Proceeds from (purchase of) assets held for sale and leaseback, net	(1,362)	1,878
Purchase of investments, net	(4,138)	(4,275)
Other	1,166	97
Cash flows used in investing activities	(59,603)	(51,705)
Cash flows from financing activities:		
Borrowings on revolving credit facility	248,000	
Principal payments on revolving credit facility	(248,000)	
Borrowings under term loan		475,000
Principal payments on debt	(3,408)	(331,373)

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Payment of debt costs		(7,357)
Change in book overdraft	(4,382)	
Repurchase of common stock	(50,000)	(363,303)
Excess tax benefits from share-based compensation arrangements	4,202	14,374
Proceeds from issuance of common stock	7,649	23,972
Cash flows used in financing activities	(45,939)	(188,687)
Net increase (decrease) in cash and cash equivalents	698	(156,793)
Cash and cash equivalents at beginning of period	15,702	233,906
Cash and cash equivalents at end of period	\$ 16,400	\$ 77,113

See accompanying notes to condensed consolidated financial statements.

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## JACK IN THE BOX INC. AND SUBSIDIARIES

## NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (UNAUDITED)

**1. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES**

**Nature of operations** Founded in 1951, Jack in the Box Inc. (the Company) operates and franchises Jack in the Box quick-service restaurants and Qdoba Mexican Grill® (Qdoba) fast-casual restaurants in 43 states. The following summarizes the number of restaurants:

	April 13, 2008	Sept. 30, 2007
<b>Jack in the Box:</b>		
Company-operated	1,393	1,436
Franchised	749	696
Total system	2,142	2,132
<b>Qdoba:</b>		
Company-operated	97	90
Franchised	326	305
Total system	423	395

The Company also operates 61 proprietary convenience stores called Quick Stuff®, which include a major-branded fuel station developed adjacent to a full-size Jack in the Box restaurant.

References to the Company throughout these notes to the condensed consolidated financial statements are made using the first person notations of we, us and our.

**Basis of presentation** The accompanying condensed consolidated financial statements have been prepared in accordance with U.S. generally accepted accounting principles and the rules and regulations of the Securities and Exchange Commission (SEC). In our opinion, all adjustments considered necessary for a fair presentation of financial condition and results of operations for these interim periods have been included. Operating results for one interim period are not necessarily indicative of the results for any other interim period or for the full year.

The condensed consolidated financial statements include the accounts of the Company, its wholly-owned subsidiaries and the accounts of any variable interest entities where we are deemed the primary beneficiary. All significant intercompany transactions are eliminated.

These financial statements should be read in conjunction with the consolidated financial statements and related notes contained in our Annual Report on Form 10-K for the fiscal year ended September 30, 2007. The accounting policies used in preparing these condensed consolidated financial statements are the same as those described in our Form 10-K, with the exception of new accounting pronouncements adopted in fiscal 2008.

**Reclassifications and adjustments** Certain prior year amounts in the condensed consolidated financial statements have been reclassified to conform to the fiscal 2008 presentation. All historical share and per share data, except for treasury stock, in our condensed consolidated financial statements and notes thereto have been restated to give retroactive recognition of our two-for-one stock split effected on October 15, 2007. Refer to Note 6, *Stockholders Equity*, for additional information regarding the stock split.

**Fiscal year** Our fiscal year is 52 or 53 weeks ending the Sunday closest to September 30. Fiscal years 2008 and 2007 include 52 weeks. Our first quarter includes 16 weeks and all other quarters include 12 weeks. All comparisons between 2008 and 2007 refer to the 12-week (quarter) and 28-week (year-to-date) periods ended April 13, 2008 and April 15, 2007, respectively, unless otherwise indicated.

**Use of estimates** In preparing the condensed consolidated financial statements in conformity with U.S. generally accepted accounting principles, management is required to make certain assumptions and estimates that affect

reported amounts of assets, liabilities, revenues, expenses and the disclosure of contingencies. In making these assumptions and estimates, management may from time to time seek advice and consider information provided by actuaries and other experts in a particular area. Actual amounts could differ materially from these estimates.

***Company-owned life insurance*** We have purchased company-owned life insurance ( COLI ) policies to support our non-qualified benefit plans. The cash surrender values of these policies were \$66.1 million and \$66.8 million as of April 13, 2008 and September 30, 2007, respectively, and are included in other assets, net in the accompanying condensed consolidated balance sheets. These policies reside in an umbrella trust for use only to pay plan benefits to participants or to pay creditors if the Company becomes insolvent. As of April 13, 2008 and September 30, 2007, the trust also included cash of \$1.5 million and \$0.7 million, respectively.

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## JACK IN THE BOX INC. AND SUBSIDIARIES

## NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (UNAUDITED)

**Franchise arrangements** Franchise arrangements generally provide for initial franchise fees, which are included in franchised restaurant revenues in the accompanying condensed consolidated statements of earnings. In addition to initial franchise fees, we also recognize gains on the sale of company-operated restaurants to franchisees. Gains on the sale of restaurant businesses to franchisees are recorded when the sales are consummated, cash proceeds are received or collection is reasonably assured, and we have no continuing involvement other than normal franchisor franchisee contractual obligations. The following is a summary of these transactions (dollars in thousands):

	Twelve Weeks Ended		Twenty-Eight Weeks Ended	
	April 13, 2008	April 15, 2007	April 13, 2008	April 15, 2007
Number of restaurants sold to franchisees	23	15	51	30
Number of new restaurants opened by franchisees	7	17	32	48
Initial franchise fees received	\$ 1,105	\$ 1,275	\$ 3,228	\$ 2,775
Proceeds from the sale of company-operated restaurants	\$ 14,118	\$ 9,631	\$ 36,053	\$ 19,292
Net assets sold (primarily property and equipment)	(2,176)	(2,387)	(7,306)	(4,891)
Gains on the sale of company-operated restaurants	\$ 11,942	\$ 7,244	\$ 28,747	\$ 14,401

**New accounting pronouncements adopted** We adopted the provisions of Financial Accounting Standards Board ( FASB ) Interpretation 48 ( FIN 48 ), *Accounting for Uncertainty in Income Taxes – an interpretation of FASB Statement No. 109*, on October 1, 2007. FIN 48 clarifies the accounting for income taxes by prescribing a minimum probability threshold that a tax position must meet before a financial statement benefit is recognized. The minimum threshold is defined in FIN 48 as a tax position that is more likely than not to be sustained upon examination by the applicable taxing authority, including resolution of any related appeals or litigation processes, based on the technical merits of the position. The adoption of this statement did not have a material impact on our condensed consolidated financial statements. Refer to Note 3, *Income Taxes*, for additional information regarding our adoption of FIN 48.

**2. RESTAURANT CLOSING, IMPAIRMENT CHARGES AND OTHER**

In 2008, we recorded impairment charges of \$1.5 million primarily related to the write-down of the carrying value of two Jack in the Box restaurants which we continue to operate. We also recognized losses on the disposition of property and equipment of \$9.0 million primarily related to our restaurant re-image program, which includes a major renovation of our restaurant facilities, a kitchen enhancement project and normal ongoing capital maintenance activities.

In 2007, losses on the disposition of property and equipment of \$6.1 million were recognized primarily relating to our re-image program and capital maintenance activity.

These impairment charges and disposition losses are included in selling, general and administrative expenses in the accompanying condensed consolidated statements of earnings.

Total accrued restaurant closing costs, included in accrued expenses and other long-term liabilities, changed as follows during 2008 and 2007 (in thousands):

	Twelve Weeks Ended	Twenty-Eight Weeks Ended
--	--------------------	--------------------------

	<b>April 13, 2008</b>	<b>April 15, 2007</b>	<b>April 13, 2008</b>	<b>April 15, 2007</b>
Balance at beginning of period	\$ 5,415	\$ 4,888	\$ 5,451	\$ 5,004
Additions and adjustments	113	132	399	254
Cash payments	(385)	(238)	(707)	(476)
Balance at end of period	\$ 5,143	\$ 4,782	\$ 5,143	\$ 4,782

Additions and adjustments primarily relate to revisions to certain sublease assumptions and the closure of two Jack in the Box restaurants in 2008.

