FULL HOUSE RESORTS INC
Form 10-Q
November 13, 2008

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UNITED STATES SECURITIES AND EXCHANGE COMMISSION
Washington, D.C. 20549
Form 10-Q

(Mark One)

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

For the quarterly period ended September 30, 2008

or

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

For the transition period from __________ to __________

Commission File No. 1-32583

FULL HOUSE RESORTS, INC.

(Exact name of registrant as specified in its charter)

Delaware	**13-3391527**
(State or other jurisdiction of incorporation or organization)	*(I.R.S. Employer Identification No.)*
4670 S. Fort Apache, Ste. 190 Las Vegas, Nevada	**89147**
(Address of principal executive offices)	*(Zip Code)*

(702) 221-7800

(Registrant s telephone number, including area code)

Indicate by check mark whether the registrant: (1) has filed all reports required to be filed by Section 13 or 15(d) of the Securities Exchange Act of 1934 during the preceding 12 months (or for such shorter period that the registrant was required to file such reports), and (2) has been subject to such filing requirements for the past 90 days. Yes þ No o

Indicate by check mark whether the registrant is a large accelerated filer, an accelerated filer, or a non-accelerated filer, or smaller reporting company. See definition of large accelerated filer, accelerated filer and small reporting company in Rule 12b-2 of the Exchange Act. (Check one):

Large Accelerated Filer o Accelerated Filer o Non Accelerated Filer o Smaller reporting company þ

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

As of November 7, 2008, there were 18,540,264 shares of Common Stock, $.0001 par value per share, outstanding.

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FULL HOUSE RESORTS, INC. AND SUBSIDIARIES
CONDENSED CONSOLIDATED BALANCE SHEETS

	September 30, 2008	December 31, 2007
ASSETS		
Current assets		
Cash	$ 6,620,762	$ 7,975,860
Accounts receivable, net	631,714	319,865
Income tax refund receivable	248,868	
Prepaid expenses	401,567	351,658
Deposits and other current assets	133,604	172,120
Assets held for sale	45,000	6,960,762
	8,081,515	15,780,265
Property and equipment, net of accumulated depreciation of $4,689,462 and $3,848,439	8,756,455	9,227,113
Long-term assets related to tribal casino projects		
Notes receivable	4,985,177	12,178,481
Contract rights, net of accumulated amortization of $714,019 and $670,927	16,810,761	14,761,133
	21,795,938	26,939,614
Other long-term assets		
Goodwill	10,308,520	10,308,520
Deposits and other	840,850	868,265
	11,149,370	11,176,785
	$ 49,783,278	$ 63,123,777
LIABILITIES AND STOCKHOLDERS EQUITY		
Current liabilities		
Current portion of long-term debt	$ 221,086	$ 259,124
Accounts payable	287,153	274,411
Accrued expenses	1,055,378	1,364,293
	1,563,617	1,897,828
Long-term liabilities		
Long-term debt due to joint venture affiliate, including accrued interest of $113,580 and $17,231	2,968,070	1,272,709
Other long-term debt, net of current portion	3,753,590	21,693,314
Deferred income tax liability	1,041,869	359,023
	9,327,146	25,222,874

Noncontrolling interest in consolidated joint venture	4,713,515	4,232,775
Stockholders equity		
Common stock, $.0001 par value, 25,000,000 shares authorized; 19,350,276 shares issued and 19,230,605 shares outstanding in 2008, and 19,342,276 shares issued and outstanding in 2007	1,935	1,934
Additional paid-in capital	42,716,771	42,702,372
Treasury stock, 119,671 shares in 2008	(182,010)	
Deferred compensation	(515,135)	(1,145,329)
Deficit	(6,278,944)	(7,890,849)
	35,742,617	33,668,128
	$ 49,783,278	$ 63,123,777

See notes to unaudited condensed consolidated financial statements.

