

LIFE TIME FITNESS, INC.
Form 10-Q
April 29, 2014

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

FORM 10-Q

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

For the quarterly period ended March 31, 2014

or

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

Commission File Number: 001-32230

Life Time Fitness, Inc.
(Exact name of registrant as specified in its charter)

Minnesota
(State or other jurisdiction of incorporation or
organization)

41-1689746
(I.R.S. Employer Identification No.)

2902 Corporate Place
Chanhassen, Minnesota
(Address of principal executive offices)

55317
(Zip Code)

952-947-0000
(Registrant's telephone number, including area code)

Indicate by check mark whether the registrant (1) has filed all reports required to be filed by Section 13 or 15(d) of the Securities Exchange Act of 1934 during the preceding 12 months (or for such shorter period that the registrant was required to file such reports), and (2) has been subject to such filing requirements for the past 90 days. Yes No
Indicate by check mark whether the registrant has submitted electronically and posted on its corporate Web site, if any, every Interactive Data File required to be submitted and posted pursuant to Rule 405 of Regulation S-T (§232.405 of this chapter) during the preceding 12 months (or for such shorter period that the registrant was required to submit and post such files). Yes No

Indicate by check mark whether the registrant is a large accelerated filer, an accelerated filer, a non-accelerated filer or a smaller reporting company. See definitions of "large accelerated filer," "accelerated filer" and "smaller reporting company" in Rule 12b-2 of the Exchange Act.

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| | | | |
|-------------------------|--|---------------------------|--------------------------|
| Large accelerated filer | <input checked="" type="checkbox"/> | Accelerated filer | <input type="checkbox"/> |
| Non-accelerated filer | <input type="checkbox"/> (Do not check if a smaller reporting company) | Smaller reporting company | <input type="checkbox"/> |

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

The number of shares outstanding of the registrant's common stock as of April 18, 2014 was 40,870,982 common shares.

PART I. FINANCIAL INFORMATION

Item 1. Financial Statements

LIFE TIME FITNESS, INC. AND SUBSIDIARIES

CONSOLIDATED BALANCE SHEETS

(In thousands, except share and per share data)

(Unaudited)

| | March 31, 2014 | December 31, 2013 |
|--|-------------------|----------------------|
| ASSETS | | |
| Current assets: | | |
| Cash and cash equivalents | \$12,540 | \$8,334 |
| Accounts receivable, net | 12,114 | 8,298 |
| Center operating supplies and inventories | 33,495 | 32,778 |
| Prepaid expenses and other current assets | 32,330 | 25,802 |
| Deferred membership origination costs | 9,549 | 9,945 |
| Deferred income taxes | 3,644 | 6,881 |
| Income tax receivable | — | 6,698 |
| Total current assets | 103,672 | 98,736 |
| Property and equipment, net | 2,147,753 | 2,105,077 |
| Restricted cash | 1,137 | 850 |
| Deferred membership origination costs | 4,980 | 5,210 |
| Goodwill | 59,195 | 49,195 |
| Intangible assets, net | 34,783 | 29,299 |
| Other assets | 42,370 | 42,684 |
| Total assets | \$2,393,890 | \$2,331,051 |
| LIABILITIES AND SHAREHOLDERS' EQUITY | | |
| Current liabilities: | | |
| Current maturities of long-term debt | \$27,095 | \$24,505 |
| Accounts payable | 29,082 | 28,645 |
| Construction accounts payable | 39,116 | 47,342 |
| Accrued expenses | 73,117 | 67,435 |
| Deferred revenue | 45,198 | 35,032 |
| Total current liabilities | 213,608 | 202,959 |
| Long-term debt, net of current portion | 902,023 | 824,093 |
| Deferred rent liability | 33,070 | 28,933 |
| Deferred income taxes | 97,423 | 100,504 |
| Deferred revenue | 5,013 | 5,246 |
| Other liabilities | 21,278 | 21,287 |
| Total liabilities | 1,272,415 | 1,183,022 |
| Commitments and contingencies (Note 6) | | |
| Shareholders' equity: | | |
| Undesignated preferred stock, 10,000,000 shares authorized; none issued or outstanding | — | — |
| Common stock, \$.02 par value, 75,000,000 shares authorized; 41,277,944 and 42,115,549 shares issued and outstanding, respectively | 826 | 843 |
| Additional paid-in capital | 347,964 | 402,147 |
| Retained earnings | 778,969 | 750,654 |