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## JACK IN THE BOX INC. AND SUBSIDIARIES

## NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (UNAUDITED)

**3. INCOME TAXES**

The income tax provisions reflect effective tax rates of 37.2% in 2008 and 36.0% in 2007. We expect the annual tax rate for fiscal year 2008 to be 37.0%-38.0%. The final annual tax rate cannot be determined until the end of the fiscal year; therefore, the actual rate could differ from our current estimates.

As of the date of our adoption of FIN 48, our gross unrecognized tax benefits for income taxes associated with uncertain tax positions totaled \$11.0 million. Of this total, \$10.4 million represented the amount of unrecognized tax benefits that, if recognized, would favorably affect the effective income tax rate in future periods. Also as of the adoption date, we had accrued interest related to the unrecognized tax benefits of \$1.2 million (exclusive of tax benefits). As of the date of adoption, we recognize interest and, when applicable, penalties related to uncertain tax positions in income tax expense. Prior to the adoption of FIN 48, interest expense related to tax uncertainties was accrued as a component of pre-tax income.

As of April 13, 2008, the gross unrecognized tax benefits for income taxes associated with uncertain tax positions decreased to \$7.0 million of which \$6.3 million represented the amount of unrecognized tax benefits that, if recognized, would favorably affect the effective income tax rate in future periods. Also as of April 13, 2008, we had accrued interest related to the unrecognized tax benefits of \$0.4 million. The majority of these changes from the previous quarter are due to a re-classification between long-term taxes payable and current income taxes payable based upon the Notice of Deficiency received from the Internal Revenue Service ( IRS ) for tax years 2004-2005. The Company considers these two years to be effectively settled within the meaning of FIN 48 and has re-classified the portion of its FIN 48 liability from these years related to the assessment, to current income taxes payable as the amount will be paid within the next twelve months. With respect to tax years 2002-2003, the IRS is still in the final stages of completion and the Company does not yet consider these years to be effectively settled.

It is reasonably possible that material changes to the gross unrecognized tax benefits will be required within the next twelve months. In addition to the anticipated completion of the IRS audit for 2002-2003, these changes relate to the possible settlement of an IRS audit of the Company's 2006 tax year that is currently in progress and the California Franchise Tax Board's continuing audit of requested claims for refund, all of which are expected to be completed within the next twelve months. In addition, the statute of limitations in various state taxing jurisdictions will expire within the next twelve months. Though the Company expects these items may result in a net reduction of its unrecognized tax benefits, an estimate of the expected change cannot be made at this time.

The federal statute of limitations for all tax years beginning with 2001 remains open at this time. Generally, the statutes of limitations for the state jurisdictions where there would be a material impact have not expired for tax years 1998 and forward. In the state of California, the statute of limitations is limited to certain items for tax years 1998-2001, and remains fully open for tax years 2002 and forward.

**4. RETIREMENT PLANS**

**Defined benefit pension plans** We sponsor defined benefit pension plans covering substantially all full-time employees. We also sponsor an unfunded supplemental executive retirement plan ( SERP ), which provides certain employees additional pension benefits. Effective January 1, 2007, the SERP was closed to any new participants. Benefits under these plans are based on the employees' years of service and compensation over defined periods of employment.

**Postretirement healthcare plans** We also sponsor healthcare plans that provide postretirement medical benefits to certain employees who meet minimum age and service requirements. The plans are contributory; with retiree contributions adjusted annually, and contain other cost-sharing features such as deductibles and coinsurance.

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## JACK IN THE BOX INC. AND SUBSIDIARIES

## NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (UNAUDITED)

**Net periodic benefit cost** The components of net periodic benefit cost were as follows (in thousands):

	Twelve Weeks Ended		Twenty-Eight Weeks Ended	
	April 13, 2008	April 15, 2007	April 13, 2008	April 15, 2007
<b>Defined benefit pension plans:</b>				
Service cost	\$ 2,592	\$ 2,200	\$ 6,047	\$ 6,181
Interest cost	3,944	3,276	9,203	9,049
Expected return on plan assets	(3,925)	(2,998)	(9,160)	(8,544)
Amortization of actuarial loss	346	465	810	1,326
Amortization of unrecognized prior service cost	209	304	487	723
Net periodic benefit cost	\$ 3,166	\$ 3,247	\$ 7,387	\$ 8,735
<b>Postretirement health plans:</b>				
Service cost	\$ 51	\$ 49	\$ 120	\$ 115
Interest cost	271	250	633	582
Amortization of actuarial gain	(189)	(216)	(442)	(501)
Amortization of unrecognized prior service cost	43	43	99	99
Net periodic benefit cost	\$ 176	\$ 126	\$ 410	\$ 295

**Cash flows** Our policy is to fund our plans at or above the minimum required by law. Details regarding 2008 contributions are as follows (in thousands):

	Defined benefit pension plans	Postretirement health plans (1)
Net contributions during the twenty-eight weeks ended April 13, 2008	\$ 8,912	\$ 289
Remaining estimated net contributions during fiscal 2008	\$ 14,400	\$ 500

(1) Net of Medicare Part D Subsidy.

**5. SHARE-BASED EMPLOYEE COMPENSATION**

**Compensation expense** We offer share-based compensation plans to attract, retain, and motivate key officers, non-employee directors, and employees to work toward the financial success of the Company. The components of share-based compensation expense recognized in each period are as follows (in thousands):

	Twelve Weeks Ended	Twenty-Eight Weeks Ended
	April 15,	April 13,
	2008	2007

	<b>April 13, 2008</b>	<b>2007</b>	<b>2008</b>	<b>2007</b>
Stock options	\$ 1,441	\$ 1,096	\$ 3,475	\$ 4,338
Performance-vested stock awards	578	530	1,342	1,251
Nonvested stock awards	187	198	429	461
Deferred compensation for directors equity classified	59	80	139	220
Deferred compensation for directors liability classified				324
Total share-based compensation expense	\$ 2,265	\$ 1,904	\$ 5,385	\$ 6,594

## 6. STOCKHOLDERS EQUITY

**Stock split** On August 3, 2007, our Board of Directors approved a two-for-one split of our common stock, that was effected in the form of a 100% stock dividend on October 15, 2007. In connection with the stock split, our shareholders approved, on September 21, 2007, an amendment to our Certificate of Incorporation to increase the number of authorized common shares from 75.0 million to 175.0 million.

**Repurchases of common stock** In November 2007, the Board approved a program to repurchase up to \$200.0 million in shares of our common stock over three years expiring November 9, 2010. We repurchased 1.9 million shares at an aggregate cost of \$50.0 million during the first two quarters of fiscal 2008. As of April 13, 2008, the total remaining amount authorized for repurchase was \$150.0 million.

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**JACK IN THE BOX INC. AND SUBSIDIARIES**  
**NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (UNAUDITED)**

**Comprehensive income** Our total comprehensive income, net of taxes, was as follows (in thousands):

	<b>Twelve Weeks Ended</b>		<b>Twenty-Eight Weeks Ended</b>	
	<b>April 13, 2008</b>	<b>April 15, 2007</b>	<b>April 13, 2008</b>	<b>April 15, 2007</b>
Net earnings	\$ 26,429	\$ 27,209	\$ 62,968	\$ 64,563
Net unrealized gains (losses) related to cash flow hedges	(1,367)	743	(7,701)	135
Tax effect	508	(286)	2,943	(41)
	(859)	457	(4,758)	94
Net realized gains reclassified into net earnings on liquidation of interest rate swaps				(371)
Tax effect				137
				(234)
Effect of amortization of unrecognized net actuarial losses and prior service cost	409		954	
Tax effect	(234)		(444)	
	175		510	
Total comprehensive income	\$ 25,745	\$ 27,666	\$ 58,720	\$ 64,423

The components of accumulated other comprehensive loss, net of taxes, were as follows at the end of each period (in thousands):

	<b>April 13, 2008</b>	<b>Sept. 30, 2007</b>
Unrecognized periodic benefit costs, net of taxes of (\$14,704) and (\$15,148), respectively	\$ (23,739)	\$ (24,249)
Net unrealized losses related to cash flow hedges, net of taxes of (\$3,499) and (\$556), respectively	(5,649)	(891)
Accumulated other comprehensive loss	\$ (29,388)	\$ (25,140)

**7. AVERAGE SHARES OUTSTANDING**

Our basic earnings per share calculation is computed based on the weighted-average number of common shares outstanding. Our diluted earnings per share calculation is computed based on the weighted-average number of common shares outstanding adjusted by the number of additional shares that would have been outstanding had the potentially dilutive common shares been issued. Potentially dilutive common shares include stock options, nonvested

stock awards, non-management director stock equivalents and shares issuable under our employee stock purchase plan. Performance-vested stock awards are included in the average diluted shares outstanding each period if the performance criteria have been met at the end of the respective periods.

