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**UNITED STATES  
SECURITIES AND EXCHANGE COMMISSION  
WASHINGTON, DC 20549**

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**FORM 10-Q**

- QUARTERLY REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934 FOR THE QUARTERLY PERIOD ENDED JUNE 26, 2007**
- TRANSITION REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934**

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 55416  
(952) 215-0660**

(Address of Principal Executive Offices and Issuer'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  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. (Check one):

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 August 1, 2007, the issuer had outstanding 16,014,320 shares of common stock.

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**PART I FINANCIAL INFORMATION****ITEM 1 Financial Statements**

**GRANITE CITY FOOD & BREWERY LTD.**  
**CONDENSED CONSOLIDATED BALANCE SHEETS**  
(Unaudited)

	<u>June 26, 2007</u>	<u>December 26, 2006</u>
<b>ASSETS:</b>		
Current assets:		
Cash and cash equivalents	\$11,247,205	\$ 7,671,750
Inventory	485,254	511,146
Prepays and other	431,009	393,803
Total current assets	<u>12,163,468</u>	<u>8,576,699</u>
Prepaid rent, net of current portion	474,337	503,267
Property and equipment, net	55,335,695	54,018,124
Intangible assets and other	718,218	760,420
Total assets	<u>\$68,691,718</u>	<u>\$63,858,510</u>
<b>LIABILITIES AND SHAREHOLDERS' EQUITY:</b>		
Current liabilities:		
Accounts payable	\$ 3,786,603	\$ 2,289,433
Accrued expenses	4,392,504	5,104,730
Deferred rent, current portion	164,699	143,928
Long-term debt, current portion	278,923	259,940
Capital lease obligations, current portion	983,930	1,885,388
Total current liabilities	<u>9,606,659</u>	<u>9,683,419</u>
Deferred rent, net of current portion	1,865,697	1,603,557
Long-term debt, net of current portion	1,865,474	2,004,986
Capital lease obligations, net of current portion	<u>31,880,585</u>	<u>37,501,605</u>
Total liabilities	<u>45,218,415</u>	<u>50,793,567</u>
Commitments and contingencies		
Shareholders' equity:		
Common stock, \$0.01 par value, 90,000,000 shares authorized; 16,014,320 and 13,370,331 shares issued and outstanding at June 26, 2007 and December 26, 2006, respectively	160,143	133,703
Additional paid-in capital	42,347,573	29,122,306
Accumulated deficit	<u>(19,034,413)</u>	<u>(16,191,066)</u>
Total shareholders' equity	<u>23,473,303</u>	<u>13,064,943</u>
Total liabilities and shareholders' equity	<u>\$68,691,718</u>	<u>\$63,858,510</u>

See notes to condensed consolidated financial statements.

**GRANITE CITY FOOD & BREWERY LTD.**  
**CONDENSED CONSOLIDATED STATEMENTS OF OPERATIONS**  
(Unaudited)

	<u>Thirteen Weeks Ended</u>		<u>Twenty-six Weeks Ended</u>	
	<u>June 26, 2007</u>	<u>June 27, 2006</u>	<u>June 26, 2007</u>	<u>June 27, 2006</u>
Restaurant revenues	\$18,453,954	\$14,417,118	\$36,636,146	\$26,309,437
Cost of sales:				
Food, beverage and retail	5,524,901	4,258,148	10,919,623	7,773,083
Labor	6,544,272	4,990,804	13,151,175	9,257,632
Direct restaurant operating	2,491,215	1,652,845	4,934,154	3,247,489
Occupancy	1,103,348	795,873	2,274,892	1,477,528
Total cost of sales	<u>15,663,736</u>	<u>11,697,670</u>	<u>31,279,844</u>	<u>21,755,732</u>
Pre-opening	416,341	262,572	512,182	1,074,374
General and administrative	1,904,946	1,621,374	3,638,998	3,070,934
Depreciation and amortization	<u>1,122,405</u>	<u>814,489</u>	<u>2,242,728</u>	<u>1,566,945</u>
Operating income (loss)	<u>(653,474)</u>	<u>21,013</u>	<u>(1,037,606)</u>	<u>(1,158,548)</u>
Interest:				
Income	70,009	24,114	102,485	56,164
Expense	<u>(857,713)</u>	<u>(563,648)</u>	<u>(1,903,278)</u>	<u>(1,061,677)</u>
Net interest expense	<u>(787,704)</u>	<u>(539,534)</u>	<u>(1,800,793)</u>	<u>(1,005,513)</u>
Loss before income tax	(1,441,178)	(518,521)	(2,838,399)	(2,164,061)
Income tax provision	<u>(2,695)</u>	<u>—</u>	<u>(4,948)</u>	<u>(500)</u>
Net loss	<u>\$ (1,443,873)</u>	<u>\$ (518,521)</u>	<u>\$ (2,843,347)</u>	<u>\$ (2,164,561)</u>
Loss per common share, basic and diluted	<u>\$ (0.09)</u>	<u>\$ (0.04)</u>	<u>\$ (0.19)</u>	<u>\$ (0.16)</u>
Weighted average shares outstanding, basic and diluted	<u>16,004,680</u>	<u>13,226,526</u>	<u>14,975,124</u>	<u>13,226,526</u>