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| | | | |
|--|-------------|-------------|---|
| Accumulated other comprehensive loss | (6,284 |) (5,615 |) |
| Total shareholders' equity | 1,121,475 | 1,148,029 | |
| Total liabilities and shareholders' equity | \$2,393,890 | \$2,331,051 | |

See notes to unaudited consolidated financial statements.

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LIFE TIME FITNESS, INC. AND SUBSIDIARIES
CONSOLIDATED STATEMENTS OF OPERATIONS

(In thousands, except per share data)

(Unaudited)

| | For the Three Months Ended March 31, | |
|--|---|-----------|
| | 2014 | 2013 |
| Revenue: | | |
| Membership dues | \$196,815 | \$186,374 |
| Enrollment fees | 3,123 | 3,396 |
| In-center revenue | 98,405 | 91,971 |
| Total center revenue | 298,343 | 281,741 |
| Other revenue | 13,612 | 9,006 |
| Total revenue | 311,955 | 290,747 |
| Operating expenses: | | |
| Center operations | 183,118 | 169,962 |
| Advertising and marketing | 12,339 | 10,959 |
| General and administrative | 15,864 | 15,356 |
| Other operating | 14,422 | 12,834 |
| Depreciation and amortization | 32,138 | 29,262 |
| Total operating expenses | 257,881 | 238,373 |
| Income from operations | 54,074 | 52,374 |
| Other income (expense): | | |
| Interest expense, net of interest income | (7,851 |) (6,129 |
| Equity in earnings of affiliate | 297 | 346 |
| Total other expense | (7,554 |) (5,783 |
| Income before income taxes | 46,520 | 46,591 |
| Provision for income taxes | 18,205 | 18,490 |
| Net income | \$28,315 | \$28,101 |
| Basic earnings per common share | \$0.70 | \$0.68 |
| Diluted earnings per common share | \$0.69 | \$0.67 |
| Weighted average number of common shares outstanding – basic | 40,603 | 41,295 |
| Weighted average number of common shares outstanding – diluted | 40,870 | 41,646 |

See notes to unaudited consolidated financial statements.

LIFE TIME FITNESS, INC. AND SUBSIDIARIES
 CONSOLIDATED STATEMENTS OF COMPREHENSIVE INCOME
 (In thousands)
 (Unaudited)

| | For the Three Months Ended March 31, | |
|---|---|----------|
| | 2014 | 2013 |
| Net income | \$28,315 | \$28,101 |
| Other comprehensive income (loss), net of income tax: | | |
| Foreign currency translation adjustments, net of income tax benefit of \$609 and \$385, respectively | (884 |) (584 |
| Unrealized gains on cash flow hedges, net of income taxes of \$(143) and \$(214), respectively | 215 | 321 |
| Other comprehensive loss, net of income tax: | (669 |) (263 |
| Comprehensive income | \$27,646 | \$27,838 |

See notes to unaudited consolidated financial statements.

LIFE TIME FITNESS, INC. AND SUBSIDIARIES
CONSOLIDATED STATEMENTS OF CASH FLOWS

(In thousands)

(Unaudited)