The following table reconciles basic weighted-average shares outstanding to diluted weighted-average shares outstanding (in thousands):

	Twelve Weeks Ended		Twenty-Eight Weeks Ended	
	April 13, 2008	April 15, 2007	April 13, 2008	April 15, 2007
Weighted-average shares outstanding basic	58,833	66,121	59,229	68,498
Assumed additional shares issued upon exercise of stock options, net of shares reacquired at the average market price	888	1,511	1,020	1,675
Assumed vesting of nonvested stock, net of shares reacquired at the average market price	213	256	220	253
Performance-vested stock awards issuable	19		19	
Weighted-average shares outstanding diluted	59,953	67,888	60,488	70,426
Stock options excluded (1)	1,397	518	1,303	602
Performance-vested awards excluded (2)	348	422	348	422

(1) Excluded from diluted weighted-average shares outstanding because their exercise prices, unamortized compensation and tax benefits exceeded the average market price of common stock for the period.

(2) Excluded from diluted weighted-average shares outstanding because the number of shares issued is contingent on achievement of performance goals at the end of a

three-year  
performance  
period.

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## JACK IN THE BOX INC. AND SUBSIDIARIES

## NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (UNAUDITED)

**8. CONTINGENCIES AND LEGAL MATTERS**

**Legal matters** We are subject to normal and routine litigation. In the opinion of management, based in part on the advice of legal counsel, the ultimate liability from all pending legal proceedings, asserted legal claims and known potential legal claims should not materially affect our operating results, financial position or liquidity.

**9. SEGMENT REPORTING**

In the first quarter of fiscal 2008, reflecting our vision of being a national restaurant company and the information currently being used in managing the Company as a two-branded restaurant operations business, we revised the composition of our segments to include results related to system restaurant operations for our Jack in the Box and Qdoba brands. This segment reporting structure reflects the Company's current management structure, internal reporting method, and financial information used in deciding how to allocate Company resources. Based upon certain quantitative thresholds, both operating segments are considered reportable segments.

We measure and evaluate our segments based on segment earnings from operations. Summarized financial information concerning our reportable segments follows (in thousands). All amounts for the fiscal year ended September 30, 2007 have been revised to conform to the new segment reporting as previously described.

	Twelve Weeks Ended		Twenty-Eight Weeks Ended	
	April 13, 2008	April 15, 2007	April 13, 2008	April 15, 2007
<b>Revenues by Segment:</b>				
Jack in the Box restaurant operations	\$ 500,633	\$ 510,898	\$ 1,163,854	\$ 1,178,529
Qdoba restaurant operations	25,755	19,962	59,140	45,273
Other	167,126	129,807	375,462	293,557
Consolidated revenues	\$ 693,514	\$ 660,667	\$ 1,598,456	\$ 1,517,359
<b>Earnings from Operations by Segment:</b>				
Jack in the Box restaurant operations	\$ 46,845	\$ 45,122	\$ 110,797	\$ 105,961
Qdoba restaurant operations	1,515	1,998	4,434	4,228
Other	23	1,002	674	1,451
Consolidated earnings from operations	\$ 48,383	\$ 48,122	\$ 115,905	\$ 111,640

Other includes distribution and Quick Stuff operating results. Interest income and expense and income taxes are not reported for our segments, in accordance with our method of internal reporting.

**10. SUPPLEMENTAL CONSOLIDATED CASH FLOW INFORMATION**

Additional information related to cash flows is as follows (in thousands):

	Twenty-Eight Weeks Ended	
	April 13, 2008	April 15, 2007
Cash paid during the year for:		
Interest, net of amounts capitalized	\$15,966	\$14,718
Income tax payments	31,942	60,755

Capital lease obligations incurred

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**11. FUTURE APPLICATION OF ACCOUNTING PRINCIPLES**

In September 2006, the FASB issued Statement of Financial Accounting Standards ( SFAS ) 157, *Fair Value Measurements*. SFAS 157 clarifies the definition of fair value, describes methods used to appropriately measure fair value, and expands fair value disclosure requirements. This statement applies under other accounting pronouncements that currently require or permit fair value measurements and is effective for fiscal years beginning after November 15, 2007, and interim periods within those years. However, the effective date of SFAS 157 as it relates to fair value measurement requirements for nonfinancial assets and liabilities that are not remeasured at fair value on a recurring basis is deferred to fiscal years beginning after December 15, 2008 and interim periods within those years. We are currently in the process of assessing the impact that SFAS 157 will have on our consolidated financial statements.

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JACK IN THE BOX INC. AND SUBSIDIARIES

NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (UNAUDITED)

In September 2006, the FASB issued SFAS 158, *Employers' Accounting for Defined Benefit Pension and Other Postretirement Plans - an amendment of FASB Statements No. 87, 88, 106 and 132(R)*. In fiscal 2007, we adopted the recognition provisions of SFAS 158 which requires recognition of the overfunded or underfunded status of a defined benefit plan as an asset or liability. SFAS 158 also requires that companies measure their plan assets and benefit obligations at the end of their fiscal year. The measurement provision of SFAS 158 is effective for fiscal years ending after December 15, 2008. We will not be able to determine the impact of adopting the measurement provision of SFAS 158 until the end of the fiscal year when such valuation is completed.

In February 2007, the FASB issued SFAS 159, *The Fair Value Option for Financial Assets and Financial Liabilities*. SFAS 159 permits entities to voluntarily choose to measure many financial instruments and certain other items at fair value. SFAS 159 is effective for fiscal years beginning after November 15, 2007. We are currently in the process of determining whether to elect the fair value measurement options available under this standard.

In March 2008, the FASB issued SFAS 161, *Disclosures about Derivative Instruments and Hedging Activities*, which amends SFAS 133 and expands disclosures to include information about the fair value of derivatives, related credit risks and a company's strategies and objectives for using derivatives. SFAS 161 is effective for fiscal periods beginning on or after November 15, 2008. We are currently in the process of assessing the impact that SFAS 161 will have on the disclosures in our consolidated financial statements.

Other accounting standards that have been issued or proposed by the FASB or other standards-setting bodies that do not require adoption until a future date are not expected to have a material impact on our consolidated financial statements upon adoption.

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**ITEM 2. MANAGEMENT'S DISCUSSION AND ANALYSIS OF FINANCIAL CONDITION AND RESULTS OF OPERATIONS**

**GENERAL**

All comparisons between 2008 and 2007 refer to the 12-week ( quarter ) and 28-week ( year-to-date ) periods ended April 13, 2008 and April 15, 2007, respectively, unless otherwise indicated.

For an understanding of the significant factors that influenced our performance during the two quarterly periods ended April 13, 2008 and April 15, 2007, we believe our Management's Discussion and Analysis of Financial Condition and Results of Operations ( MD&A ) should be read in conjunction with the Condensed Consolidated Financial Statements and related Notes included in this Quarterly Report as indexed on page two.

Our MD&A consists of the following sections:

***Overview*** a general description of our business, the quick-service dining segment of the restaurant industry and fiscal 2008 highlights.

***Financial reporting changes*** a summary of significant financial statement reclassifications, adjustments and new accounting pronouncements adopted.

