

FINISH LINE INC /IN/  
Form 10-Q  
December 20, 2006

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**SECURITIES AND EXCHANGE COMMISSION**

**WASHINGTON, D.C. 20549**

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**FORM 10-Q**

(Mark One)

**QUARTERLY REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934**  
For the quarterly period ended November 25, 2006

OR

**TRANSITION REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934**  
For the transition period from \_\_\_\_\_ to \_\_\_\_\_

Commission File number 0-20184

**The Finish Line, Inc.**

(Exact name of registrant as specified in its charter)

**Indiana**  
(State or other jurisdiction)

**35-1537210**  
(I.R.S. Employer identification number)

of incorporation or organization)

**3308 North Mitthoeffer Road Indianapolis, Indiana**  
(Address of principal executive offices)

**46235**  
(zip code)

**317-899-1022**

(Registrant's telephone number, including area code)

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(Former name, former address and former fiscal year, if changed since last report.)

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(Former name, former address and former fiscal year, if changed since last report.)

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, or a non-accelerated filer. See definition of accelerated filer and large accelerated filer in Rule 12b-2 of the Exchange Act.

Large accelerated filer  Accelerated filer  Non-accelerated filer

Indicate by check mark whether the registrant is a shell company (as defined in Rule 12b-2 of the Exchange Act).

Yes  No

Shares of common stock outstanding at December 15, 2006:

Class A	41,931,260
Class B	5,141,336

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## PART 1. FINANCIAL INFORMATION

## ITEM 1. FINANCIAL STATEMENTS

## THE FINISH LINE, INC.

## CONSOLIDATED BALANCE SHEETS

(In thousands)

	November 25, 2006 (unaudited)	November 26, 2005 (unaudited)	February 25, 2006
<b>ASSETS</b>			
<b>CURRENT ASSETS:</b>			
Cash and cash equivalents	\$ 12,899	\$ 39,339	\$ 47,488
Marketable securities			49,075
Accounts receivable, net	17,802	16,254	11,999
Merchandise inventories, net	356,856	311,453	268,590
Income taxes recoverable		254	4,375
Other	5,948	10,690	
Total current assets	393,505	377,990	381,527
<b>PROPERTY AND EQUIPMENT:</b>			
Land	1,557	1,557	1,557
Building	39,529	34,014	33,757
Leasehold improvements	283,342	242,879	243,312
Furniture, fixtures, and equipment	112,268	90,740	93,221
Construction in progress	3,251	2,989	10,753
	439,947	372,179	382,600
Less accumulated depreciation	184,437	157,116	161,418
	255,510	215,063	221,182
Deferred income taxes	14,162	1,361	11,118
Intangible assets	13,751	14,074	13,989
Total assets	\$ 676,928	\$ 608,488	\$ 627,816

See accompanying notes.

## THE FINISH LINE, INC.

## CONSOLIDATED BALANCE SHEETS

(In thousands)

	November 25, 2006 (unaudited)	November 26, 2005 (unaudited)	February 25, 2006
<b>LIABILITIES AND SHAREHOLDERS EQUITY</b>			
<b>CURRENT LIABILITIES:</b>			
Accounts payable	\$ 118,579	\$ 108,317	\$ 84,006
Short-term borrowings	20,400		
Employee compensation	8,919	8,732	12,026
Accrued property and sales tax	6,137	6,540	8,254
Deferred income taxes	13,291	8,703	12,429
Other liabilities and accrued expenses	17,640	20,335	25,700
<b>Total current liabilities</b>	<b>184,966</b>	<b>152,627</b>	<b>142,415</b>
Deferred credits from landlords	64,379	56,216	56,859
<b>SHAREHOLDERS EQUITY:</b>			
Preferred stock, \$.01 par value; 1,000 shares authorized; none issued			
Common stock, \$.01 par value			
Class A:			
Shares authorized - 100,000			
Shares issued 47,649			
Shares outstanding - (November 25, 2006 41,928; November 26, 2005 42,709; February 25, 2006 42,865)	476	476	476
Class B:			
Shares authorized 10,000			
Shares issued and outstanding 5,141	52	52	52
Additional paid-in capital	148,129	141,286	142,645
Retained earnings	327,391	292,797	319,656
Treasury stock - (November 25, 2006 5,721; November 26, 2005 4,940; February 25, 2006 4,784)	(48,465)	(34,966)	(34,287)
<b>Total shareholders equity</b>	<b>427,583</b>	<b>399,645</b>	<b>428,542</b>
<b>Total liabilities and shareholders equity</b>	<b>\$ 676,928</b>	<b>\$ 608,488</b>	<b>\$ 627,816</b>

See accompanying notes.

## THE FINISH LINE, INC.

## CONSOLIDATED STATEMENTS OF OPERATIONS

(In thousands, except per share amounts)

(Unaudited)

	Thirteen Weeks Ended		Thirty Nine Weeks Ended	
	November 25, 2006	November 26, 2005	November 25, 2006	November 26, 2005
Net sales	\$ 281,507	\$ 273,980	\$ 909,188	\$ 906,820
Cost of sales (including occupancy expenses)	203,639	196,432	643,578	627,474
Gross profit	77,868	77,548	265,610	279,346
Selling, general, and administrative expenses	82,655	76,540	248,254	228,794
Operating income (loss)	(4,787)	1,008	17,356	50,552
Interest income (expense), net	(21)	345	864	1,406
Income (loss) before income taxes	(4,808)	1,353	18,220	51,958
Provision (benefit) for income taxes	(1,828)	508	6,923	19,485
Net income (loss)	\$ (2,980)	\$ 845	\$ 11,297	\$ 32,473
Basic net income (loss) per share	\$ (.06)	\$ .02	\$ .24	\$ .67
Basic weighted average shares	46,909	48,312	47,328	48,740
Diluted net income (loss) per share	\$ (.06)	\$ .02	\$ .24	\$ .65
Diluted weighted average shares	46,909	49,058	47,882	49,605
Dividends declared per share	\$ .025	\$ .025	\$ .075	\$ .075

See accompanying notes.