| | For the Three Months Ended | |
|---|----------------------------|-----------|
| | March 31, | |
| | 2014 | 2013 |
| Cash flows from operating activities: | | |
| Net income | \$28,315 | \$28,101 |
| Adjustments to reconcile net income to net cash provided by operating activities: | | |
| Depreciation and amortization | 32,138 | 29,262 |
| Deferred income taxes | (77 |) 4,582 |
| Gain on disposal of property and equipment, net | (416 |) (228 |
| Amortization of deferred financing costs | 577 | 505 |
| Share-based compensation | 3,286 | 2,830 |
| Excess tax benefit related to share-based compensation | (846 |) (4,657 |
| Changes in operating assets and liabilities | 14,889 | 16,645 |
| Other | (206 |) (809 |
| Net cash provided by operating activities | 77,660 | 76,231 |
| Cash flows from investing activities: | | |
| Purchases of property and equipment | (82,826 |) (59,145 |
| Acquisitions, net of cash acquired | (12,400 |) — |
| Proceeds from sale of property and equipment | 447 | 555 |
| Proceeds from property insurance settlements | — | 121 |
| Increase in other assets | (33 |) (730 |
| Increase in restricted cash | (287 |) (275 |
| Net cash used in investing activities | (95,099 |) (59,474 |
| Cash flows from financing activities: | | |
| Proceeds from long-term borrowings | 80,000 | 75,000 |
| Repayments of long-term borrowings | (4,909 |) (1,696 |
| Proceeds from (repayments of) credit facility, net | 5,300 | (78,400 |
| Increase in deferred financing costs | (947 |) (465 |
| Excess tax benefit related to share-based compensation | 846 | 4,657 |
| Proceeds from stock option exercises | 2,139 | 872 |
| Proceeds from employee stock purchase plan | 483 | 414 |
| Stock purchased for employee stock purchase plan | (701 |) (569 |
| Repurchases of common stock | (60,498 |) (19,349 |
| Net cash provided by (used in) financing activities | 21,713 | (19,536 |
| Effect of exchange rates on cash and cash equivalents | (68 |) (26 |
| Increase (decrease) in cash and cash equivalents | 4,206 | (2,805 |
| Cash and cash equivalents – beginning of period | 8,334 | 16,499 |
| Cash and cash equivalents – end of period | \$12,540 | \$13,694 |
| See notes to unaudited consolidated financial statements. | | |

LIFE TIME FITNESS, INC. AND SUBSIDIARIES
 NOTES TO UNAUDITED CONSOLIDATED FINANCIAL STATEMENTS

(Table amounts in thousands, except share and per share data)

1. Basis of Presentation

The accompanying unaudited consolidated financial statements have been prepared in accordance with accounting principles generally accepted in the United States for interim financial information and with the instructions to Form 10-Q and Article 10 of Regulation S-X. Accordingly, they do not include all of the information and notes required by accounting principles generally accepted in the United States for complete financial statements. In the opinion of management, all adjustments (consisting of normal recurring adjustments) considered necessary to fairly present our consolidated financial position, results of operations and cash flows for the periods have been included. These interim consolidated financial statements and the related notes should be read in conjunction with the annual consolidated financial statements and notes included in the latest Form 10-K, as filed with the Securities and Exchange Commission ("SEC"), which includes audited consolidated financial statements for the three fiscal years ended December 31, 2013.

2. Share-Based Compensation

Stock Option and Incentive Plans

We have three share-based compensation plans: the Amended and Restated Life Time Fitness, Inc. 2004 Long-Term Incentive Plan (the "2004 Plan"); the Life Time Fitness, Inc. 2011 Long-Term Incentive Plan (the "2011 Plan") and an Employee Stock Purchase Plan (the "ESPP"), collectively, the share-based compensation plans. We no longer make grants under the 2004 Plan. There are 2,500,000 shares of common stock reserved for grant under the 2011 Plan and, as of March 31, 2014, there were 933,817 shares available for grant. The types of awards that may be granted under the 2011 Plan include incentive and non-qualified options to purchase shares of common stock, stock appreciation rights, restricted shares, restricted share units, performance awards and other types of share-based awards.

As of March 31, 2014, we had granted a total of 1,929,665 options to purchase common stock under all of the share-based compensation plans, of which options to purchase 98,954 shares were outstanding and vested, and a total of 5,132,304 restricted shares were granted, of which 1,440,460 restricted shares were outstanding and unvested. We use the term "restricted shares" to define unvested shares granted to employees and non-employee directors. We use the term "vest" to define the lapse of vesting restrictions on restricted shares.