***Results of operations*** an analysis of our consolidated statements of earnings for the periods presented in our condensed consolidated financial statements.

***Liquidity and capital resources*** an analysis of cash flows including capital expenditures, aggregate contractual obligations, share repurchase activity, known trends that may impact liquidity, and the impact of inflation.

***Discussion of critical accounting estimates*** a discussion of accounting policies that require critical judgments and estimates.

***New accounting pronouncements*** a discussion of new accounting pronouncements, dates of implementation and impact on our consolidated financial position or results of operations, if any.

***Cautionary statements regarding forward-looking statements*** a discussion of the forward-looking statements used by management.

**OVERVIEW**

As of April 13, 2008, Jack in the Box Inc. (the Company ) operated and franchised 2,142 Jack in the Box quick-service restaurants and 423 Qdoba Mexican Grill ( Qdoba ) fast-casual restaurants, primarily in the western and southern United States.

Our primary source of revenue is from retail sales at company-operated restaurants. We also derive revenue from sales of food and packaging to Jack in the Box and Qdoba franchised restaurants, retail sales from fuel and convenience stores ( Quick Stuff ), and revenue from franchisees including royalties, based upon a percent of sales, franchise fees and rents. In addition, we recognize gains from the sale of company-operated restaurants to franchisees, which are presented as a reduction of operating costs and expenses in the accompanying condensed consolidated statements of earnings.

The quick-service restaurant industry is complex and challenging. Challenges presently facing the sector include higher levels of consumer expectations, intense competition with respect to market share, restaurant locations, labor, menu and product development, trends for healthier eating, and changes in the economy, including costs of commodities and changes in consumer spending which have been impacted by, among other factors, an unstable housing market, higher fuel prices and higher unemployment rates in certain markets.

To address these challenges and others, management has a strategic plan focused on four key initiatives. The first initiative is a growth strategy that includes opening new restaurants and increasing same-store sales. The second initiative is a holistic reinvention of the Jack in the Box brand through menu innovation, upgrading guest service and re-imaging Jack in the Box restaurant facilities to reflect the personality of Jack the chain's fictional founder and

popular spokesman. The third strategic initiative is to expand franchising through new restaurant development and the sales of company-operated restaurants to franchisees to generate higher returns and higher

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margins, while mitigating business-cost and investment risks. The fourth initiative is to improve our business model to improve restaurant profitability, margins and returns, reduce operating costs and increase the long-term value of our business.

The following summarizes the most significant events occurring in fiscal 2008:

**Restaurant Sales.** Jack in the Box company-operated restaurants open more than one year ( same-store ) sales increased 0.8% year-to-date, on top of an increase of 5.9% a year ago. System same-store sales at Qdoba restaurants increased 3.5% year-to-date, on top of an increase of 3.8% a year ago.

**New Market Expansion.** We expanded into a new contiguous company market in Denver, Colorado, opening two Jack in the Box restaurants and we opened our third restaurant in Corpus Christi, a new market we entered at the end of last fiscal year. Franchisees are also expanding into new contiguous markets in Texas. In 2008, franchisees opened one Jack in the Box restaurant in Midland/Odessa and remain on track to open additional Jack in the Box restaurants in Abilene and San Angelo.

**Re-Image Program.** We continued to re-image our Jack in the Box restaurants with a comprehensive program that includes a complete redesign of the dining room and common areas. In 2008, the Company and franchisees re-imaged 133 restaurants bringing the total number of re-imaged restaurants to nearly 500 since the current program was adopted in 2006. The entire Jack in the Box system, including franchised locations, is expected to be re-imaged over the next 3-4 years.

**Franchising Program.** We continued to execute our strategic initiative to expand franchising through new restaurant development and sales of company-operated restaurants to franchisees. In 2008, we refranchised 51 Jack in the Box restaurants, and Qdoba and Jack in the Box franchisees opened 32 new restaurants. At April 13, 2008, approximately 35% of our Jack in the Box restaurants were franchised. Our long-term goal is to grow the percentage of franchise ownership of the Jack in the Box system by approximately 5% annually and move toward an ultimate goal of 70%-80%, which is more closely aligned with that of the QSR industry.

**Treasury Highlights.** Pursuant to a stock repurchase program authorized by our Board of Directors, we repurchased 1.9 million shares of our common stock for an aggregate of \$50.0 million.

**FINANCIAL REPORTING CHANGES**

Historical share and per share data for 2007 in our Quarterly Report on Form 10-Q have been restated to give retroactive recognition of our two-for-one stock split that was effected in the form of a 100% stock dividend on October 15, 2007, with the exception of treasury share data as no stock dividend was paid with respect to treasury shares. Refer to Note 6, *Stockholders' Equity*, in the notes to the condensed consolidated financial statements for additional information regarding the stock split.

**Table of Contents****RESULTS OF OPERATIONS**

The following table sets forth, unless otherwise indicated, the percentage relationship to total revenues of certain items included in our condensed consolidated statements of earnings.

	Twelve Weeks Ended		Twenty-Eight Weeks Ended	
	April 13, 2008	April 15, 2007	April 13, 2008	April 15, 2007
Revenues:				
Restaurant sales	70.8%	75.7%	71.2%	75.9%
Distribution and other sales	24.1	19.7	23.5	19.4
Franchised restaurant revenues	5.1	4.6	5.3	4.7
Total revenues	100.0%	100.0%	100.0%	100.0%
Operating costs and expenses:				
Restaurant costs of sales (1)	33.0%	31.1%	32.9%	31.1%
Restaurant operating costs (1)	50.5	50.6	50.3	50.6
Distribution and other costs of sales (1)	99.7	98.9	99.6	99.2
Franchised restaurant costs (1)	41.9	42.5	40.1	40.8
Selling, general and administrative expenses	9.5	10.5	9.8	10.5
Gains on sale of company-operated restaurants	(1.7)	(1.1)	(1.8)	(0.9)
Earnings from operations	7.0	7.3	7.3	7.4

(1) As a percentage of the related sales and/or revenues.

The following table summarizes the number of systemwide restaurants:

**SYSTEMWIDE RESTAURANT UNITS**

	April 13, 2008	Sept. 30, 2007	April 15, 2007
<b>Jack in the Box:</b>			
Company-operated	1,393	1,436	1,456
Franchised	749	696	642
Total system	2,142	2,132	2,098
<b>Qdoba:</b>			
Company-operated	97	90	73
Franchised	326	305	280
Total system	423	395	353

**Consolidated:**

Company-operated	1,490	1,526	1,529
Franchised	1,075	1,001	922
Total system	2,565	2,527	2,451

Since April 15, 2007, we opened 41 company-operated Jack in the Box restaurants (along with four new Quick Stuff convenience stores) and 15 company-operated Qdoba restaurants. Franchisees opened 13 Jack in the Box and 64 Qdoba restaurants since a year ago.

**Revenues**

Restaurant sales decreased \$9.6 million, or 1.9%, in the quarter and \$13.3 million, or 1.2%, year-to-date primarily due to a decrease in the number of Jack in the Box company-operated restaurants reflecting the sale of company-operated restaurants to franchisees. This decrease was partially offset by increases in per store average (PSA) sales at Jack in the Box and Qdoba company-operated restaurants, as well as an increase in the number of Qdoba company-operated restaurants. Same-store sales at Jack in the Box company-operated restaurants decreased 0.1% in the quarter and increased 0.8% year-to-date compared with a year ago, reflecting price increases of approximately 2.5% year-to-date. Our restaurants in Texas, the Southeast and other key markets continue to perform well, but we have seen a slowdown in certain western markets, such as some of those in California, due to the downturn in the housing market, higher fuel prices and unemployment.