## THE FINISH LINE, INC.

## CONSOLIDATED STATEMENTS OF CASH FLOW

(In thousands) - (Unaudited)

	Thirty-Nine Weeks Ended	
	November 25, 2006	November 26, 2005
<b>OPERATING ACTIVITIES:</b>		
Net income	\$ 11,297	\$ 32,473
Adjustments to reconcile net income to net cash used in operating activities:		
Depreciation and amortization	28,679	24,870
Deferred income taxes	(2,182)	695
Share-based compensation	4,302	501
Loss on disposal of property and equipment	339	7
Tax benefit from exercise of stock options		1,871
Excess tax benefits from share-based compensation	(1,200)	
Changes in operating assets and liabilities:		
Accounts receivable	(5,803)	(2,024)
Merchandise inventories	(88,266)	(70,211)
Other current assets	(1,573)	(7,528)
Accounts payable	34,573	15,939
Employee compensation	(3,107)	(4,151)
Other liabilities and accrued expenses	(7,456)	666
Deferred credits from landlords	7,520	5,684
Net cash used in operating activities	(22,877)	(1,208)
<b>INVESTING ACTIVITIES:</b>		
Purchases of property and equipment	(63,334)	(51,432)
Proceeds from disposal of property and equipment	226	24
Lease acquisition costs		(17)
Settlement of Man Alive holdback	(1,500)	
Proceeds from sale of available-for-sale marketable securities	155,475	249,575
Purchases of available-for-sale marketable securities	(106,400)	(192,400)
Net cash (used in) provided by investing activities	(15,533)	5,750
<b>FINANCING ACTIVITIES:</b>		
Proceeds from short-term borrowings	57,600	
Repayments on short-term borrowings	(37,200)	
Dividends paid to shareholders	(3,582)	(3,670)
Proceeds from issuance of shares	1,422	2,341
Excess tax benefits from share-based compensation	1,200	
Purchase of treasury stock	(15,619)	(19,865)
Net cash provided by (used in) financing activities	3,821	(21,194)
Net decrease in cash and cash equivalents	(34,589)	(16,652)
Cash and cash equivalents at beginning of period	47,488	55,991
Cash and cash equivalents at end of period	\$ 12,899	\$ 39,339

See accompanying notes.



**The Finish Line, Inc.**

**NOTES TO CONSOLIDATED FINANCIAL STATEMENTS**

**(Unaudited)**

**1. Summary of Significant Accounting Policies**

**Basis of Presentation**

The accompanying unaudited consolidated financial statements of The Finish Line, Inc., along with its wholly-owned subsidiaries, (collectively, the Company) have been prepared in accordance with accounting principles generally accepted in the United States for interim financial information and with instructions to Form 10-Q and Article 10 of Regulation S-X. Accordingly, they do not include all the information and footnotes required by accounting principles generally accepted in the United States for complete financial statements. Preparation of the financial statements requires management to make estimates and assumptions that affect the amounts reported in the financial statements and accompanying notes. Actual results could differ from these estimates. In the opinion of management, all adjustments, consisting only of normal recurring adjustments, considered necessary for a fair presentation, have been included.

The Company has experienced, and expects to continue to experience, significant variability in sales and net income from reporting period to reporting period. Therefore, the results of the interim periods presented herein are not necessarily indicative of the results to be expected for any other interim period or the full year.

Certain amounts in the financial statements of the prior year have been reclassified to conform to the current year presentation. These reclassifications had no effect on net income.

These financial statements should be read in conjunction with the financial statements and notes thereto contained in the Company's Annual Report on Form 10-K for the year ended February 25, 2006 (fiscal 2006).

**Recently Issued Accounting Pronouncements**

In June 2006, the Financial Accounting Standards Board (FASB) issued Interpretation No. 48, *Accounting for Uncertainty in Income Taxes an interpretation of FASB Statement No. 109* (FIN 48). FIN 48 clarifies the recognition threshold and measurement principles for the financial statement recognition and measurement of a tax position taken or expected to be taken in a tax return. FIN 48 also provides guidance on derecognition, classification, interest and penalties, accounting in interim periods, disclosure and transition. FIN 48 is effective for fiscal years beginning after December 15, 2006 (fiscal year 2008). The Company is currently evaluating the provisions of FIN 48.

In June 2006, the FASB ratified the Emerging Issues Task Force (EITF) consensus on EITF Issue No. 06-3, *How Taxes Collected from Customers and Remitted to Governmental Authorities Should Be Presented in the Income Statement (That Is, Gross versus Net Presentation)*. EITF Issue No. 06-3 states that the classification of taxes as gross or net is an accounting policy decision that is dependent on type of tax and that similar taxes are to be presented in a similar manner. EITF Issue No. 06-3 is effective for reporting periods beginning after December 15, 2006. EITF Issue No. 06-3 will not impact the method for recording sales taxes in the Company's consolidated financial statements as the Company has historically presented sales excluding all taxes.



In September 2006, the FASB issued Statement of Financial Accounting Standards ( SFAS ) No. 157, *Fair Value Measurements* ( SFAS No. 157 ). SFAS No. 157 provides guidance for using fair value to measure assets and liabilities and only applies when other standards require or permit the fair value measurement of assets and liabilities. It does not expand the use of fair value measurement. SFAS No. 157 is effective for fiscal years beginning after November 15, 2007. Adoption of SFAS No. 157 is not expected to have a material impact on the Company's results of operations, financial condition or liquidity.