Total share-based compensation expense included in our consolidated statements of operations for the three months ended March 31, 2014 and 2013, was as follows:

| | For the Three Months Ended | |
|---|----------------------------|---------|
| | March 31, | |
| | 2014 | 2013 |
| Share-based compensation expense related to restricted shares | \$3,256 | \$2,800 |
| Share-based compensation expense related to ESPP | 30 | 30 |
| Total share-based compensation expense | \$3,286 | \$2,830 |

LIFE TIME FITNESS, INC. AND SUBSIDIARIES
 NOTES TO UNAUDITED CONSOLIDATED FINANCIAL STATEMENTS
 (Table amounts in thousands, except share and per share data)

Summary of Restricted Stock Activity

| | Shares | Weighted Average Grant Date Fair Value |
|----------------------------------|-----------|--|
| Outstanding at December 31, 2013 | 1,429,730 | \$44.19 |
| Granted | 391,733 | \$44.38 |
| Canceled | (91,013 |) \$45.30 |
| Vested | (289,990 |) \$40.31 |
| Outstanding at March 31, 2014 | 1,440,460 | \$44.95 |

During the three months ended March 31, 2014 and 2013, we issued 391,733 and 328,550 shares of restricted stock, respectively, with an aggregate grant date fair value of \$17.4 million and \$13.8 million, respectively. The grant date fair value of restricted shares that vested during the three months ended March 31, 2014 and 2013 was \$11.7 million and \$20.1 million, respectively. The total value of each restricted stock grant, based on the fair value of the stock on the date of grant, is amortized to compensation expense on a straight-line basis over the related vesting period. As of March 31, 2014, there was \$35.3 million of unrecognized compensation expense related to restricted stock that is expected to vest. We plan to recognize this amount over a weighted average period of 2.9 years.

Special 2012 Long-Term Performance-Based Restricted Stock Grant

In May, July and August 2012, the Compensation Committee of our Board of Directors approved the grant of a total of 658,500 shares of long-term performance-based restricted stock to serve as an incentive to our senior management team to achieve certain cumulative diluted earnings per share ("EPS") and return on invested capital ("ROIC") targets during performance periods that end on December 31, 2015 and December 31, 2016. On March 31, 2014, 576,500 shares remained outstanding under this grant.

The Compensation Committee set the cumulative diluted EPS targets at 1.5 times the compound annual growth rate under our then-current long range plan and the ROIC targets at 1.1 times the ROIC under our then-current long range plan. The following are the performance metrics underlying the targets:

| | Cumulative Diluted EPS Measurement Period | EPS Target | ROIC Measurement Period | ROIC Target | |
|---|---|---------------|-------------------------------|----------------|---|
| 2015 Performance Period | 4/1/2012 | | 1/1/2015 | | |
| 50% vest if we achieve both performance targets | through 12/31/2015 | \$ 13.68 | through 12/31/2015 | 8.9 | % |
| 2016 Performance Period | 4/1/2012 | | 1/1/2016 | | |
| All/remaining vest if we achieve both performance targets | through 12/31/2016 | \$ 18.96 | through 12/31/2016 | 9.0 | % |

A maximum of \$26.5 million could be recognized as compensation expense under this grant if all cumulative diluted EPS and ROIC targets are met. We do not believe that achievement of either the cumulative diluted EPS or the ROIC targets is currently probable, and, therefore, we have not recognized any compensation expense associated with the grant.

If it becomes probable that the cumulative diluted EPS and ROIC performance targets will be achieved, a cumulative adjustment will be recorded and the remaining compensation expense will be recognized over the remaining performance period. If all of the targets had been considered probable at March 31, 2014, we would have recognized \$12.3 million of non-cash performance share-based compensation expense during the period ended March 31, 2014. The probability of reaching the targets is evaluated each reporting period. If we later determined

LIFE TIME FITNESS, INC. AND SUBSIDIARIES
 NOTES TO UNAUDITED CONSOLIDATED FINANCIAL STATEMENTS

(Table amounts in thousands, except share and per share data)

that it is no longer probable that the minimum cumulative diluted EPS and ROIC performance targets for the grants will be met, no further compensation expense would be recognized and any previously recognized compensation expense would be reversed. In the event that we do not achieve the specified cumulative diluted EPS and ROIC targets for the performance period ending December 31, 2016, the restricted shares will be forfeited. None of these shares were included in our total diluted share count at March 31, 2014 or 2013.