Distribution and other sales, representing distribution sales to Jack in the Box and Qdoba franchisees, as well as Quick Stuff fuel and convenience store sales, grew to \$167.1 million and \$375.5 million, respectively in 2008 from \$129.8 million and \$293.6 million in 2007. Sales from our Quick Stuff locations increased \$24.6 million and \$51.0

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million, respectively, compared with a year ago due to increases in PSA fuel sales and the number of locations to 61 at the end of the quarter from 57 a year ago. The increase in PSA fuel sales reflects higher retail prices offset in part by a decrease in year-to-date gallons sold. Distribution sales to Jack in the Box and Qdoba franchisees increased \$12.7 million and \$30.9 million, respectively, in 2008 compared with the same periods in 2007 reflecting an increase in the number of franchised restaurants serviced by our distribution centers.

Franchised restaurant revenues, which includes rents, royalties and fees from restaurants operated by franchisees, increased \$5.2 million and \$12.5 million, respectively, in 2008 to \$35.6 million and \$84.5 million, primarily due to an increase in the number of franchised restaurants. The number of franchised restaurants increased to 1,075 at the end of the quarter from 922 a year ago, reflecting the franchising of Jack in the Box company-operated restaurants and new restaurant development by Qdoba and Jack in the Box franchisees.

**Operating Costs and Expenses**

Restaurant costs of sales, which include food and packaging costs, increased to \$162.0 million and \$374.7 million, respectively, in 2008 from \$155.5 million and \$358.1 million in 2007. Restaurant costs of sales increased to 33.0% and 32.9% of sales, respectively, in 2008 compared with 31.1% in both periods of 2007 as higher commodity costs, primarily cheese, shortening, dairy and eggs, as well as product mix changes were partially offset by selling price increases and lower packaging costs.

Restaurant operating costs decreased to \$247.8 million and \$572.3 million, respectively, in 2008 from \$253.4 million and \$582.7 million in 2007. Restaurant operating costs improved to 50.5% and 50.3% of sales, respectively, in 2008 compared with 50.6% in both periods of 2007 due primarily to a 40-basis-points decline in labor costs in both periods, as effective labor management more than offset increased minimum wages in several states in which we operate. In both periods, the benefit provided by declining labor costs was partially offset by higher depreciation expense related to increased capital spending associated with the Company's on-going comprehensive re-image program and kitchen enhancement project, and higher costs for utilities.

Costs of distribution and other sales increased to \$166.7 million and \$374.1 million, respectively, in 2008 from \$128.4 million and \$291.2 million in 2007, primarily reflecting an increase in the related sales. As a percentage of the related sales, these costs increased to 99.7% and 99.6% in 2008 from 98.9% and 99.2% in 2007, due primarily to higher retail prices per gallon of fuel.

Franchised restaurant costs, principally rents and depreciation on properties leased to Jack in the Box franchisees, increased to \$14.9 million and \$33.8 million, respectively in 2008 from \$12.9 million and \$29.3 million in 2007, due primarily to an increase in the number of franchised restaurants. As a percentage of franchised restaurant revenues, franchised restaurant costs decreased to 41.9% and 40.1%, respectively, in 2008 from 42.5% and 40.8% in 2007 due primarily to the leverage provided by higher franchise revenues.

Selling, general and administrative expenses ( SG&A ) decreased \$3.8 million and \$2.5 million, respectively, in 2008 to \$65.8 million and \$156.4 million. The decrease is primarily due to effective management of field general and administrative expenses as well as lower salaries and related benefits associated with the Company's refranchising strategy reducing expenses by \$1.7 million and \$4.5 million, respectively, in 2008 compared with a year ago. Additionally, compensation and benefit costs, including pension expense, share-based and incentive compensation and offsetting changes in the cash surrender value of our COLI policies and our non-qualified deferred compensation obligation supported by these policies, decreased \$1.5 million and \$0.5 million, respectively, in 2008 compared to a year ago. A \$1.2 million charge recorded in the second quarter of fiscal 2007 related to a legal matter also contributed to the decrease in 2008. These SG&A decreases were partially offset by higher general and administrative expenses at Qdoba of \$0.9 million and \$1.9 million, respectively, in support of their continued growth and a \$1.6 million year-to-date increase in facility charges primarily related to the Jack in the Box re-image program, a Jack in the Box kitchen enhancement project and the impairment of two restaurants we continue to operate. As a percent of revenues, SG&A improved to 9.5% and 9.8% of revenues in 2008 compared with 10.5% in both periods a year ago due primarily to the leverage from higher revenues and lower costs in the quarter.

Gains on sale of company-operated restaurants to franchisees were \$11.9 million and \$28.7 million, respectively, from the sale of 23 and 51 Jack in the Box restaurants, in 2008 compared with \$7.2 million and \$14.4 million, from the sale of 15 and 30 Jack in the Box restaurants, in 2007. The change in gains relates to the number of restaurants

sold and the specific sales and cash flows of those restaurants.

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### **Interest Expense**

Interest expense decreased \$1.5 million and \$2.2 million, respectively, in 2008 to \$6.8 million and \$15.9 million from \$8.3 million and \$18.1 million in 2007, which included a \$1.9 million charge in the first quarter to write-off deferred financing fees in connection with the replacement of our credit facility. The decrease in interest expense exclusive of the charge in the prior year relates to lower average interest rates, and in the quarter lower average bank borrowings, compared with a year ago.

### **Interest Income**

Interest income decreased \$3.0 million and \$7.0 million, respectively, in 2008 to \$0.04 million and \$0.3 million from \$3.1 million and \$7.3 million in 2007 primarily reflecting lower average cash balances.

### **Income Taxes**

The income tax provisions reflect effective tax rates of 37.2% in 2008 and 36.0% in 2007. We expect the annual tax rate for fiscal year 2008 to be 37.0%-38.0%. The final annual tax rate cannot be determined until the end of the fiscal year; therefore, the actual rate could differ from our current estimates.

### **Net Earnings**

Net earnings in the quarter were \$26.4 million, or \$.44 per diluted share, in 2008 compared to \$27.2 million, or \$.40 per diluted share, in 2007. Year-to-date net earnings were \$63.0 million, or \$1.04 per diluted share, in 2008 compared to \$64.6 million, or \$.92 per diluted share, in 2007.

## **LIQUIDITY AND CAPITAL RESOURCES**

**General.** Our primary sources of short-term and long-term liquidity are expected to be cash flows from operations, the revolving bank credit facility, the sale of company-operated restaurants to franchisees and the sale and leaseback of certain restaurant properties.

Our cash requirements consist principally of:

working capital;

capital expenditures for new restaurant construction, restaurant renovations and upgrades of our management information systems;

income tax payments;

debt service requirements; and

obligations related to our benefit plans.

Based upon current levels of operations and anticipated growth, we expect that cash flows from operations, combined with other financing alternatives in place or available, will be sufficient to meet our capital expenditure, working capital and debt service requirements.

As is common in the restaurant industry, we maintain relatively low levels of accounts receivable and inventories, and our vendors grant trade credit for purchases such as food and supplies. We also continually invest in our business through the addition of new units and refurbishment of existing units, which are reflected as long-term assets and not as part of working capital. As a result, we typically maintain current liabilities in excess of current assets which result in a working capital deficit.

Cash and cash equivalents increased \$0.7 million to \$16.4 million at April 13, 2008 from \$15.7 million at the beginning of the fiscal year. This increase is primarily due to cash flows provided by operating activities and proceeds from the sale of restaurants to franchisees, which were offset in part by property and equipment expenditures and the use of cash to repurchase our common stock. We generally reinvest available cash flows from operations to develop new restaurants or enhance existing restaurants, to repurchase shares of our common stock and to reduce debt.

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**Cash Flows.** The following table summarizes our cash flows from operating, investing and financing activities for the 28-weeks ended April 13, 2008 and April 15, 2007 (in thousands):

	2008	2007
Total cash provided by (used in):		
Operating activities	\$ 106,240	\$ 83,599
Investing activities	(59,603)	(51,705)
Financing activities	(45,939)	(188,687)
Increase (decrease) in cash and cash equivalents	\$ 698	\$ (156,793)

**Operating Activities.** In 2008, operating cash flows increased \$22.6 million compared with a year ago primarily as a result of the timing of payments made for income taxes.