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FULL HOUSE RESORTS, INC. AND SUBSIDIARIES
UNAUDITED CONDENSED CONSOLIDATED STATEMENTS OF OPERATIONS

	Three months ended September 30,		Nine months ended September 30,	
	2008	**2007**	**2008**	**2007**
Revenues				
Casino	$ 1,925,134	$ 2,031,271	$ 5,694,645	$ 5,385,458
Food and beverage	498,175	587,103	1,633,989	1,452,885
Other operating income	21,017	14,223	72,285	333,108
	2,444,326	2,632,597	7,400,919	7,171,451
Operating costs and expenses				
Casino	541,732	584,205	1,819,068	1,664,040
Food and beverage	599,502	534,368	1,754,819	1,407,200
Project development costs	62,392	102,541	133,024	348,274
Selling, general and administrative	1,534,118	1,446,772	4,866,210	5,254,049
Depreciation and amortization	306,889	326,874	902,123	932,568
	3,044,633	2,994,760	9,475,244	9,606,131
Operating gains (losses)				
Equity in net income of unconsolidated joint venture, and related guaranteed payments	1,372,168	1,022,340	3,566,950	3,096,045
Unrealized gains (losses) on notes receivable, tribal governments	137,356	(209,106)	1,974,040	719,195
Impairment loss, land previously held for development			(85,000)	
	1,509,524	813,234	5,455,990	3,815,240
Income from continuing operations before other income (expense) and noncontrolling interest in net income (loss) of consolidated joint venture and income taxes	909,217	451,071	3,381,665	1,380,560
Other income (expense)				
Interest and other income	33,196	378,057	128,873	664,536
Interest expense	(122,381)	(329,330)	(420,767)	(952,605)
Income from continuing operations before noncontrolling interest in net income (loss) of consolidated joint venture and income taxes	820,032	499,798	3,089,771	1,092,491
Noncontrolling interest in net (income) loss of consolidated joint venture	94,506	(12,044)	(480,740)	(123,634)
Income from continuing operations before income taxes	914,538	487,754	2,609,031	968,857

Income taxes		(374,865)		33,077		(1,035,268)		(251,324)
Income from continuing operations		539,673		520,831		1,573,763		717,533
Income from discontinued operations, net of tax				83,960		38,142		214,461
Net income	$	539,673	$	604,791	$	1,611,905	$	931,994
Income from continuing operations per common share								
Basic and diluted	$	0.03	$	0.03	$	0.08	$	0.04
Income from discontinued operations per common share								
Basic and diluted	$	0.00	$	0.00	$	0.00	$	0.01
Net income per common share								
Basic and diluted	$	0.03	$	0.03	$	0.08	$	0.05
Weighted-average number of common shares outstanding								
Basic and diluted		19,332,356		19,342,276		19,338,969		19,291,437

See notes to unaudited condensed consolidated financial statements.

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FULL HOUSE RESORTS, INC. AND SUBSIDIARIES
UNAUDITED CONDENSED CONSOLIDATED STATEMENTS OF CASH FLOWS

	Nine months ended September 30, 2008	2007
Net cash provided by operating activities	$ 1,550,235	$ 2,150,515
Investing activities:		
Deposits and other cash costs of the Stockman s Casino acquisition, net of cash acquired of $920,824		(8,317,493)
Acquisition of contract rights and other assets	(2,092,720)	(402,261)
Purchase of property and equipment	(379,517)	(157,510)
Advances to tribal governments, net of $2,124 and $33,277 expensed	(86,123)	(308,323)
Proceeds from sale of assets	6,961,020	900
Proceeds from repayment of tribal advances	9,253,467	
Other	(700)	
Net cash provided by (used in) investing activities	13,655,427	(9,184,687)
Financing activities:		
Payments on long-term debt	(17,977,762)	(4,721,790)
Proceeds from borrowings from joint venture affiliate	1,599,012	
Purchase of treasury stock	(182,010)	
Dividends paid		(3,042,084)
Net cash used in financing activities	(16,560,760)	(7,763,874)
Net decrease in cash	(1,355,098)	(14,798,046)
Cash, beginning of period	7,975,860	22,117,482
Cash, end of period	$ 6,620,762	$ 7,319,436

See notes to unaudited condensed consolidated financial statements.

