

**UNITED STATES  
SECURITIES AND EXCHANGE COMMISSION**  
Washington, D.C. 20549

**FORM 10-K**

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

For the fiscal year ended **December 26, 2006**.

**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 **000-29643**

**GRANITE CITY FOOD & BREWERY LTD.**

(Exact name of registrant as specified in its charter)

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

**41-1883639**  
(I.R.S. Employer Identification No.)

**5402 Parkdale Drive, Suite 101**  
**Minneapolis, Minnesota**  
(Address of principal executive offices)

**55416**  
(Zip Code)

**(952) 215-0660**  
(Registrant's telephone number, including area code)

Securities registered pursuant to Section 12(b) of the Act:

Title of each class	Name of each exchange on which registered
Common Stock, \$0.01 par value	NASDAQ Capital Market

Indicate by check mark if the registrant is a well-known seasoned issuer, as defined in Rule 405 of the Securities Act.  
Yes  No

Indicate by check mark if the registrant is not required to file reports pursuant to Section 13 or Section 15(d) of the Act.  
Yes  No

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, and (2) has been subject to such filing requirements for the past 90 days. Yes  No

Indicate by check mark if disclosure of delinquent filers pursuant to Item 405 of Regulation S-K is not contained herein, and will not be contained, to the best of registrant's knowledge, in definitive proxy or information statements incorporated by reference in Part III of this Form 10-K or any amendment to this Form 10-K.

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

As of June 27, 2006, the aggregate market value of the registrant's common stock held by non-affiliates (assuming for the sole purpose of this calculation, that all directors and officers of the registrant are "affiliates") was \$38,409,560 (based on the closing sale price of the registrant's common stock as reported on the NASDAQ Capital Market). The number of shares of common stock outstanding at that date was 13,226,526 shares.

The number of shares of common stock outstanding as of February 14, 2007 was 13,370,331.

#### DOCUMENTS INCORPORATED BY REFERENCE

Certain information required by Part III of this document is incorporated by reference to specified portions of the registrant's definitive proxy statement for the annual meeting of shareholders to be held in June 2007.

---

---

---

**GRANITE CITY FOOD & BREWERY LTD.**  
**FORM 10-K ANNUAL REPORT**  
**FOR THE FISCAL YEAR ENDED DECEMBER 26, 2006**

**TABLE OF CONTENTS**

PART I

- Item 1. Business
- Item 1A. Risk Factors
- Item 1B. Unresolved Staff Comments
- Item 2. Properties
- Item 3. Legal Proceedings
- Item 4. Submission of Matters to a Vote of Security Matters

PART II

- Item 5. Market for Registrant's Common Equity, Related Stockholder Matters and Issuer Purchases of Equity Securities
- Item 6. Selected Financial Data
- Item 7. Management's Discussion and Analysis of Financial Condition and Results of Operations
- Item 7A. Quantitative and Qualitative Disclosures About Market Risk
- Item 8. Financial Statements and Supplementary Data
- Item 9. Changes in and Disagreements With Accountants on Accounting and Financial Disclosure
- Item 9A. Controls and Procedures
- Item 9B. Other Information

PART III

- Item 10. Directors, Executive Officers and Corporate Governance
- Item 11. Executive Compensation
- Item 12. Security Ownership of Certain Beneficial Owners and Management and Related Stockholder Matters
- Item 13. Certain Relationships and Related Transactions, and Director Independence
- Item 14. Principal Accountant Fees and Services

PART IV

- Item 15. Exhibits and Financial Statement Schedules

SIGNATURES.

INDEX TO FINANCIAL STATEMENTS

INDEX TO EXHIBITS

*This Annual Report contains forward-looking statements that involve risks and uncertainties. The statements contained in this Annual Report that are not purely historical are forward-looking statements within the meaning of Section 27A of the Securities Act of 1933, as amended, and Section 21E of the Securities Exchange Act of 1934, as amended. These forward-looking statements include, without limitation, statements relating to future economic conditions in general and statements about the future:*

- *Strategy and business;*
- *Development plans and growth;*
- *Sales, earnings, income, expenses, operating results, profit margins, capital resource needs and competition;*
- *Ability to obtain and protect intellectual property and proprietary rights.*

*All of these forward-looking statements are based on information available to us on the date of filing this Annual Report. Our actual results could differ materially. The forward-looking statements contained in this Annual Report, and other written and oral forward-looking statements made by us from time to time, are subject to certain risks and uncertainties that could cause actual results to differ materially from those anticipated in the forward-looking statements. Factors that might cause such a difference include, but are not limited to, those discussed in Item 1A of this report entitled "Risk Factors."*