**Investing Activities.** Cash flows used in investing activities increased \$7.9 million in 2008 compared with a year ago primarily due to higher capital expenditures offset in part by an increase in proceeds from the sale of company-operated restaurants to franchisees.

**Capital Expenditures.** Our capital expenditure program includes, among other things, investments in new locations, restaurant remodeling, and information technology enhancements. We used cash of \$91.3 million for purchases of property and equipment in 2008 compared with \$68.7 million in 2007. The increase in capital expenditures primarily relates to a kitchen enhancement project and our on-going comprehensive re-image program.

In fiscal year 2008, capital expenditures are expected to be approximately \$175-\$185 million, including investment costs related to the Jack in the Box restaurant re-image program and kitchen enhancements. We plan to open approximately 22-28 new company-operated Jack in the Box restaurants, and under our brand reinvention strategy, plan to re-image approximately 250 company-operated restaurants.

**Sale of Company-Operated Restaurants.** We continued our strategy of selectively selling Jack in the Box company-operated restaurants to franchisees. In 2008, we generated proceeds of \$36.1 million from the sale of 51 restaurants compared with \$19.3 million in 2007 from the sale of 30 restaurants. In fiscal year 2008, we expect cash flows of \$65-\$75 million from the sale of approximately 100 company-operated restaurants to franchisees.

**Financing Activities.** Cash used in financing activities decreased \$142.7 million compared with a year ago primarily attributable to proceeds received in 2007 related to our new credit facility, offset in part by a decrease in debt related payments, share repurchases and proceeds from the issuance of common stock. Share repurchases, up to the limit authorized by the Board of Directors, are at the discretion of management and depend on market conditions, capital requirements and other factors.

**Credit Facility.** Our credit facility is comprised of (i) a \$150.0 million revolving credit facility maturing on December 15, 2011 and (ii) a term loan of \$415.0 million maturing on December 15, 2012, both bearing interest at London Interbank Offered Rate ( LIBOR ) plus 1.125%.

As part of the credit agreement, we may also request the issuance of up to \$75.0 million in letters of credit, the outstanding amount of which reduces the net borrowing capacity under the agreement. The credit facility requires the payment of an annual commitment fee based on the unused portion of the credit facility. The credit facility's interest rates and the annual commitment rate are based on a financial leverage ratio, as defined in the credit agreement. Our obligations under the credit facility are secured by first priority liens and security interests in the capital stock, partnership and membership interests owned by us and (or) our subsidiaries, and any proceeds thereof, subject to certain restrictions set forth in the credit agreement. Additionally, the credit agreement includes a negative pledge on all tangible and intangible assets (including all real and personal property) with customary exceptions.

**Interest Rate Swaps.** To reduce our exposure to rising interest rates under our new credit facility, in March 2007, we entered into two interest rate swaps that effectively converted \$200.0 million of our variable rate term loan borrowings to a fixed-rate basis for three years. These agreements have been designated as cash flow hedges under the terms of SFAS 133, *Accounting for Derivative Instruments and Hedging Activities*, with effectiveness assessed on

changes in the present value of the term loan interest payments. There was no hedge ineffectiveness in 2008. Accordingly, changes in the fair value of the interest rate swap contracts were recorded, net of taxes, as a component of

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accumulated other comprehensive loss in the Company's condensed consolidated balance sheet as of April 13, 2008.

*Debt Covenants.* We are subject to a number of covenants under our various debt instruments, including limitations on additional borrowings, acquisitions, loans to franchisees, capital expenditures, lease commitments, stock repurchases and dividend payments, as well as requirements to maintain certain financial ratios, cash flows and net worth. As of April 13, 2008, we were in compliance with all debt covenants.

*Debt Outstanding.* At April 13, 2008, we had \$415.0 million outstanding under the term loan and letters of credit outstanding of \$40.3 million. Total debt outstanding decreased to \$429.9 million at April 13, 2008 from \$433.3 million at the beginning of the fiscal year due to scheduled debt repayments.

*Repurchases of Common Stock.* In November 2007, the Board approved a program to repurchase up to \$200.0 million in shares of our common stock over three years expiring November 9, 2010. We repurchased 1.9 million shares at an aggregate cost of \$50.0 million during the first two quarters of fiscal 2008. As of April 13, 2008, the total remaining amount authorized for repurchase was \$150.0 million.

*Share-based Compensation.* Proceeds from the issuance of common stock decreased \$16.3 million in 2008 reflecting a decline in the exercise of employee stock options compared with 2007, which also resulted in a corresponding decrease in tax benefits from share based compensation. As options granted are exercised, the Company will continue to receive proceeds and a tax deduction, but the amount and the timing of these cash flows cannot be reliably predicted as option holders' decisions to exercise options will be largely driven by movements in the Company's stock price.

*Off-Balance Sheet Arrangements.* Other than operating leases, we are not a party to any off-balance sheet arrangements that have, or are reasonably likely to have, a current or future material effect on our financial condition, changes in financial condition, results of operations, liquidity, capital expenditures or capital resources. We finance a portion of our new restaurant development through sale-leaseback transactions. These transactions involve selling restaurants to unrelated parties and leasing the restaurants back.

**DISCUSSION OF CRITICAL ACCOUNTING ESTIMATES**

We have identified the following as our most critical accounting estimates, which are those that are most important to the portrayal of the Company's financial condition and results and require management's most subjective and complex judgments. Information regarding our other significant accounting estimates and policies are disclosed in Note 1 of our most recent Annual Report on Form 10-K filed with the SEC.

*Share-based Compensation* We account for share-based compensation in accordance with SFAS 123R. Under the provisions of SFAS 123R, share-based compensation cost is estimated at the grant date based on the award's fair-value as calculated by an option pricing model and is recognized as expense ratably over the requisite service period. The option pricing models require various highly judgmental assumptions including volatility, forfeiture rates, and expected option life. If any of the assumptions used in the model change significantly, share-based compensation expense may differ materially in the future from that recorded in the current or prior periods.

*Retirement Benefits* We sponsor pension and other retirement plans in various forms covering those employees who meet certain eligibility requirements. Several statistical and other factors, which attempt to anticipate future events, are used in calculating the expense and liability related to the plans, including assumptions about the discount rate, expected return on plan assets and the rate of increase in compensation levels, as determined by us using specified guidelines. In addition, our outside actuarial consultants also use certain statistical factors such as turnover, retirement and mortality rates to estimate our future benefit obligations. The actuarial assumptions used may differ materially from actual results due to changing market and economic conditions, higher or lower turnover and retirement rates or longer or shorter life spans of participants. These differences may affect the amount of pension expense we record.

*Self Insurance* We are self-insured for a portion of our losses related to workers' compensation, general liability, automotive, medical and dental programs. In estimating our self-insurance accruals, we utilize independent actuarial estimates of expected losses, which are based on statistical analysis of historical data. These assumptions are closely monitored and adjusted when warranted by changing circumstances. Should a greater amount of claims occur compared to what was estimated or medical costs increase beyond what was expected, accruals might not be sufficient, and additional expense may be recorded.

*Long-lived Assets* Property, equipment and certain other assets, including amortized intangible assets, are reviewed for impairment when indicators of impairment are present. This review includes a restaurant-level analysis

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that takes into consideration a restaurant's operating cash flows, the period of time since a restaurant has been opened or remodeled, and the maturity of the related market. When indicators of impairment are present, we perform an impairment analysis on a restaurant-by-restaurant basis. If the sum of undiscounted future cash flows is less than the net carrying value of the asset, we recognize an impairment loss by the amount which the carrying value exceeds the fair value of the asset. Our estimates of future cash flows may differ from actual cash flows due to, among other things, economic conditions or changes in operating performance.

*Goodwill and Other Intangibles* We also evaluate goodwill and intangible assets not subject to amortization annually or more frequently if indicators of impairment are present. If the determined fair values of these assets are less than the related carrying amounts, an impairment loss is recognized. The methods we use to estimate fair value include future cash flow assumptions, which may differ from actual cash flows due to, among other things, economic conditions or changes in operating performance. During the fourth quarter of fiscal 2007, we reviewed the carrying value of our goodwill and indefinite life intangible assets and determined that no impairment existed as of September 30, 2007.