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FULL HOUSE RESORTS, INC. AND SUBSIDIARIES
NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS (UNAUDITED)

1. BASIS OF PRESENTATION

The interim condensed consolidated financial statements of Full House Resorts, Inc. and its subsidiaries (collectively, the Company) included herein reflect all adjustments that are, in the opinion of management, necessary to present fairly the financial position and results of operations for the interim periods presented. Certain information normally included in annual financial statements prepared in accordance with accounting principles generally accepted in the United States of America has been omitted pursuant to the interim financial information rules and regulations of the United States Securities and Exchange Commission.

These unaudited interim condensed consolidated financial statements should be read in conjunction with the annual audited consolidated financial statements and notes thereto included in the Company s Annual Report on Form 10-KSB/A (Amendment No. 1), filed April 1, 2008, for the year ended December 31, 2007, from which the balance sheet information as of that date was derived. Certain minor reclassifications to amounts previously reported have been made to conform to the current period presentation, none of which affected previously reported net income or earnings per share. The results of operations for the period ended September 30, 2008, are not necessarily indicative of the results to be expected for the year ending December 31, 2008.

The condensed consolidated financial statements include the accounts of the Company and its wholly-owned subsidiaries, including Stockman s Casino (Stockman s). Gaming Entertainment (Michigan), LLC (GEM), a 50%-owned investee of the Company that is jointly owned by RAM Entertainment, LLC (RAM) (Note 10), has been consolidated pursuant to the guidance in Financial Accounting Standards Board (FASB) Interpretation No. 46R, *Consolidation of Variable Interest Entities*. The Company accounts for its investment in Gaming Entertainment (Delaware), LLC (GED) (Note 3) using the equity method of accounting. All material intercompany accounts and transactions have been eliminated.

2. SHARE-BASED COMPENSATION

For the three months ended September 30, 2008 and 2007, the Company recognized share-based compensation expense of $223,959 and $228,844, respectively, related to the amortization of restricted stock grants in prior years and a stock grant in July 2008, which is included in selling, general and administrative expenses. For the nine months ended September 30, 2008 and 2007, share-based compensation expense recognized was $644,594 and $1,364,060, respectively. At September 30, 2008, the Company had deferred share-based compensation of $515,135, which is expected to be amortized through February 2010 using the straight-line method, by employee. Specifically, the Company expects to recognize share-based compensation expense of $209,561 in the fourth quarter of 2008, $288,885 in 2009 and $16,689 in 2010.

3. INVESTMENT IN UNCONSOLIDATED JOINT VENTURE

The Company s investment in unconsolidated joint venture is comprised of a 50% ownership interest in GED, a joint venture between the Company and Harrington Raceway Inc (HRI). GED has a management agreement with Harrington Raceway and Casino (Harrington) (formerly known as Midway Slots and Simulcast), which is located in Harrington, Delaware. GED has no non-operating income or expenses, is treated as a partnership for income tax purposes and consequently recognizes no federal or state income tax provision. As a result, income from operations for GED is equal to net income for each period presented, and there are no material differences between its income for financial and tax reporting purposes.

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On June 18, 2007, the Company restructured its joint venture agreement with HRI to allow HRI greater flexibility in GED s management of the facility while providing the Company with guaranteed growth in its share of GED s net income for the remaining term of the management contract. Under the terms of the restructured joint venture agreement, the Company is to receive the greater of 50% of GED s net income as currently prescribed under the joint venture agreement, or an 8% increase in its 50% share of GED s 2007 net income. The 8% guaranteed growth factor applied to the 2007 net income takes into account the expansion at Harrington that was completed in February 2008, and resets to an annual 5% growth rate in 2009 through the expiration of the GED management contract in August 2011. As a result of the restructured joint venture agreement, the Company has received or accrued additional guaranteed payments of $474,118 and 681,742 for the three and nine months ended September 30, 2008, respectively, which is included in the equity in net income of GED in the accompanying consolidated financial statements.