## 2. Stock Based Compensation

On February 26, 2006, the Company adopted SFAS No. 123(R), *Share-Based Payment* ( SFAS 123(R) ), which requires the measurement and recognition of compensation expense for all share-based awards made to employees and directors based on estimated fair values on the grant date. SFAS 123(R) supersedes the Company's previous accounting under Accounting Principles Board Opinion No. 25, *Accounting for Stock Issued to Employees* ( APB 25 ) for periods beginning in fiscal 2007.

SFAS 123(R) requires companies to estimate the fair value of share-based awards on the date of grant and recognize as expense the value of the portion of the award that is ultimately expected to vest over the requisite service period. Prior to the adoption of SFAS 123(R), the Company accounted for share-based awards to employees and directors in accordance with APB 25. Under APB 25, no share-based compensation expense was recognized in the Company's Consolidated Statements of Operations for stock options granted to employees and directors when the exercise price equaled the fair market value of the underlying stock at the date of grant.

The Company adopted SFAS 123(R) using the modified prospective transition method, which requires the application of the accounting standard as of February 26, 2006, the first day of the Company's fiscal year 2007. The Company's Consolidated Financial Statements as of and for the thirteen and thirty-nine weeks ended November 25, 2006 reflect the impact of SFAS 123(R). In accordance with the modified prospective transition method, the Company's Consolidated Financial Statements for prior periods have not been restated to reflect, and do not include, the impact of SFAS 123(R).

Under the modified prospective transition method, share-based compensation expense recognized in the Company's Consolidated Statements of Operations for the thirteen and thirty-nine weeks ended November 25, 2006 and for the balance of fiscal year 2007 will include compensation expense for:

Unvested share-based awards granted prior to February 26, 2006, based on the grant date fair value determined in accordance with the pro forma provisions of SFAS No. 123 *Accounting for Stock-Based Compensation* ( SFAS 123 ).

Share-based awards granted subsequent to February 26, 2006, based on the grant date fair value determined in accordance with the provisions of SFAS 123(R).

Total share-based compensation expense recognized under SFAS 123(R) for the thirteen and thirty-nine weeks ended November 25, 2006 was \$1.4 and \$4.3 million, respectively. Share-based compensation expense of \$0.3 and \$0.5 million for the thirteen and thirty-nine weeks ended November 26, 2005 related to options that were granted in prior years that had an exercise price below the fair market value on the date of grant, which the Company expensed under APB 25 over the requisite service period.

Share-based compensation expense recognized in the Consolidated Statements of Operations for the thirteen and thirty-nine weeks ended November 25, 2006 is based on awards ultimately expected to vest, and accordingly has been reduced for estimated forfeitures. SFAS 123(R) requires forfeitures to be estimated at the time of grant and revised, if necessary, in subsequent periods if actual forfeitures differ from those estimates. As a result, beginning in fiscal 2007, the Company began applying an estimated forfeiture rate based on historical data to determine the amount of compensation expense recognized in the Consolidated Statements of Operations. Prior to 2007, the Company used the actual forfeiture method allowed under SFAS 123, which assumed that all options would vest and pro forma expense was only adjusted when options were actually forfeited prior to the vesting dates.

Compensation expense for stock options is recognized, net of forfeitures, over the requisite service period on a straight-line basis, using a single option approach (each option is valued as one grant, irrespective of the number of vesting tranches). Restricted stock expense is recognized, net of forfeitures, on a straight-line basis over the requisite service period.

As a result of adopting SFAS 123(R) on February 26, 2006, the Company's income (loss) before income taxes and net income (loss) for the thirteen weeks ended November 25, 2006 are \$1.1 million and \$0.7 million lower, respectively, and for the thirty-nine weeks ended November 25, 2006, are \$3.2 million and \$2.0 million lower, respectively, than if it had continued to account for share-based compensation under APB 25. Basic and diluted earnings per share for the thirteen weeks ended November 25, 2006 are \$0.01 lower and for the thirty-nine weeks ended November 25, 2006 are \$0.04 lower than if the Company had continued to account for share-based compensation under APB 25.

Prior to the adoption of SFAS 123(R), the Company presented all tax benefits of deductions resulting from the exercise of stock options as operating cash flows in the Consolidated Statements of Cash Flows. SFAS 123(R) requires the cash flows resulting from the tax benefits resulting from tax deductions in excess of the compensation cost recognized for those options (excess tax benefits) to be classified as financing cash flows. The \$1.2 million excess tax benefit classified as a financing cash inflow would have been classified as an operating cash inflow if the Company had continued to account for share-based compensation under APB 25.

The following table is presented for comparative purposes and illustrates the pro forma effect on net income and earnings per share as if the Company had applied the fair value recognition provisions of SFAS 123 to share-based employee compensation prior to February 26, 2006 (in thousands except per share data):

	<b>Thirteen weeks ended November 26, 2005</b>	<b>Thirty-nine weeks ended November 26, 2005</b>
	<b>(in thousands except per share amounts)</b>	
Net income as reported	\$ 845	\$ 32,473
Total share-based employee compensation expense using the fair value based method, net of related tax	(1,154)	(2,827)
Share-based employee compensation expense recorded, net of related tax	164	314
Pro forma net income (loss)	\$ (145)	\$ 29,960
<b>Diluted net income per share:</b>		
As reported	\$ .02	\$ .65
Pro forma	\$ .61	\$ .61
<b>Basic net income per share:</b>		
As reported	\$ .02	\$ .67
Pro forma	\$ .62	\$ .62

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The Company will continue to use the Black-Scholes option-pricing model for valuation of options granted to employees and directors. The Company's determination of the fair value of options is affected by the Company's stock price as well as assumptions regarding a number of highly complex and subjective variables. These variables include, but are not limited to, the Company's expected stock price volatility over the term of the awards and projected employee stock option exercise behaviors.