See notes to condensed consolidated financial statements.

**GRANITE CITY FOOD & BREWERY LTD.**  
**CONDENSED CONSOLIDATED STATEMENTS OF CASH FLOWS**  
(Unaudited)

	<u>Twenty-six Weeks Ended</u>	
	<u>June 26,</u>	<u>June 27,</u>
	<u>2007</u>	<u>2006</u>
Cash flows from operating activities:		
Net loss	\$(2,843,347)	\$(2,164,561)
Adjustments to reconcile net loss to net cash used in operating activities:		
Depreciation and amortization	2,242,728	1,566,945
Stock option compensation expense	466,459	407,484
Loss on disposal of asset	79,126	2,414
Deferred rent	264,022	181,195
Changes in operating assets and liabilities:		
Inventory	25,892	(76,151)
Prepays and other	(8,276)	(593,770)
Accounts payable	209,092	253,990
Accrued expenses	(712,226)	344,783
Net cash used in operating activities	<u>(276,530)</u>	<u>(77,671)</u>
Cash flows from investing activities:		
Purchase of:		
Property and equipment	(2,289,499)	(2,580,432)
Intangible assets and other	(3,617)	(11,112)
Net cash used in investing activities	<u>(2,293,116)</u>	<u>(2,591,544)</u>
Cash flows from financing activities:		
Payments on capital lease obligations	(6,522,478)	(442,214)
Payments on long term-debt	(120,529)	(119,132)
Proceeds (cost incurred) from issuance of stock	12,788,108	(2,141)
Net cash provided by (used in) financing activities	<u>6,145,101</u>	<u>(563,487)</u>
Net increase (decrease) in cash	3,575,455	(3,232,702)
Cash and cash equivalents, beginning	7,671,750	9,836,231
Cash and cash equivalents, ending	<u>\$11,247,205</u>	<u>\$ 6,603,529</u>
Supplemental disclosure of non-cash investing and financing activities:		
Land, buildings and equipment acquired under capital lease agreements	<u>\$ —</u>	<u>\$ 5,364,351</u>
Property and equipment, intangibles and stock issuance costs included in accounts payable	<u>\$ 1,288,078</u>	<u>\$ 1,322,239</u>
Income taxes paid	<u>\$ 4,948</u>	<u>\$ 500</u>

See notes to condensed consolidated financial statements.

**GRANITE CITY FOOD & BREWERY LTD.**

**NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS  
(Unaudited)**

Thirteen and Twenty-six weeks ended June 26, 2007 and June 27, 2006

**1. Summary of significant accounting policies**

Background

Granite City Food & Brewery Ltd. (the "Company") develops and operates casual dining restaurants known as Granite City Food & Brewery®. The restaurant theme is upscale casual dining with a wide variety of menu items that are prepared fresh daily, combined with freshly brewed hand-crafted beers finished on-site. The first Granite City restaurant opened in St. Cloud, Minnesota in July 1999 and the Company subsequently expanded to other Midwest markets, opening its 19<sup>th</sup> restaurant on July 3, 2007. The Company also operates a beer production facility which is used to provide raw material support to its restaurants to create consistent quality and operational efficiencies.

The Company's expansion strategy focuses on development of restaurants in markets where management believes the Company's concept will have broad appeal and attractive restaurant-level economics.