Unaudited summary information for GED s operations is as follows:

	Three months ended September 30,		**Nine months ended September 30,**	
	2008	**2007**	**2008**	**2007**
Management fee revenues	$ 1,891,311	$ 2,177,901	$ 6,072,794	$ 6,561,511
Net income	1,796,144	2,044,678	5,770,416	6,192,088

4. FAIR VALUE MEASUREMENTS

On January 1, 2008, the Company adopted the methods of fair value accounting described in Statement of Financial Accounting Standards No. 157*, Fair Value Measurements* (SFAS No. 157), to value its financial assets that were previously carried at estimated fair value. The adoption of SFAS No. 157 in the first quarter of 2008 did not have any effect on the Company s previously used fair value estimation methodology or on net income. Financial Accounting Standards Board Staff Position FAS 157-3, *Determining the Fair Value of Financial Asset when the market for that asset is not active*, (FSP FAS 157-3) was issued in October 2008 and was retroactively effective for the quarter ended September 30, 2008. The implementation of FSP FAS 157-3 did not have a material impact on the Company s valuation techniques, financial position, results of operations and cash flows.

To date, the Company has chosen not to elect the fair value option as offered by Statement of Financial Accounting Standards No. 159, *The Fair Value Option for Financial Assets and Financial Liabilities including an amendment of FAS 115,* for its financial assets and liabilities that had not been previously carried at fair value. Therefore, material financial assets and liabilities not carried at fair value are still reported on a historical cost basis.

The Company s financial assets that are measured at estimated fair value use inputs from among the three levels of the fair value hierarchy set forth in SFAS No. 157 as follows:

Level 1 inputs: Unadjusted quoted prices in active markets for identical assets or liabilities, which prices are available at the measurement date.

Level 2 inputs: Include quoted prices for similar assets and liabilities in active markets, quoted prices for identical or similar assets and liabilities in markets that are not active, inputs other than quoted prices that are observable for the asset or liability (*i.e.* interest rates, yield curves, *etc.*) and inputs that are derived principally from or corroborated by observable market data by correlation or other means (marked corroborated inputs).

Level 3 inputs: Unobservable inputs that reflect management s estimates about the assumptions that market participants would use in pricing the asset or liability. Management develops these inputs based on the best information available, including internally-developed data.

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The Company has no financial assets that are measured using level 1 or 2 inputs. Due to the absence of observable market quotes on the Company s notes receivable from tribal governments (Note 5), the Company utilizes valuation models that rely exclusively on Level 3 inputs, including those that are based on management s estimates of expected cash flow streams, future interest rates, casino opening dates and discount rates. The estimated casino opening dates used in the valuations take into account project-specific circumstances such as ongoing litigation, the status of required regulatory approvals, construction periods and other factors. Factors considered in the determination of an appropriate discount rate include discount rates typically used by gaming industry investors and appraisers to value individual casino properties outside of Nevada, and discount rates produced by the widely-accepted Capital Asset Pricing Model (CAPM). The following key assumptions are used in the CAPM:

S&P 500, average benchmark investment returns (medium-term horizon risk premiums);

Risk free investment return equal to the trailing 10-year average for 90-day treasury bills;

Investment beta factor equal to the average of a peer group of similar entities in the hotel and gaming industry;

Project-specific adjustments based on the status of the project (*i.e.*, litigation, regulatory approvals, tribal politics, *etc.*), and typical size premiums for micro-cap and low-cap companies.

A tabular summary of the current period activity related to notes receivable from tribal governments, is presented in Note 5.

5. NOTES RECEIVABLE, TRIBAL GOVERNMENTS

The Company has notes receivable related to advances to tribes to fund tribal operations and development expenses related to potential casino projects. Repayment of these notes is contingent upon the development of the projects, and ultimately, the successful operation of the facilities. The Company s agreements with the tribes provide for the reimbursement of these advances plus applicable interest either from the proceeds of any outside financing of the development, the actual operation itself or in the event that the Company does not complete the development, from the revenues of the tribal gaming operation following completion of development activities undertaken by others.