*Allowances for Doubtful Accounts* Our trade receivables consist primarily of amounts due from franchisees for rents on subleased sites, royalties and distribution sales. We continually monitor amounts due and maintain an allowance for doubtful accounts for estimated losses. This estimate is based on our assessment of the collectibility of specific accounts, as well as a general allowance based on historical trends, the financial condition of our franchisees, consideration of the general economy and the aging of such receivables. We have good relationships with our franchisees and high collection rates; however, if the future financial condition of our franchisees were to deteriorate, resulting in their inability to make specific required payments, we may be required to increase the allowance for doubtful accounts.

*Legal Accruals* The Company is subject to claims and lawsuits in the ordinary course of its business. A determination of the amount accrued, if any, for these contingencies is made after analysis of each matter. We continually evaluate such accruals and may increase or decrease accrued amounts as we deem appropriate.

*Income Taxes* We estimate certain components of our provision for income taxes. These estimates include, among other items, depreciation and amortization expense allowable for tax purposes, allowable tax credits, effective rates for state and local income taxes and the tax deductibility of certain other items. We adjust our annual effective income tax rate as additional information on outcomes or events becomes available.

Our estimates are based on the best available information at the time that we prepare the income tax provision. We generally file our annual income tax returns several months after our fiscal year-end. Income tax returns are subject to audit by federal, state and local governments, generally years after the returns are filed. These returns could be subject to material adjustments or differing interpretations of the tax laws.

Effective October 1, 2007, we adopted FASB Interpretation 48, *Accounting for Uncertainty in Income Taxes* an interpretation of FASB Statement No. 109 ( FIN 48 ). FIN 48 requires that a position taken or expected to be taken in a tax return be recognized or derecognized in the financial statements when it is more likely than not (i.e., a likelihood of more than fifty percent) that the position would be sustained upon examination by tax authorities. A recognized tax position is then measured at the largest amount of benefit that is greater than fifty percent likely of being realized upon ultimate settlement.

**NEW ACCOUNTING PRONOUNCEMENTS**

In September 2006, the FASB issued SFAS 157, *Fair Value Measurements*. SFAS 157 clarifies the definition of fair value, describes methods used to appropriately measure fair value, and expands fair value disclosure requirements. This statement applies under other accounting pronouncements that currently require or permit fair value measurements and is effective for fiscal years beginning after November 15, 2007, and interim periods within those years. However, the effective date of SFAS 157 as it relates to fair value measurement requirements for nonfinancial assets and liabilities that are not remeasured at fair value on a recurring basis is deferred to fiscal years beginning after December 15, 2008 and interim periods within those years. We are currently in the process of assessing the impact that SFAS 157 will have on our consolidated financial statements.

In September 2006, the FASB issued SFAS 158, *Employers' Accounting for Defined Benefit Pension and Other Postretirement Plans* an amendment of FASB Statements No. 87, 88, 106 and 132(R). In fiscal 2007, we adopted the

recognition provisions of SFAS 158 which requires recognition of the overfunded or underfunded status of a defined benefit plan as an asset or liability. SFAS 158 also requires that companies measure their plan assets and benefit

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obligations at the end of their fiscal year. The measurement provision of SFAS 158 is effective for fiscal years ending after December 15, 2008. We will not be able to determine the impact of adopting the measurement provision of SFAS 158 until the end of the fiscal year when such valuation is completed.

In February 2007, the FASB issued SFAS 159, *The Fair Value Option for Financial Assets and Financial Liabilities*. SFAS 159 permits entities to voluntarily choose to measure many financial instruments and certain other items at fair value. SFAS 159 is effective for fiscal years beginning after November 15, 2007. We are currently in the process of determining whether to elect the fair value measurement options available under this standard.

In March 2008, the FASB issued SFAS 161, *Disclosures about Derivative Instruments and Hedging Activities*, which amends SFAS 133 and expands disclosures to include information about the fair value of derivatives, related credit risks and a company's strategies and objectives for using derivatives. SFAS 161 is effective for fiscal periods beginning on or after November 15, 2008. We are currently in the process of assessing the impact that SFAS 161 will have on the disclosures in our consolidated financial statements.

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Item 4. Ownership

(i) Mr. Robotti: (1)(2)

(a) Amount beneficially owned: 2,243,326 shares

(b) Percent of class: 7.90%

(c) Number of shares as to which such person has:

(i) Sole power to vote or direct the vote: 10,000 shares

(ii) Shared power to vote or to direct the vote: 2,233,326 shares

(iii) Sole power to dispose or to direct the disposition of: 10,000 shares

(iv) Shared power to dispose or to direct the disposition of: 2,233,326 shares

(ii) ROBT: (1)

(a) Amount beneficially owned: 2,233,326 shares

(b) Percent of class: 7.86%

(c) Number of shares as to which such person has:

(i) Sole power to vote or direct the vote: 0 shares

(ii) Shared power to vote or to direct the vote: 2,233,326 shares

(iii) Sole power to dispose or to direct the disposition of: 0 shares

(iv) Shared power to dispose or to direct the disposition of: 2,233,326 shares

(iii) Robotti Advisors: (1)

(a) Amount beneficially owned: 2,216,633 shares

(b) Percent of class: 7.80%

(c) Number of shares as to which such person has:

(i) Sole power to vote or direct the vote: 0 shares

(ii) Shared power to vote or to direct the vote: 2,216,633 shares

(iii) Sole power to dispose or to direct the disposition of: 0 shares

(iv) Shared power to dispose or to direct the disposition of: 2,216,633 shares

(iv) Robotti Securities: (1)

(a) Amount beneficially owned: 16,523 shares

(b) Percent of class: less than one percent

(c) Number of shares as to which such person has:

(i) Sole power to vote or direct the vote: 0 shares

(ii) Shared power to vote or to direct the vote: 16,523 shares

- (iii) Sole power to dispose or to direct the disposition of: 0 shares
- (iv) Shared power to dispose or to direct the disposition of: 16,523 shares

(v) Mr. Wasiak: (1)

- (a) Amount beneficially owned: 1,030,922 shares
- (b) Percent of class: 3.63%
- (c) Number of shares as to which such person has:
  - (i) Sole power to vote or direct the vote: 0 shares
  - (ii) Shared power to vote or to direct the vote: 1,030,922 shares
  - (iii) Sole power to dispose or to direct the disposition of: 0 shares
  - (iv) Shared power to dispose or to direct the disposition of: 1,030,922 shares

(vi) RMC: (1)

- (a) Amount beneficially owned: 1,030,922 shares
- (b) Percent of class: 3.63%
- (c) Number of shares as to which such person has:
  - (i) Sole power to vote or direct the vote: 0 shares
  - (ii) Shared power to vote or to direct the vote: 1,030,922 shares
  - (iii) Sole power to dispose or to direct the disposition of: 0 shares
  - (iv) Shared power to dispose or to direct the disposition of: 1,030,922 shares

(vii) RIC: (1)

- (a) Amount beneficially owned: 649,599 shares
  - (b) Percent of class: 2.29%
  - (c) Number of shares as to which such person has:
    - (i) Sole power to vote or direct the vote: 0 shares
    - (ii) Shared power to vote or to direct the vote: 649,599 shares
    - (iii) Sole power to dispose or to direct the disposition of: 0 shares
    - (iv) Shared power to dispose or to direct the disposition of: 649,599 shares
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(viii) RI: (1)

- (a) Amount beneficially owned: 381,323 shares
- (b) Percent of class: 1.34%
- (c) Number of shares as to which such person has
  - (i) Sole power to vote or direct the vote: 0 shares
  - (ii) Shared power to vote or to direct the vote: 381,323 shares
  - (iii) Sole power to dispose or to direct the disposition of: 0 shares
  - (iv) Shared power to dispose or to direct the disposition of: 381,323 shares

(ix) OCM: (1)