The weighted-average estimated fair value of employee stock options granted during the thirty-nine weeks ended November 25, 2006 and November 26, 2005 was \$6.40 and \$6.51, respectively, per share based on the following weighted-average assumptions:

	Thirty-nine weeks ended	
	November 25, 2006	November 26, 2005
Expected volatility	45.0%	49.8%
Risk-free interest rate	4.7%	4.1%
Dividend yield	.76%	.66%
Expected life (years)	4.5	5.0

The expected volatility assumption is based on the Company's analysis of historical volatility. The risk-free interest rate assumption is based upon the average daily closing rates during the quarter for U.S. treasury notes that have a life, which approximates the expected life of the option. The dividend yield assumption is based on the Company's history and expectation of future dividend payouts. The expected life of employee stock options represents the weighted-average period the stock options are expected to remain outstanding.

Fair value of restricted stock awards is based on the market value of an unrestricted share on the grant date.

The Company's stock option activity for the thirty-nine weeks ended November 25, 2006 was as follows:

	Number of Shares	Weighted Average Option Price Per Share	Weighted Average Remaining Contractual Life (Years)	Aggregate Intrinsic Value
Outstanding at February 25, 2006	3,115,720	\$ 10.87		
Granted	370,500	\$ 15.54		
Exercised	(294,200)	\$ 3.42		
Canceled	(80,560)	\$ 15.35		
Outstanding at November 25, 2006	3,111,460	\$ 12.02	6.7	\$ 10,745,577
Exercisable at November 25, 2006	1,362,930	\$ 9.04	5.6	\$ 7,594,743

As of November 25, 2006, there was \$6.5 million of total unrecognized compensation cost, net of estimated forfeitures, related to nonvested options. That cost is expected to be recognized over a weighted average period of 2.1 years.

The Company's restricted stock activity for the thirty-nine weeks ended November 25, 2006 was as follows:

	Number of Shares	Weighted Average Grant Date Fair Value
Unvested at February 25, 2006	101,300	\$ 14.35
Granted	153,450	\$ 16.07
Vested		\$
Canceled	(12,500)	\$ 15.07

Unvested at November 25, 2006

242,250 \$ 15.40

As of November 25, 2006, there was \$2.3 million of total unrecognized compensation cost, net of estimated forfeitures, related to nonvested restricted stock. That cost is expected to be recognized over a weighted average period of 2.2 years.

### **3. Common Stock**

On July 22, 2004, the Company's Board of Directors approved a new stock repurchase program which authorizes the Company to purchase, on the open market or in privately negotiated transactions through December 2007, up to 5 million shares of the Company's outstanding Class A Common Stock. During the thirty-nine weeks ended November 25, 2006, the Company purchased 1,260,017 shares of its Class A Common Stock at an average price of \$12.40 per share for an aggregate purchase price of \$15,619,000. There were no shares repurchased during the thirteen weeks ended November 25, 2006. As of November 25, 2006, the Company has 2,415,383 shares still available for repurchase under the program.

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

*This quarterly report on Form 10-Q may contain certain statements that we believe are, or may be considered to be, forward-looking statements, within the meaning of Section 27A of the Securities Act of 1933 and Section 21E of the Securities Exchange Act of 1934. These forward-looking statements generally can be identified by use of statements that include phrases such as believe, expect, anticipate, intend, plan, foresee, may, will, estimates, potential, continue or other similar words or phrases. Similarly, statements that describe our objectives, plans or goals also are forward-looking statements. All of these forward-looking statements are subject to risks and uncertainties that could cause our actual results to differ materially from those contemplated by the relevant forward-looking statement. The principal risk factors that could cause actual performance and future actions to differ materially from the forward-looking statements include, but are not limited to, product demand and market acceptance risks, the effect of economic conditions, the effect of competitive products and pricing, the availability of products, management of growth, and the other risks detailed in the Company's Securities and Exchange Commission filings. Readers are urged to consider these factors carefully in evaluating the forward-looking statements. The forward-looking statements included in this Form 10-Q are made only as of the date of this report and we undertake no obligation to publicly update these forward-looking statements to reflect subsequent events or circumstances.*

### **General**

The following discussion and analysis should be read in conjunction with Management's Discussion and Analysis of Financial Condition, including Critical Accounting Policies, included in the Company's Annual Report on Form 10-K for the year ended February 25, 2006 (fiscal 2006).

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The following table sets forth store and square feet information of the Company by brand for each of the following periods:

	Thirteen weeks ended		Thirty-nine weeks ended	
	November 25, 2006	November 26, 2005	November 25, 2006	November 26, 2005
<b>Number of Stores:</b>				
<b>Finish Line</b>				
Beginning of period	672	639	657	598
Opened	21	20	40	64
Closed	(1)	(1)	(5)	(4)
End of period	692	658	692	658
<b>Man Alive</b>				
Beginning of period	76	38	51	37
Opened	12	11	37	12
Closed				
End of period	88	49	88	49
<b>Paiva</b>				
Beginning of period	6			
Opened	6		12	
Closed				
End of period	12		12	
<b>Total</b>				
Beginning of period	754	677	708	635
Opened	39	31	89	76
Closed	(1)	(1)	(5)	(4)
End of period	792	707	792	707