As of September 30, 2008, and December 31, 2007, notes receivable from tribal governments as follows:

	September 30, 2008	December 31, 2007 *
Contractual (stated) amount (including interest)		
FireKeepers Development Authority	$ 5,000,000	$ 14,250,815
Other	1,281,329	1,308,859
	$ 6,281,329	$ 15,559,674
Estimated fair value of notes receivable related to tribal casino projects:		
FireKeepers Development Authority	$ 3,931,389	$ 11,189,359
Other	1,053,788	989,122
	$ 4,985,177	$ 12,178,481

* Presentation of contractual amounts as of

December 31, 2007, has been revised to conform to the current year presentation, and now include accrued interest of $1,475,574. The inclusion of interest in the 2007 period was solely for comparability and did not change previously reported net income, since the related receivables, including accrued interest, are presented at their estimated fair values.

On May 6, 2008, the FireKeepers Development Authority (the Authority) closed on the sale of $340 million of Senior Secured Notes and a $35 million equipment financing facility to fund the development and construction of the Authority s FireKeepers Casino in Michigan. On the same date, GEM received a payment of approximately $9.3 million on its notes receivable from the Authority which resulted in an increase in the estimated fair value of the notes receivable of approximately $1.8 million recorded as an unrealized gain in the first quarter of 2008. The remaining $5.0 million is to be paid 180 days following the opening of the casino, subject to there being adequate funds remaining in the construction disbursement account. If there are insufficient funds to repay the remaining balance, the Authority will be obligated to repay the balance in 60 monthly installments beginning 180 days following the opening of the casino, with interest at prime plus 1%.

As of September 30, 2008, management extended its estimate of the opening date for the Montana casino from the fourth quarter of 2009 to the second quarter of 2010. Management had expected that the tribe would receive key federal and state approvals during the third quarter which were not received. Management also expects that a pending change in the federal administration will further delay the approval process until the second quarter of next year. The effect of the change in the estimated opening date reduced the estimated fair value of the note receivable related to the Montana project by $51,364 as of September 30, 2008.

In March 2008, management formally decided to discontinue pursuing the Nambé Pueblo project. However, the Pueblo has affirmed its responsibility to repay reimbursable development advances of approximately $662,000, plus interest at prime plus 2%, out of any future gaming revenues, if any. Management currently believes that the Nambé Pueblo intends to develop a slot machine operation with approximately 200 devices, which would be attached to its travel center and provide the Nambé Pueblo with the financial wherewithal to repay the amounts owed to the Company. Accordingly, management has estimated the fair value of the note receivable from the Nambé Pueblo at $484,874 as of September 30, 2008.

The following table summarizes the changes in the estimated fair value of notes receivable from tribal governments, determined using Level 3 fair value inputs, from January 1, 2008, to September 30, 2008:

	Total	FireKeepers Development Authority	Other tribes
Balances, January 1, 2008	$ 12,178,481	$ 11,189,359	$ 989,122
Total advances	108,029		108,029
Advances allocated to contract rights	(24,030)		(24,030)
Advances expensed as period costs	2,124	2,124	
Repayment of notes receivable	(9,253,467)	(9,253,467)	
Unrealized gains (losses) included in earnings	1,974,040	1,993,373	(19,333)
Balances, September 30, 2008	$ 4,985,177	$ 3,931,389	$ 1,053,788

6. CONTRACT RIGHTS

At September 30, 2008 and December 31, 2007, contract rights consist of the following:

September 30, 2008	**Cost**	**Accumulated Amortization**	**Carrying value**
FireKeepers project, initial cost	$ 4,155,213	$	$ 4,155,213
FireKeepers project, additional	13,210,373	(714,019)	12,496,354
Other projects	159,194		159,194

	$ 17,524,780	$ (714,019)	$ 16,810,761

December 31, 2007	**Cost**	**Accumulated Amortization**	**Carrying Value**
FireKeepers project, initial cost	$ 4,155,213	$	$ 4,155,213
FireKeepers project, additional	11,141,683	(670,927)	10,470,756
Other projects	135,164		135,164
	$ 15,432,060	$ (670,927)	$ 14,761,133

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In connection with the Authority s financing of the FireKeepers Casino development in the second quarter of 2008, GEM funded $2,068,690 of financing costs on behalf of the Authority, as required by the management agreement, which was recorded as additional contract rights related to the FireKeepers project. The financing costs p