Summary of Stock Option Activity

| | Shares | Weighted Average Exercise Price | Weighted Average Remaining Contractual Term (Years) | Aggregate Intrinsic Value |
|----------------------------------|-----------|---------------------------------------|--|------------------------------|
| Outstanding at December 31, 2013 | 215,668 | \$25.64 | 1.1 | \$4,616 |
| Exercised | (111,675) |) \$19.16 | | |
| Canceled | (5,039) |) \$44.66 | | |
| Outstanding at March 31, 2014 | 98,954 | \$31.99 | 1.4 | \$1,601 |
| Vested at March 31, 2014 | 98,954 | \$31.99 | 1.4 | \$1,601 |

No stock options have been granted since 2007. As of March 31, 2014, there was no unrecognized compensation expense related to stock options.

The aggregate intrinsic values in the table above represent the total pretax intrinsic values (the differences between our closing stock price and the exercise price, multiplied by the number of in-the-money options) that would have been received by the option holders had all option holders exercised their options on that date. This amount changes based on the fair market value of our stock. Total intrinsic value of options exercised during the three months ended March 31, 2014 and 2013 was \$3.2 million and \$0.9 million, respectively.

Our net cash proceeds from the exercise of stock options were \$2.1 million and \$0.9 million for the three months ended March 31, 2014 and 2013, respectively. The excess income tax benefit realized from stock option exercises and restricted stock vesting was \$0.8 million and \$4.7 million, respectively, for those same periods. In accordance with the related accounting guidance, this tax benefit is presented as a financing cash inflow. There is a corresponding cash outflow included in cash flows from operating activities.

Employee Stock Purchase Plan

Our ESPP provides for the sale of up to 1,500,000 shares of our common stock to our employees at discounted purchase prices. The cost per share under this plan is 90% of the fair market value of our common stock on the last day of the purchase period, as defined. The current purchase period for employees under the ESPP began January 1, 2014 and ends June 30, 2014. Compensation expense under the ESPP is estimated based on the discount of 10% at the end of the purchase period. During the three months ended March 31, 2014, \$0.5 million was withheld from employees for the purpose of purchasing shares under the ESPP. There were 1,245,581 shares of common stock available for purchase under the ESPP as of March 31, 2014.

Share Repurchase Plans

In June 2006, our Board of Directors authorized the repurchase of up to 500,000 shares of our common stock from time to time in the open market or otherwise for the primary purpose of offsetting the dilutive effect of shares issued under our ESPP. During the three months ended March 31, 2014, we repurchased 15,146 shares under this authorization for approximately \$0.7 million. As of March 31, 2014, there were 245,581 remaining shares authorized to be repurchased for this purpose.

In August 2013, our Board of Directors authorized the repurchase of up to \$200.0 million of our outstanding common stock from time to time through open market or privately negotiated transactions. The authorization to repurchase shares terminates when the aggregate repurchase amount totals \$200.0 million or at the close of business on August

16, 2015, whichever occurs first. The share repurchase program does not obligate us to repurchase any

LIFE TIME FITNESS, INC. AND SUBSIDIARIES
 NOTES TO UNAUDITED CONSOLIDATED FINANCIAL STATEMENTS

(Table amounts in thousands, except share and per share data)

dollar amount or number of shares of our common stock and the program may be extended, modified, suspended or discontinued at any time. During the three months ended March 31, 2014, we repurchased 1,250,000 shares under this program for approximately \$60.5 million. As of March 31, 2014, \$108.5 million remained authorized under this program.