Principles of consolidation and presentation

The accompanying unaudited condensed consolidated financial statements have been prepared in accordance with accounting principles generally accepted in the United States of America and regulations of the Securities and Exchange Commission. Accordingly, they do not include all the information and footnotes required by U.S. generally accepted accounting principles for complete financial statements. These statements include the accounts and operations of the Company and its subsidiary corporations under which its Kansas locations are operated. Fifty-one percent of the stock of each of the subsidiary corporations is owned by a resident of Kansas and the Company owns the remainder of the stock of each corporation. Each resident-owner of the stock of these entities has entered into a buy-sell agreement with each corporation providing, among other things, that transfer of the shares is restricted and that the shareholder must sell his shares to the corporation upon certain events, including termination of employment (if employed by the Company) or any event which disqualifies the resident-owner from owning the shares under applicable laws and regulations of the state. The Company has entered into a master agreement with each separate corporation that permits the operation of the restaurants and leases to each corporation the Company's property and facilities. Each corporation pays all of its operating expenses and obligations, and the Company retains, as consideration for the operating arrangements and the lease of property and facilities, the net profit from its operations. The Company has determined that the foregoing ownership structure will cause these separate corporations to be treated as variable interest entities in which the Company has a controlling financial interest for the purpose of FASB Interpretation 46 (R), *Consolidation of Variable Interest Entities*. As such, the corporations are consolidated with the Company's financial statements and the Company's financial statements do not reflect a minority ownership in those separate corporations. All references to the Company in these financial statements relate to the consolidated entity.

In the opinion of management, all adjustments, consisting of normal recurring adjustments, which are necessary for a fair statement of its financial position as of June 26, 2007 and the results of operations for the interim periods ended June 26, 2007 and June 27, 2006 have been included.

The balance sheet at December 26, 2006, has been derived from the audited financial statements at that date, but does not include all of the information and notes required by generally accepted accounting principles for complete financial statements. Certain information and note disclosures normally included in the Company's annual financial statements have been condensed or omitted. These condensed financial statements should be read in conjunction with the financial statements and notes thereto included in the Company's Annual Report

on Form 10-K for the fiscal year ended December 26, 2006, filed with the Securities and Exchange Commission on February 21, 2007.

The results of operations for the twenty-six weeks ended June 26, 2007 are not necessarily indicative of the results to be expected for the entire year.

#### Reclassification

Certain reclassifications have been made to the financial statements for the second quarter and first half of 2006 in order for them to conform to the presentation of the financial statements for the second quarter and first half of 2007. These reclassifications have no effect on the accumulated deficit or net loss previously reported.

#### Revenue recognition

Revenue is derived from the sale of prepared food and beverage and select retail items. Revenue is recognized at the time of sale and is reported on the Company's statement of operations net of sales taxes collected. Revenue derived from gift card sales is recognized at the time the gift card is redeemed. Until the redemption of gift cards occurs, the outstanding balances on such cards are included in accrued expenses in the accompanying consolidated balance sheets. The Company recognizes gift card breakage amounts based upon historical redemption patterns, which represent the balance of gift cards for which the Company believes the likelihood of redemption by the customer is remote.

#### Cash and cash equivalents

The Company maintains its cash at financial institutions in Minnesota, South Dakota, Kansas and Ohio. At times the bank balances exceed the limits insured by federal agencies. The Company considers all highly liquid instruments with maturities of three months or less at the time of issuance to be cash equivalents.

#### Stock-based compensation

The Company records stock-based compensation in accordance with the provisions of Financial Accounting Standards Board ("FASB") Statement of Financial Accounting Standard ("SFAS") No. 123 (revised 2004) ("SFAS 123(R)"), *Share-Based Payment*, and SEC Staff Accounting Bulletin No. 107 ("SAB 107"), *Share-Based Payment*, requiring the measurement and recognition of all share-based compensation under the fair value method. The Company implemented SFAS 123(R) using the modified prospective method, effective December 28, 2005, the first day of its 2006 fiscal year.

#### Accounting for leases

The Company leases most of its restaurant properties. Leases are accounted for under the provisions of SFAS No. 13 and SFAS No. 98, *Accounting for Leases*, as well as other subsequent amendments and authoritative literature including FASB Staff Position No. FAS 13-1, *Accounting for Rental Costs Incurred During a Construction Period*. For leases that contain rent escalations, the Company records the total rent payable during the lease term on a straight-line basis over the initial lease term, including the "build-out" or "rent-holiday" period where no rent payments are typically due under the terms of the lease. Any difference between minimum rent and straight-line rent is recorded as deferred rent. Contingent rent expense, which is based on a percentage of revenue, is also recorded to the extent it exceeds minimum base rent per the lease agreement. Deferred rent also includes a tenant improvement allowance the Company received which is being amortized as a reduction of rent expense on a straight-line basis over the initial term of the lease.