## PART I

### Item 1. Business.

#### Overview

We are a Modern American upscale casual restaurant chain. As of February 1, 2007, we operated 18 restaurants in eight Midwestern states featuring on-premises breweries under the name of Granite City Food & Brewery. We believe our menu features affordable yet high quality family favorite menu items prepared from made-from-scratch recipes and served in generous portions. We believe that the sophisticated yet unpretentious restaurants, proprietary food and beverage products, attractive price points and high service standards combine for a great dining experience. The location of each restaurant and the month and year of its opening appear in the following chart:

Unit	Location	Opened
1	St. Cloud, Minnesota	June 1999
2	Sioux Falls, South Dakota	December 2000
3	Fargo, North Dakota	November 2001
4	Des Moines, Iowa	September 2003
5	Cedar Rapids, Iowa	November 2003
6	Davenport, Iowa	January 2004
7	Lincoln, Nebraska	May 2004
8	Maple Grove, Minnesota	June 2004
9	Wichita, Kansas	July 2005
10	Eagan, Minnesota	September 2005
11	Kansas City, Missouri	November 2005
12	Kansas City, Kansas	January 2006
13	Olathe, Kansas	March 2006
14	West Wichita, Kansas	July 2006
15	St. Louis Park, Minnesota	September 2006
16	Omaha, Nebraska	October 2006
17	Roseville, Minnesota	November 2006
18	Madison, Wisconsin	December 2006

We developed the foregoing restaurants using proceeds from the sale of our securities, building and equipment financing and cash flow from operations. We built units 4-9, 11-14 and 16-18 based upon the prototype we developed in early 2003. In 2004 and 2005, we retrofitted units 1-3 to conform to this prototype model. In 2005 and 2006, we developed units 10 and 15, respectively, which were conversions of existing restaurants. With the exception of units 1-3 and 15, we developed all of our units under our multi-site development agreement with a commercial developer that provides us with assistance in site selection, construction management and financing for new restaurants. Under this agreement, we lease the land and building of each new restaurant from our developer.

We operate a beer production facility which facilitates the initial stage of our brewing process—the production of non-alcoholic wort —using our patented brewing process called Fermentus Interruptus™. We believe that Fermentus Interruptus and the use of a centrally located beer production facility improves the economics of microbrewing as it eliminates the initial stages of brewing and storage at multiple locations, thereby reducing equipment and development costs at new restaurant locations. Additionally, having a common starting point for the production of wort creates consistency of taste for our product from unit to unit. The wort produced at our beer production facility is transported by truck to the fermentation vessels at each of our restaurants where the brewing process is completed. We believe that our current beer production facility, which was opened in June 2005, has the capacity to service 30 to 35 restaurant locations.

We operate Granite City University where the training of each of our managers takes place under the instruction of full-time, dedicated trainers. Our eight-week training program consists of both “hands on” as well as classroom training for all aspects of management. All salaries of our managers in training and our trainers as well as all related costs incurred at Granite City University are recorded as a component of corporate general and administrative costs. In January 2006, we relocated Granite City University from our Des Moines restaurant to our Maple Grove restaurant.

We utilize a new store opening team which consists of experienced restaurant managers who are dedicated to the opening of our new restaurants. Generally, this team arrives at a new restaurant site two to three months in advance of the restaurant opening date and coordinates all staffing and training matters for that new restaurant. We believe that a dedicated team delivers a more disciplined opening process and ensures adherence to our company’s exacting standards and culture. We formed our new store opening team in July 2005.

We maintain a website at [www.gcfb.net](http://www.gcfb.net), which is also accessible through [www.gcfb.com](http://www.gcfb.com). We make available on our website, free of charge, our annual, quarterly and current reports, and all amendments to those reports, as soon as reasonably practicable after that material is electronically filed with, or furnished to, the Securities and Exchange Commission. Our Code of Business Conduct and Ethics and key committee charters are also available on our websites and in print upon written request to Granite City Food & Brewery Ltd., 5402 Parkdale Drive, Suite 101, Minneapolis, Minnesota 55402, Attention: Investor Relations. Unless otherwise indicated, we do not intend to incorporate the contents of our websites into this Annual Report or any other document filed with the Security and Exchange Commission.

We were incorporated on June 26, 1997, as a Minnesota corporation and became a publicly traded company in June 2000. Our corporate offices are located at 5402 Parkdale Drive, Suite 101, Minneapolis, Minnesota 55416, and our telephone number is (952) 215-0660.