	November 25,	November 26,
	2006	2005
<b>Square feet information as of:</b>		
<b>Finish Line</b>		
Square feet	3,854,382	3,706,986
Average store size	5,570	5,634
<b>Man Alive</b>		
Square feet	287,987	149,946
Average store size	3,273	3,060
<b>Paiva</b>		
Square feet	47,087	
Average store size	3,924	
<b>Total</b>		
Square feet	4,189,456	3,856,932
<b>Results of Operations</b>		

The following table sets forth net sales of the Company by major category for each of the following periods (In thousands):

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<b>Category</b>	<b>Thirteen Weeks Ended</b>			
	<b>November 25, 2006 (unaudited)</b>		<b>November 26, 2005 (unaudited)</b>	
Footwear	\$ 212,047	75%	\$ 209,804	77%
Softgoods	69,460	25%	64,176	23%
Total	\$ 281,507	100%	\$ 273,980	100%

<b>Category</b>	<b>Thirty-Nine Weeks Ended</b>			
	<b>November 25, 2006 (unaudited)</b>		<b>November 26, 2005 (unaudited)</b>	
Footwear	\$ 717,184	79%	\$ 724,020	80%
Softgoods	192,004	21%	182,800	20%
Total	\$ 909,188	100%	\$ 906,820	100%

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The following table and subsequent discussion sets forth operating data of the Company as a percentage of net sales for the periods indicated below.

	Thirteen Weeks Ended		Thirty-Nine Weeks Ended	
	November 25,	November 26,	November 25,	November 26,
	2006	2005	2006	2005
	(unaudited)		(unaudited)	
Net sales	100.0%	100.0%	100.0%	100.0%
Cost of sales (including occupancy costs)	72.3	71.7	70.8	69.2
Gross profit	27.7	28.3	29.2	30.8
Selling, general and administrative expenses	29.4	27.9	27.3	25.2
Operating income (loss)	(1.7)	.4	1.9	5.6
Interest income net		.1	.1	.2
Income (loss) before income taxes	(1.7)	.5	2.0	5.8
Provision (benefit) for income taxes	(.6)	.2	.8	2.2
Net income (loss)	(1.1)%	.3%	1.2%	3.6%

**Thirteen Weeks Ended November 25, 2006 Compared to Thirteen Weeks Ended November 26, 2005**

Net sales increased 2.7% to \$281.5 million for the thirteen weeks ended November 25, 2006 from \$274.0 million for the thirteen weeks ended November 26, 2005. This increase in net sales was primarily attributable to an increase in net sales from new stores, partially offset by a 3.3% decrease in comparable store sales for the thirteen weeks ended November 25, 2006. As of November 25, 2006, the number of stores in operation increased by 85 stores (12.0%) to 792 from 707 at November 26, 2005. The 85 additional stores were made up of 42 new Finish Line stores less 8 Finish Line stores closed plus 39 new Man Alive stores and 12 new Paiva stores. Comparable footwear net sales for the thirteen weeks ended November 25, 2006, decreased approximately 2.1% versus the thirteen weeks ended November 26, 2005. Comparable softgoods net sales decreased approximately 7.2% for the comparable period. The 2.1% decline in footwear net sales is primarily related to poor performance in women's running and men's basketball during the thirteen weeks ended November 25, 2006. The 7.2% decline in softgoods net sales is primarily due to poor performance in private label apparel as well as a slow down in accessories. Net sales per square foot for comparable stores decreased to \$68 from \$71 for the same thirteen-week period of the prior year.

Gross profit for the thirteen weeks ended November 25, 2006 was \$77.9 million, an increase of \$0.3 million (0.4%) over the thirteen weeks ended November 26, 2005. During this same period, gross profit decreased to 27.7% of net sales versus 28.3% for the prior year. This 0.6% decrease as a percentage of net sales was due to a 0.6% increase in occupancy costs as a percentage of net sales. The 0.6% increase in occupancy costs as a percentage of net sales was primarily a result of deleveraging due to the negative 3.3% comparable store sales for the thirteen weeks ended November 25, 2006.

Selling, general and administrative expenses increased \$6.1 million (8.0%) to \$82.7 million (29.4% of net sales) for the thirteen weeks ended November 25, 2006 from \$76.5 million (27.9% of net sales) for the thirteen weeks ended November 26, 2005. This increase was primarily attributable to the operating costs related to operating 85 additional stores (34 net Finish Line stores, 39 Man Alive stores and 12 Paiva stores) at November 25, 2006 versus November 26, 2005. The 1.5% increase of selling, general and administrative expenses as a percentage of net sales was primarily related to the following factors: a) an increase of 0.9% in payroll related expenses primarily due to deleveraging from negative comparable store sales; b) an increase of 0.4% in share-based compensation primarily due to the adoption of FAS 123R; and c) an increase of 0.9% as a result of incremental Man Alive and Paiva costs. These were offset partially by a decrease of 0.8% in advertising. The 0.8% decrease in advertising as a percentage of net sales was primarily due to a planned reduction of marketing expenses by reducing the catalog circulation during the thirteen weeks ended November 25, 2006.



Net interest expense was \$21,000 for the thirteen weeks ended November 25, 2006 compared to net interest income of \$0.3 million for the thirteen weeks ended November 26, 2005. The decrease of \$0.3 million was primarily due to lower cash and marketable securities balances during the thirteen weeks ended November 25, 2006 as compared to the thirteen weeks ended November 26, 2005 as well as short-term borrowings during the thirteen weeks ended November 25, 2006 compared to no short-term borrowings during the thirteen weeks ended November 26, 2005.

Income taxes were a benefit of \$1.8 million for the thirteen weeks ended November 25, 2006, compared to expense of \$0.5 million for the thirteen weeks ended November 26, 2005. This \$2.3 million decrease in income tax expense was due to a loss before income taxes of \$4.8 million for the thirteen weeks ended November 25, 2006 compared to income before taxes of \$1.4 million for the thirteen weeks ended November 26, 2005, along with an increase in the effective tax rate from 37.5% for the thirteen weeks ended November 26, 2005 to 38.0% for the thirteen weeks ended November 25, 2006.