#### Earnings (loss) per share

Basic loss per common share is calculated by dividing net loss by the weighted average number of common shares outstanding in each respective fiscal period.

#### Recent accounting pronouncements

In July 2006, the Financial Accounting Standards Board ("FASB") issued FASB Interpretation No. 48, *Accounting for Uncertainty in Income Taxes*, ("FIN 48") which clarifies the accounting and disclosures for uncertainty in income taxes recognized in the financial statements in accordance with SFAS No. 109,



“Accounting for Income Taxes.” FIN 48 also provides guidance on the de-recognition of uncertain tax positions, financial statement classification, accounting for interest and penalties, accounting for interim periods and adds new disclosure requirements. The adoption of FIN 48 did not have a material impact on the Company’s financial statements or disclosures. As of December 26, 2006 and June 26, 2007 the Company did not recognize any assets or liabilities for unrecognized tax benefits relative to uncertain tax positions. Upon review of the Company’s net operating loss carryforwards, management believes it is more likely than not that the Company’s tax positions taken will be sustained. Any interest or penalties resulting from examinations will be recognized as a component of the income tax provision. However, since there are no unrecognized tax benefits as a result of tax positions taken, there are no accrued interest and penalties.

In September 2006, the FASB issued SFAS No. 157, *Fair Value Measurements* (“SFAS 157”). SFAS 157 provides guidance for using fair value to measure assets and liabilities. The standard expands required disclosures about the extent to which companies measure assets and liabilities at fair value, the information used to measure fair value, and the effect of fair value measurements on earnings. SFAS 157 is effective for fiscal years beginning after November 15, 2007. The Company is currently evaluating the impact of adopting SFAS 157 on its consolidated financial statements.

In February 2007, the FASB issued SFAS 159, *The Fair Value Option for Financial Assets and Financial Liabilities (as amended)* (“SFAS 159”), which permits entities to choose to measure many financial instruments and certain other items at fair value. The standard provides companies with the opportunity to mitigate volatility in reported earnings caused by measuring related assets and liabilities differently without having to apply complex hedge accounting provisions. The provisions of SFAS 159 are effective for fiscal years beginning after November 15, 2007. The Company is currently evaluating the impact of adopting SFAS 159 on its financial statements.

**2. Non-current assets**

Property and equipment

Property and equipment are recorded at cost and depreciated over the estimated useful lives of the related assets. The cost of leasehold improvements is depreciated over the initial term of the related lease. Depreciation is computed on the straight-line method for financial reporting purposes and accelerated methods for income tax purposes. Amortization of assets acquired under capital lease is included in depreciation expense. The following is a summary of the Company’s property and equipment at June 26, 2007 and December 26, 2006:

	<u>June 26, 2007</u>	<u>December 26, 2006</u>
Land	\$ 18,000	\$ 18,000
Buildings	33,841,945	33,851,945
Leasehold improvements	8,262,104	8,220,963
Equipment and furniture	21,187,216	20,728,013
Construction in progress*	<u>3,634,098</u>	<u>624,422</u>
	66,943,363	63,443,343
Less accumulated depreciation	<u>11,607,668</u>	<u>9,425,219</u>
	<u>\$ 55,335,695</u>	<u>\$ 54,018,124</u>

\*Construction in progress includes the following approximate amounts for items yet to be placed in service:

	<u>June 26, 2007</u>	<u>December 26, 2006</u>
Architecture fees for future locations	\$ 400,000	\$ 100,000
Equipment at future locations	\$ 3,180,000	\$ 400,000
Equipment at the beer production facility	—	\$ 125,000
Cost to secure property leases at future locations	\$ 45,000	—

Included in property and equipment are the following assets held under capital leases:

	<u>June 26, 2007</u>	<u>December 26, 2006</u>
Land	\$ 18,000	\$ 18,000
Building	33,841,945	33,851,945
Equipment and leasehold improvements	1,624,533	7,807,724
	<u>35,484,478</u>	<u>41,677,669</u>
Less accumulated depreciation	4,351,987	3,718,654
	<u>\$ 31,132,491</u>	<u>\$ 37,959,015</u>