- (a) Amount beneficially owned: shares: 25,000
- (b) Percent of class: less than one percent
- (c) Number of shares as to which such person has
  - (i) Sole power to vote or direct the vote: 0 shares
  - (ii) Shared power to vote or to direct the vote: 25,000 shares
  - (iii) Sole power to dispose or to direct the disposition of: 0 shares
  - (iv) Shared power to dispose or to direct the disposition of: 25,000 shares

(x) OPF: (1)

- (a) Amount beneficially owned: 25,000 shares
- (b) Percent of class: less than one percent
- (c) Number of shares as to which such person has
  - (i) Sole power to vote or direct the vote: 0 shares
  - (ii) Shared power to vote or to direct the vote: 25,000 shares
  - (iii) Sole power to dispose or to direct the disposition of: 0 shares
  - (iv) Shared power to dispose or to direct the disposition of: 25,000 shares

(xi) Suzanne Robotti: (1)

- (a) Amount beneficially owned: 10,000 shares
- (b) Percent of class: less than one percent
- (c) Number of shares as to which such person has
  - (i) Sole power to vote or direct the vote: 10,000 shares
  - (ii) Shared power to vote or to direct the vote: 0 shares
  - (iii) Sole power to dispose or to direct the disposition of: 10,000 shares
  - (iv) Shared power to dispose or to direct the disposition of: 0 shares

(xii) Mr. Vitetta: (1)

- (a) Amount beneficially owned: 30 shares
- (b) Percent of class: less than one percent
- (c) Number of shares as to which such person has
  - (i) Sole power to vote or direct the vote: 30 shares
  - (ii) Shared power to vote or to direct the vote: 0 shares
  - (iii) Sole power to dispose or to direct the disposition of: 30 shares
  - (iv) Shared power to dispose or to direct the disposition of: 0 shares

\* Based on an aggregate of 28,405,103 shares of Common Stock, par value \$0.10 per share, outstanding as of October 27, 2017, as disclosed in the Issuer's Quarterly Report on Form 10-Q, for the quarter ended September 30, 2017.

(1) Each of the Reporting Persons disclaims beneficial ownership of the securities reported herein by the other Reporting Persons and any other person named herein except to the extent of any pecuniary interest therein. Each of the Reporting Persons disclaims membership in a "group" within the meaning of Section 13(d)(3) of the Securities Exchange Act of 1934, as amended (the "Exchange Act"), or Rule 13d-5(b)(1) under the Exchange Act with any other Reporting Person or other person.

(2) The number of shares reported by Mr. Robotti does not include the shares of Common Stock referenced above in Item 4(xi) owned by Mr. Robotti's wife or the shares of Common Stock referenced above in Item 4(xii) owned by his nephew, all of which shares Mr. Robotti disclaims beneficial ownership.

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Item 5. Ownership of Five Percent or Less of a Class.

Not Applicable.

Item 6. Ownership of More than Five Percent on Behalf of Another Person.

Robotti Securities' discretionary customers and Robotti Advisors' clients have the right to receive and the power to direct the receipt of dividends from, and the proceeds from the sale of, Common Stock owned by them.

Except as set forth in the immediately preceding sentence, no person other than the Reporting Persons is known to have the right to receive or the power to direct the receipt of dividends from, or the proceeds from the sale of, such Common Stock beneficially owned by the Reporting Persons. No discretionary customer or client is known to any Reporting Person to have the right to receive or the power to direct the receipt of dividends from, or the proceeds from the sale of, more than five percent of the Issuer's Common Stock.

Item 7. Identification and Classification of the Subsidiary Which Acquired the Security Being Reported on by the Parent

7. Holding Company or Control Person.

See Item 2 and Note (1) in Item 4.

Item 8. Identification and Classification of Members of the Group.

See Item 2 and Note (1) in Item 4.

Item 9. Notice of Dissolution of Group.

Not Applicable.

Item 10. Certifications:

By signing below we certify that, to the best of our knowledge and belief, the securities referred to above were not acquired and are not held for the purpose of or with the effect of changing or influencing the control of the issuer of the securities and were not acquired and are not held in connection with or as a participant in any transaction having that purpose or effect, other than activities solely in connection with a nomination under §240.14a-11.

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SIGNATURE

After reasonable inquiry and to the best of our knowledge and belief, we certify that the information set forth in this statement is true, complete and correct.

Date: February 1, 2018

Robotti & Company, Incorporated

By: /s/ Robert E. Robotti  
Robert E. Robotti

By: /s/ Robert E. Robotti  
Name: Robert E. Robotti  
Title: President and Treasurer

Robotti & Company Advisors, LLC

By: /s/ Robert E. Robotti  
Name: Robert E. Robotti  
Title: President and Treasurer

/s/ Kenneth R. Wasiak  
Kenneth R. Wasiak

Ravenswood Management Company, L.L.C.

The Ravenswood Investment Company, L.P.

By: /s/ Robert E. Robotti  
Name: Robert E. Robotti  
Title: Managing Member

By: Ravenswood Management Company, L.L.C.  
Its General Partner

Ravenswood Investments III, L.P.

By: /s/ Robert E. Robotti  
Name: Robert E. Robotti  
Title: Managing Member

By: Ravenswood Management Company, L.L.C.  
Its General Partner

Robotti Securities, LLC

By: /s/ Robert E. Robotti  
Name: Robert E. Robotti  
Title: Managing Member

By: /s/ Robert E. Robotti  
Name: Robert E. Robotti  
Title: Managing Member

Ossia Capital Management, L.L.C.

Ossia Partners Fund, L.L.C.

By: /s/ Robert E. Robotti  
Name: Robert E. Robotti  
Title: Managing Member

By: Ossia Capital Management, L.L.C.  
Its General Partner

By: /s/ Robert E. Robotti  
Name: Robert E. Robotti  
Title: Managing Member

/s/ Suzanne Robotti  
Suzanne Robotti

/s/ Daniel Vitetta  
Daniel Vitetta

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Exhibit 2

JOINT FILING AGREEMENT

The undersigned hereby agree to the joint filing of the Statement on Schedule 13G Amendment No. 4 filed herewith, and any amendments thereto, relating to the Common Stock, par value \$.10 per share, of LSB Industries, Inc., with the Securities and Exchange Commission pursuant to and in accordance with the provisions of Rule 13d-1(k)(1)(iii) under the Securities Exchange Act of 1934, as amended.

This Agreement may be executed in separate counterparts, each of which shall be deemed an original, but all of which shall constitute one and the same instrument.

Date: February 1, 2018

Robotti & Company, Incorporated

/s/ Robert E. Robotti  
Robert E. Robotti

By:/s/ Robert E. Robotti  
Name: Robert E. Robotti  
Title: President and Treasurer

Robotti & Company Advisors, LLC

By:/s/ Robert E. Robotti  
Name: Robert E. Robotti  
Title: President and Treasurer

/s/ Kenneth R. Wasiak  
Kenneth R. Wasiak

Ravenswood Management Company, L.L.C.

The Ravenswood Investment Company, L.P.

By:/s/ Robert E. Robotti  
Name: Robert E. Robotti  
Title: Managing Member

By:Ravenswood Management Company, L.L.C.  
Its General Partner

Ravenswood Investments III, L.P.

By:/s/ Robert E. Robotti  
Name: Robert E. Robotti  
Title: Managing Member

By:Ravenswood Management Company, L.L.C.  
Its General Partner

Robotti Securities, LLC

By:/s/ Robert E. Robotti  
Name: Robert E. Robotti  
Title: Managing Member

By:/s/ Robert E. Robotti  
Name: Robert E. Robotti  
Title: Managing Member

Ossia Capital Management, L.L.C.

Ossia Partners Fund, L.L.C.

By:/s/ Robert E. Robotti  
Name: Robert E. Robotti  
Title: Managing Member

By:Ossia Capital Management, L.L.C.  
Its General Partner

By:/s/ Robert E. Robotti  
Name: Robert E. Robotti  
Title: Managing Member

/s/ Suzanne Robotti  
Suzanne Robotti

/s/ Daniel Vitetta  
Daniel Vitetta

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