Net loss was \$3.0 million for the thirteen weeks ended November 25, 2006 compared to net income of \$0.8 million for the thirteen weeks ended November 26, 2005. Net loss per diluted share was \$.06 for the thirteen weeks ended November 25, 2006 compared to net income per diluted share of \$.02 for the thirteen weeks ended November 26, 2005. Diluted weighted average shares outstanding were 46,909,000 and 49,058,000 for the thirteen weeks ended November 25, 2006 and November 26, 2005, respectively. The decrease in weighted average shares outstanding is primarily related to the 2.5 million shares repurchased by the Company since August 27, 2005, partially offset by the exercise of Company stock options.

#### **Thirty-Nine Weeks Ended November 25, 2006 Compared to Thirty-Nine Weeks Ended November 26, 2005**

Net sales increased 0.3%, or \$2.4 million, to \$909.2 million for the thirty-nine weeks ended November 25, 2006 from \$906.8 million for the thirty-nine weeks ended November 26, 2005. Of this increase, \$27.0 million was attributable to a 12.0% increase in the number of stores open (42 Finish Line stores opened less 8 stores closed plus 39 Man Alive stores and 12 Paiva stores opened) during the period from 707 at November 26, 2005 to 792 at November 25, 2006. The balance of the increase was attributable to a \$29.2 million increase in net sales from the existing stores open only part of the first thirty-nine weeks of last year offset by a comparable store net sales decrease of 5.8% for the thirty-nine weeks ended November 25, 2006. Comparable footwear net sales for the thirty-nine weeks ended November 25, 2006, decreased approximately 5.1%. The 5.1% decline is primarily related to the poor performance of women's and kids' footwear during the thirty-nine weeks ended November 25, 2006. Comparable softgoods net sales decreased approximately 8.3% for the comparable period. The 8.3% decrease in comparable net softgoods net sales was primarily due to a decline in the average retail selling price of softgoods. This is primarily related to the shift in fashion from licensed jerseys to more branded and private label sold during the thirty-nine weeks ended November 25, 2006. Net sales per square foot for comparable stores decreased to \$224 from \$244 for the same period of the prior year.

Gross profit for the thirty-nine weeks ended November 25, 2006 was \$265.6 million, a decrease of \$13.7 million (4.9%) over the \$279.3 million for the thirty-nine weeks ended November 26, 2005. Gross profit was 29.2% of net sales for the thirty-nine weeks ended November 25, 2006 compared to 30.8% for the thirty-nine weeks ended November 26, 2005. This 1.6% decrease as a percentage of net sales was due to a 1.1% increase in occupancy costs as a percentage of net sales, a 0.4% decrease in margin for product sold as a percentage of net sales, and a 0.1% increase in shrink expense as a percentage of net sales. The 1.1% increase in occupancy costs as a percentage of net sales was primarily a result of deleveraging due to the 5.8% decrease in comparable store sales for the thirty-nine weeks ended November 25, 2006. The 0.4% decrease in margin for product sold was primarily related to a more promotional environment during the thirty-nine weeks ended November 25, 2006 compared to the thirty-nine weeks ended November 26, 2005.

Selling, general and administrative expenses increased \$19.5 million (8.5%) to \$248.3 million (27.3% of net sales) for the thirty-nine weeks ended November 25, 2006 from \$228.8 million (25.2% of net sales) for the thirty-nine weeks ended November 26, 2005. This dollar increase was primarily attributable to the operating costs related to operating 85 additional stores at November 25, 2006 versus November 26, 2005. The 2.1% increase in selling, general and administrative expenses as a percentage of net sales was primarily related to the following: a) an increase of 0.7% in payroll related expenses primarily due to deleveraging from negative comparable store sales; b) an increase of 0.4% in share-based compensation primarily due to the adoption of FAS 123R; c) an increase in freight of 0.3% due to shipping to 85 additional stores opened this year and deleveraged due to negative comparable store sales as well as higher fuel surcharges; d) an increase in depreciation of 0.3% due to 85 additional stores opened this year but deleveraged from negative comparable store sales; and e) an increase of 0.6% as a result of incremental Man Alive and Paiva costs. These changes were partially offset by a decrease in advertising expense of 0.2% of net sales as well as the thirty-nine weeks ended November 26, 2005 including a \$1.5 million (0.2% of net sales) reserve related to a class action lawsuit.

Net interest income was \$0.9 million (0.1% of net sales) for the thirty-nine weeks ended November 25, 2006, compared to net interest income of \$1.4 million (0.2% of net sales) for the thirty-nine weeks ended November 26, 2005, a decrease of \$0.5 million (38.5%). This decrease was due primarily to lower cash and marketable securities balances for the thirty-nine weeks ended November 25, 2006 compared to the thirty-nine weeks ended November 26, 2005 as well as short-term borrowings during the thirty-nine weeks ended November 25, 2006 compared to no short-term borrowings during the thirty-nine weeks ended November 26, 2005.

The Company's provision for federal and state income taxes was \$6.9 million (0.8% of net sales) for the thirty-nine weeks ended November 25, 2006 compared to \$19.5 million (2.2% of net sales) for the thirty-nine weeks ended November 26, 2005. The \$12.6 million decrease in income tax expense is due to the decreased level in income before income taxes for the thirty-nine weeks ended November 25, 2006 partially offset by an increase in effective tax rate to 38.0% for the thirty-nine weeks ended November 25, 2006 from 37.5% for the thirty-nine weeks ended November 26, 2005.