Intangible assets and other

Intangible assets and other assets consisted of the following:

	<u>June 26, 2007</u>	<u>December 26, 2006</u>
Intangible assets:		
Liquor licenses	\$ 264,415	\$ 264,415
Trademarks	123,251	109,741
Other:		
Capitalized loan costs	175,379	205,054
Security deposits	269,279	279,427
	<u>832,324</u>	<u>858,637</u>
Less accumulated amortization	114,106	98,217
	<u>\$ 718,218</u>	<u>\$ 760,420</u>

### 3. Accrued expenses

Accrued expenses consisted of the following:

	<u>June 26, 2007</u>	<u>December 26, 2006</u>
Payroll related	\$ 1,914,607	\$ 2,205,712
Deferred revenue from gift cards	869,914	1,355,773
Sales taxes	465,048	493,772
Interest	279,083	278,131
Real estate taxes	335,536	245,299
Insurance	—	89,646
Other	528,316	436,397
	<u>\$ 4,392,504</u>	<u>\$ 5,104,730</u>

### 4. Capital leases

In March 2007, the Company completed a private placement of common stock to accredited investors described in Note 7 below. Utilizing approximately \$6.0 million of these proceeds, the Company retired the entire balance of capital lease debt due DHW Leasing, L.L.C. ("DHW") pursuant to the master lease agreement entered into in September 2006.

Minimum future lease payments under all capital leases as of June 26, 2007 are:

<u>Year ended:</u>	<u>Capital Leases</u>
2007	\$ 2,075,557
2008	4,076,234
2009	4,023,444
2010	3,847,242
2011	3,737,719
Thereafter	<u>52,462,327</u>
Total minimum lease payments	<u>70,222,523</u>
Less amount representing interest	<u>37,358,008</u>
Present value of net minimum lease payments	<u>32,864,515</u>
Less current portion	<u>983,930</u>
Long-term portion of obligations	<u>\$ 31,880,585</u>

Amortization expense related to the assets held under capital leases is included with depreciation expense on the Company's statements of operations.

## 5. Commitments and contingencies

### Litigation

From time to time, lawsuits are threatened or filed against the Company in the ordinary course of business. Such lawsuits typically involve claims from customers, former or current employees, and others related to issues common to the restaurant industry. A number of such claims may exist at any given time. Although there can be no assurance as to the ultimate disposition of these matters, it is management's opinion, based upon the information available at this time, that the expected outcome of these matters, individually or in the aggregate, will not have a material adverse effect on the results of operation, liquidity or financial condition of the Company.

### Rockford, Illinois:

In July 2007, the Company commenced leasing its Rockford, Illinois restaurant under a 15-year net lease agreement based on the terms specified in the development agreement with Dunham Capital Management L.L.C. ("Dunham") for the development of restaurants. The restaurant was constructed for the Company on a build-to-suit basis. Currently, the annual rent is \$441,000 of which \$231,742 is classified as a capital lease and \$179,258 plus percentage rent is classified as an operating lease. Every five years, base rent exclusive of the land portion of the lease will increase 10%. The Company will be responsible for any real-estate taxes and all operating costs and the lease may be extended at the Company's option for up to three additional five-year periods on the same terms and conditions. Rental costs associated with the operating lease incurred during the construction period were recognized as pre-opening costs and escalated rent will be recognized as expense on a straight-line basis over the term of the lease.

### East Peoria and Orland Park, Illinois, Creve Coeur, Missouri and Rogers, Arkansas:

In 2007, the Company entered into 20-year net lease agreements relating to restaurants it anticipates opening during 2007 in East Peoria and Orland Park, Illinois, Creve Coeur, Missouri and Rogers, Arkansas under the terms specified in the development agreement with Dunham. Each restaurant will be constructed for the Company on a build-to-suit basis. The annual rent of each will be equal to 10.5% of the construction cost including land cost and will escalate 10% at the end of each five-year period. The Company will be responsible for any real-estate taxes and all operating costs. The term of each lease will commence when operations begin and may be extended at the Company's option for up to five additional five-year periods on the same terms and conditions. Rental costs associated with the operating leases incurred during the