### **Our Granite City Food & Brewery Concept and Business Strategy**

Our objective is to develop and operate successful restaurants by consistently exceeding our guests' expectations in product, service and overall dining experience, thereby becoming a leader in the casual dining industry. We continue to pursue consistent, long-term growth in unit and overall company earnings in an effort to provide returns for our shareholders. Our Granite City Food & Brewery concept targets a broad guest base by incorporating two popular national dining preferences: high quality, casual, value-priced food, and fresh, handcrafted, quality beers. We believe this concept differentiates us from many of our competitors, who feature pre-prepared, smaller portioned food items and mass-produced, pre-packaged beers. The principal elements of our concept and business strategy are as follows:

- *Offer a Broad Selection of Quality Foods at Reasonable Prices.* Granite City Food & Brewery restaurants feature quality food items prepared from scratch daily, based upon hearty Midwestern fare infused with Southwestern, Cajun and California influences. We place a heavy emphasis on freshness, variety, generous portions and attractive presentation. We feature many items designed with our handcrafted beers in mind, both as ingredients and to accompany meals. Our menu is strategically tailored for patrons who tend to have greater price sensitivity toward lunch items than dinner items. When a guest opens the menu, he or she finds a special section of lunch selections featured at prices that provide a premium meal at a special value for midday diners.
- *Offer Old World, Classic Beers Made with an Efficient Brewing Process.* We brew ales and lagers in the Old World tradition. Our array of craftbrewed beers is distinguishable from other domestically produced beers by its freshness, flavor and brewing styles. We permanently offer on tap four unique handcrafted beers which are produced from the highest quality ingredients. Additionally, we produce seasonal and special ales and lagers handcrafted to promote special events.
- *Create a Fun, Energetic Atmosphere and Destination Dining Experience.* We focus on providing the Granite City guest with a fun, warm and energetic atmosphere. Our restaurant interiors are spacious, open settings designed to create an environment that is upscale, casual and unpretentious. Guests may watch the brewing process and see food preparation in our open display kitchens, or watch sporting events or other entertainment on the many televisions throughout our dining and bar areas. We celebrate the art of brewing and cooking by showcasing our breweries and kitchens.
- *Create a Passionate Culture of Service.* We foster a passionate culture of guest service among employees, by emphasizing guest service and a comfortable dining experience provided by a knowledgeable, energetic staff. Our intense employee training and supervision is designed to develop motivated, service-oriented employees who strive to deliver strong customer satisfaction. Our employees are trained to understand how our foods are flavored and prepared, and to describe our handcrafted beers in order to introduce guests to the Granite City concept. We have a store-level management presence during all business hours to maintain a high level of service at all times and to support our employees in ensuring guest satisfaction.
- *Achieve Attractive Restaurant and Microbrewery Economics.* We believe that our restaurant-microbrewery concept and the pricing of our products fit well in our existing markets and the markets we have targeted for expansion. We also believe that we have the ability to achieve attractive economics through the sale of higher margin menu items such as our handcrafted beers.

- *Pursue Deliberate and Careful Expansion.* We continue to pursue a disciplined expansion strategy in markets where we believe our concept will have broad appeal and attractive restaurant-level economics. We believe that continued growth in the Midwest will allow us to achieve attractive economics by establishing name recognition and product branding throughout the region.

### **Existing and Proposed Locations**

As of February 1, 2007, we operated 18 Granite City Food & Brewery restaurants as set forth in “Description of Business—Overview.” Our prototypical restaurant consists of an approximately 9,450 square foot facility conveniently located just off one or more interstate highways and is centrally located within the respective area’s retail, lodging and transportation activity. Our restaurants have open atmospheres with exposed ceilings as well as floor-to-ceiling window systems creating expansive views of patio areas used for dining during warm weather months. This window treatment allows activity to be viewed both inside and outside the restaurant and creates a bright, open environment. We use granite and other rock materials along with natural woods and glass to create a balanced, clean, natural interior feel. The interiors are accented with vintage photographs of the local area brewing industry, as well as historical photos of the community landscape. We believe our design creates a fun and energetic atmosphere that promotes a destination dining experience.