Net income decreased 65.2% to \$11.3 million for the thirty-nine weeks ended November 25, 2006 compared to \$32.5 million for the thirty-nine weeks ended November 26, 2005. Net income per diluted share decreased 63.1% to \$.24 for the thirty-nine weeks ended November 25, 2006 compared to net income per diluted share of \$.65 for the thirty-nine weeks ended November 26, 2005. Diluted weighted average shares outstanding were 47,882,000 and 49,605,000 for the periods ended November 25, 2006 and November 26, 2005, respectively. The decrease in weighted average shares outstanding is primarily related to the 2.5 million shares repurchased by the Company since August 27, 2005, partially offset by the exercise of Company stock options.

#### **Liquidity and Capital Resources**

The Company used net cash of \$22.9 million in its operating activities during the thirty-nine weeks ended November 25, 2006 as compared to net cash used in its operating activities of \$1.2 million during the thirty-nine weeks ended November 26, 2005. The increase of \$21.7 million used in operations was due primarily to the \$21.2 million decrease in net income for the thirty-nine weeks ended November 25, 2006 compared to the thirty-nine weeks ended November 26, 2005.

Consolidated merchandise inventories were \$356.9 million at November 25, 2006 compared to \$268.6 million at February 25, 2006 and \$311.5 million at November 26, 2005. On a per square foot basis, Finish Line merchandise inventories (excluding Man Alive and Paiva) at November 25, 2006 increased 4.9% compared to November 26, 2005, and were 21.4% higher than at February 25, 2006. The 21.4% increase from February 25, 2006 is due to the seasonality of the business and building inventory in November for the holiday season in December, which is consistent with prior years.

The Company had working capital of \$208.5 million at November 25, 2006, a decrease of \$30.6 million from the working capital of \$239.1 million at February 25, 2006.

The Company used net cash of \$15.5 million for its investing activities and generated cash of \$5.8 million for the thirty-nine week periods ended November 25, 2006 and November 26, 2005, respectively. In the thirty-nine weeks ended November 25, 2006, \$63.3 million was used primarily for constructing new stores, remodeling existing stores and expanding the corporate offices. Proceeds from the sale of available-for-sale marketable securities were \$155.5 million for the thirty-nine weeks ended November 25, 2006 offset by purchases of \$106.4 million of available-for-sale marketable securities. A portion of the proceeds were used to purchase \$15.6 million of treasury shares and pay \$3.6 million in dividends during the thirty-nine week period ended November 25, 2006.

At November 25, 2006 the Company had cash and cash equivalents of \$12.9 million and interest bearing debt of \$20.4 million. Cash equivalents are primarily invested in tax-exempt instruments with daily liquidity. The Company anticipates repaying any outstanding short-term borrowings during the fourth quarter.

The Company currently plans to open 40 Finish Line stores (all were opened by November 25, 2006), 37 Man Alive stores (all were opened by November 25, 2006), 14-15 Paiva stores (12 were opened by November 25, 2006), remodel 17 existing Finish Line stores (16 have been completed through November 25, 2006) and close 5-8 Finish Line stores during this fiscal year. In addition, the Company completed the expansion of the existing corporate office in Indianapolis and has begun renovation on the previous corporate office space along with various other projects. The Company expects capital expenditures for the current fiscal year to approximate \$65.0-70.0 million. In fiscal 2008, the Company currently plans to open 20-25 Finish Line stores, 15-20 Man Alive stores and no Paiva stores. The Company also plans to remodel 10-12 Finish Line stores and 2-4 Man Alive stores. Management believes that cash on hand, operating cash flow and the Company's existing \$75.0 million bank facility, which expires on February 25, 2010, will provide sufficient capital to complete the Company's current store expansion program and to satisfy the Company's other capital requirements in the foreseeable future.

On July 22, 2004, the Company's Board of Directors approved a new stock repurchase program which authorizes the Company to purchase, on the open market or in privately negotiated transactions through December 2007, up to 5.0 million shares of the Company's Class A Common Stock outstanding. During the thirty-nine weeks ended November 25, 2006, the Company purchased 1.3 million shares of its Class A Common Stock at an average price of \$12.40 per share for an aggregate purchase price of \$15.6 million. The Company has 2.4 million shares still available to repurchase under the program.

The Company's contractual obligations primarily consist of long-term debt, operating leases, and purchase orders for merchandise inventory. Other than short-term borrowings of \$20.4 million outstanding as of November 25, 2006, there have been no significant changes in the Company's contractual obligations since February 25, 2006, other than those which occur in the normal course of business (primarily changes in the Company's merchandise inventory related to purchase obligations, which fluctuate throughout the year as a result of the seasonal nature of the Company's operations, and additional operating leases entered into due to store openings).

### Recently Issued Accounting Pronouncements

In June 2006, the Financial Accounting Standards Board ( FASB ) issued Interpretation No. 48, *Accounting for Uncertainty in Income Taxes an interpretation of FASB Statement No. 109* ( FIN 48 ). FIN 48 clarifies the recognition threshold and measurement principles for the financial statement recognition and measurement of a tax position taken or expected to be taken in a tax return. FIN 48 also provides guidance on derecognition, classification, interest and penalties, accounting in interim periods, disclosure and transition. FIN 48 is effective for fiscal years beginning after December 15, 2006 (fiscal year 2008). The Company is currently evaluating the provisions of FIN 48.

In June 2006, the FASB ratified the Emerging Issues Task Force ( EITF ) consensus on EITF Issue No. 06-3, *How Taxes Collected from Customers and Remitted to Governmental Authorities Should Be Presented in the Income Statement (That Is, Gross versus Net Presentation)*. EITF Issue No. 06-3 states that the classification of taxes as gross or net is an accounting policy decision that is dependent on type of tax and that similar taxes are to be presented in a similar manner. EITF Issue No. 06-3 is effective for reporting periods beginning after December 15, 2006. EITF Issue No. 06-3 will not impact the method for recording sales taxes in the Company's consolidated financial statements as the Company has historically presented sales excluding all taxes.

In September 2006, the FASB issued Statement of Financial Accounting Standards ( SFAS ) No. 157, *Fair Value Measurements*. SFAS No. 157 provides guidance for using fair value to measure assets and liabilities and only applies when other standards require or permit the fair value measurement of assets and liabilities. It does not expand the use of fair value measurement. SFAS No. 157 is effective for fiscal years beginning after November 15, 2007. Adoption of SFAS No. 157 is not expected to have a material impact on the Company's results of operations, financial condition or liquidity.

### Critical Accounting Policies and Estimates

The preparation of financial statements in conformity with generally accepted accounting principles requires management to adopt accounting policies related to estimates and assumptions that affect the reported amounts of assets and liabilities at the date of the financial statements and the reported amounts of revenues and expenses during the reporting period, as well as the related disclosure of contingent assets and liabilities at the date of the financial statements. On an ongoing basis, management evaluates its accounting policies, estimates and judgments, including those related to inventories, long lived assets and contingencies. Management bases its estimates and judgments on historical experience and various other factors that are believed to be reasonable under the circumstances. Actual results may differ from these estimates. There have been no significant changes to the critical accounting policies and estimates disclosed in the Company's Annual Report on Form 10-K for the fiscal year ended February 25, 2006.

### ITEM 3. QUANTITATIVE AND QUALITATIVE DISCLOSURES ABOUT MARKET RISK

For a discussion of the Company's market risk associated with interest rates as of February 25, 2006 see *Quantitative and Qualitative Disclosures about Market Risk* in Item 7A of Part II of the Company's Annual Report on Form 10-K for the fiscal year ended February 25, 2006. There have been no significant change in related market risk factors since February 25, 2006.

**ITEM 4. CONTROLS AND PROCEDURES**

**Disclosure Controls and Procedures.** With the participation of our Chief Executive Officer and Chief Financial Officer, we have evaluated the effectiveness of our disclosure controls and procedures (as such term is defined in Rules 13a-15(e) and 15d-15(e) under the Securities Exchange Act of 1934, as amended (the Exchange Act)), as of the end of the period covered by this report. Based upon such evaluation, our Chief Executive Officer and Chief Financial Officer have concluded that, as of the end of such period, our disclosure controls and procedures were effective in ensuring that (i) information required to be disclosed by the Company in the reports that it files or submits under the Exchange Act is recorded, processed, summarized and reported, within the time periods specified in the Securities Exchange Commission's rules and forms and (ii) information required to be disclosed by the Company in the reports that it files or submits under the Exchange Act is accumulated and communicated to the Company's management, including its principal executive and principal financial officers, or persons performing similar functions, as appropriate to allow timely decisions regarding required disclosure.

**Internal Control Over Financial Reporting.** There have not been any changes in our internal control over financial reporting (as such term is defined in Rules 13a-15(f) and 15d-15(f) under the Exchange Act) during the fiscal quarter to which this report relates that have materially affected, or are reasonably likely to materially affect, our internal control over financial reporting.

PART II OTHER INFORMATION

**ITEM 1: LEGAL PROCEEDINGS**

The Company is subject from time to time, to certain legal proceedings and claims in the ordinary course of conducting its business. Although it is not possible to predict with certainty the eventual outcome of any litigation, in the opinion of management, the Company's legal proceedings are not expected to have a material adverse effect on the Company's financial position or results of operations.

**ITEM 1A: RISK FACTORS**

The risk factors that affect the Company's business and financial results are discussed in Item 1A: Risk Factors in the Company's Annual Report on Form 10-K for the fiscal year ended February 25, 2006. For the thirteen weeks ended November 25, 2006, there has been no significant change to identified risk factors.

**ITEM 2: CHANGES IN SECURITIES, USE OF PROCEEDS AND ISSUER PURCHASES OF EQUITY SECURITIES**

None.

**ITEM 3: DEFAULTS UPON SENIOR SECURITIES**

None.

**ITEM 4: SUBMISSION OF MATTERS TO A VOTE OF SECURITY HOLDERS**

None.

**ITEM 5: OTHER INFORMATION**

None.

**ITEM 6: EXHIBITS**

(a) Exhibits

- 10.1 Form of Employment Agreement, dated as of October 30, 2006 (incorporated by reference to Exhibit 10.1 to the Company's Form 8-K filed with the Securities and Exchange Commission on October 30, 2006)
- 10.2 Form of Founders Letter, dated as of October 30, 2006 (incorporated by reference to Exhibit 10.2 to the Company's Form 8-K filed with the Securities and Exchange Commission on October 30, 2006)
- 31.1 Certification of Chief Executive Officer Pursuant to Exchange Act Rule 13a-14(a) and 15d-14(a), as amended
- 31.2 Certification of Chief Financial Officer Pursuant to Exchange Act Rule 13a-14(a) and 15d-14(a), as amended
- 32 Certification Pursuant to 18 U.S.C. Section 1350, As Adopted Pursuant to Section 906 of the Sarbanes-Oxley Act of 2002



**SIGNATURES**

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

THE FINISH LINE, INC.

Date: December 20, 2006

By: /s/ Kevin S. Wampler  
Kevin S. Wampler

Executive Vice President-Chief Financial Officer and Assistant  
Secretary



Exhibit Index

**Exhibit**

<b>Number</b>	<b>Description</b>
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