We plan to continue using our prototypical model as we open future restaurants under our multi-site development agreement; however, where appropriate, we may convert existing restaurants to our Granite City concept. Additionally, we intend to explore alternative restaurant designs to reduce the cost of our initial capital investment and we may alter our model to meet various state and local regulatory requirements, including, but not limited to, pollution control requirements, liquor license ordinances and smoking regulations. Based upon our existing prototype, we anticipate that pre-opening costs and the initial purchase of furniture, fixtures and equipment will require an investment by us of approximately \$1.0 million to \$1.6 million for each new restaurant. We anticipate that our new restaurants will require an investment by our developer of approximately \$3.0 million to \$4.5 million each for land and building. We expect these costs will vary from one market to another based on real estate values, zoning regulations, labor markets and other variables.

We developed our existing restaurants using proceeds from the sale of our securities, building and equipment financing and cash flow from operations. We built units 4-9, 11-14 and 16-18 based upon the prototype we developed in early 2003. In 2004 and 2005, we retrofitted units 1-3 to conform to this prototype model. In 2005 and 2006, we developed units 10 and 15, respectively, which were conversions of existing restaurants. With the exception of units 1-3 and 15, we developed all of our units under our multi-site development agreement with a commercial developer that provides us with assistance in site selection, construction management and financing for new restaurants. Under this agreement, we lease the land and building of each new restaurant from our developer.

We intend to open eight new restaurants in 2007 and have entered into agreements or are in negotiations for locations in Illinois, Arkansas, Missouri and Minnesota.

### **Development Agreement**

In October 2002, we entered into the above-referenced development agreement with Dunham Capital Management L.L.C. (“Dunham”) for the development of restaurants. Dunham is controlled by Donald A. Dunham, Jr., who is a member of DHW Leasing, L.L.C. (“DHW”) and an affiliate of Granite Partners, L.L.C. (“Granite Partners”), a beneficial owner of less than 2% of our securities. The development agreement gives Dunham the right to develop, construct and lease up to 22 restaurants for us

prior to December 31, 2012. We are not bound to authorize the construction of restaurants during the term of the development agreement, but generally cannot use another developer to develop or own a restaurant as long as the development agreement is in effect. We can use another developer if Dunham declines to build a particular restaurant, if the agreement is terminated because of a default by Dunham, or if our company is sold or merged into another company. In the case of a merger or sale of our company, the development agreement may be terminated. As of February 1, 2007, 14 restaurants had been constructed for us under this development agreement.

The development agreement provides for a cooperative process between Dunham and our company for the selection of restaurant sites and the development of restaurants on those sites, scheduling for the development and construction of each restaurant once a location is approved, and controls on the costs of development and construction using bidding and guaranteed maximum cost concepts. The development agreement provides that restaurants are leased to us on the basis of a triple net lease. The rental rate of each lease is calculated using a variable formula which is based on approved and specified costs of development and construction and an indexed interest rate. The term of each lease is 20 years with five five-year options to renew. Instead of renewing, we may purchase the restaurant real estate for the fair market value during the last year of the original term.

Generally, the land portion of the leases we enter into with Dunham is classified as an operating lease because the fair value of the land is more than 25% of the leased property at the inception of the lease. The building portion of the leases is classified as a capital lease because its present value is greater than 90% of the estimated fair value at the beginning of the lease. As such, payments made to Dunham for the land portion of the leases are classified as rent expense while payments made for the building portion of the leases are classified as principal and interest on a capital lease.

The selection of our Granite City locations has been and will continue to be based upon criteria which we have determined are important for restaurant development. These criteria include minimum "trade area" populations, proximity to regional retail, entertainment, financial and educational hubs, as well as excellent accessibility and visibility.

In September 2006, we entered into an amendment of this development agreement that applies to our Omaha, Madison and Roseville restaurants as well as all future restaurants built under the development agreement. Under the terms of the amendment, in lieu of previously negotiated future adjustments to restaurant lease rates, lease rates would be increased by 10% commencing on the fifth anniversary of each lease and on each five-year anniversary thereafter.

Dunham also has the right to sell the underlying land and building to third parties or assign our leases. As of February 1, 2007, Dunham had sold three of our restaurant sites to third parties. The assignment or sale of a lease by Dunham has had no material impact on our operations.

## **Menu**

At the core of our concept is our 85-item menu complemented by fresh, handcrafted beers. Our menu is committed to full flavored ingredients and is based on the preparation of distinctive items not generally featured on restaurant chain menus. We create new menu items and weekly specials on a regular basis. All menu items are staff and guest-tested, then refined before menu implementation.

Our menu is strategically tailored for patrons who tend to have greater price sensitivity toward lunch items than dinner items. When our menu is opened, our guests find a special section of lunch selections featured at prices currently ranging from \$4.99 to \$7.49, providing a premium meal at a special value for midday diners. We also offer signature selections, meals which are marketed as our chefs' personal