3. Earnings per Share

Basic EPS is computed by dividing net income applicable to common shareholders by the weighted average number of shares of common stock outstanding for each year. Diluted EPS is computed similarly to basic EPS, except that the denominator is increased for the conversion of any dilutive common stock equivalents, the assumed exercise of dilutive stock options using the treasury stock method and unvested restricted stock awards using the treasury stock method. Stock options excluded from the calculation of diluted EPS because the option exercise price was greater than the average market price of the common share were 15,540 and 20,037 for the three months ended March 31, 2014 and 2013, respectively.

The basic and diluted EPS calculations are shown below:

| | For the Three Months Ended | |
|--|----------------------------|----------|
| | March 31, | |
| | 2014 | 2013 |
| Net income | \$28,315 | \$28,101 |
| Weighted average number of common shares outstanding – basic | 40,603 | 41,295 |
| Effect of dilutive stock options | 19 | 93 |
| Effect of dilutive restricted stock awards | 248 | 258 |
| Weighted average number of common shares outstanding – diluted | 40,870 | 41,646 |
| Basic earnings per common share | \$0.70 | \$0.68 |
| Diluted earnings per common share | \$0.69 | \$0.67 |

4. Operating Segment

Our operations are conducted mainly through our distinctive and large, multi-use sports and athletic, professional fitness, family recreation and spa centers in a resort-like environment. We aggregate the activities of our centers and other ancillary products and services into one reportable segment. Each of the centers has similar economic characteristics, services, product offerings and customers, and in-center revenues are derived primarily from services to our members. Each of the other ancillary products and services either directly or indirectly, through advertising or branding, complement the operations of the centers. Our chief operating decision maker uses EBITDA as the primary measure of operating segment performance. Our chief operating decision maker is our Chief Executive Officer.

LIFE TIME FITNESS, INC. AND SUBSIDIARIES
 NOTES TO UNAUDITED CONSOLIDATED FINANCIAL STATEMENTS

(Table amounts in thousands, except share and per share data)

The following table presents revenue for the three months ended March 31, 2014 and 2013:

| | For the Three Months Ended | |
|-------------------------|----------------------------|-----------|
| | March 31, | |
| | 2014 | 2013 |
| Membership dues | \$196,815 | \$186,374 |
| Enrollment fees | 3,123 | 3,396 |
| Personal training | 48,883 | 46,014 |
| Other in-center revenue | 49,522 | 45,957 |
| Total center revenue | 298,343 | 281,741 |
| Other revenue | 13,612 | 9,006 |
| Total revenue | \$311,955 | \$290,747 |

5. Supplemental Cash Flow Information

Decreases (increases) in operating assets and increases (decreases) in operating liabilities are as follows:

| | For the Three Months Ended | |
|---|----------------------------|-----------|
| | March 31, | |
| | 2014 | 2013 |
| Accounts receivable, net | \$(3,943) |) \$794 |
| Center operating supplies and inventories | (724) |) (1,899) |
| Prepaid expenses and other current assets | (5,539) |) (2,146) |
| Deferred membership origination costs | 626 | 602 |
| Income tax receivable | 6,698 | — |
| Accounts payable | 684 | 2,723 |
| Accrued expenses | 6,513 | 8,921 |
| Deferred revenue | 6,336 | 6,543 |
| Deferred rent liability | 4,150 | 641 |
| Other liabilities | 88 | 466 |
| Changes in operating assets and liabilities | \$14,889 | \$16,645 |

We made cash payments for income taxes of \$1.3 million and \$8.9 million for the three months ended March 31, 2014 and 2013, respectively.

We made cash payments for interest, net of capitalized interest, of \$7.1 million and \$5.1 million for the three months ended March 31, 2014 and 2013, respectively. Capitalized interest was \$0.8 million and \$0.5 million for the same periods.

Construction accounts payable was \$39.1 million and \$34.9 million at March 31, 2014 and 2013, respectively.

6. Commitments and Contingencies

Litigation — We are engaged in proceedings incidental to the normal course of business. Due to their nature, such legal proceedings involve inherent uncertainties, including but not limited to court rulings, negotiations between affected parties and governmental intervention. We have established reserves for matters that are probable and estimable in amounts we believe are adequate to cover reasonable adverse judgments not covered by insurance. These reserves are not material to our consolidated financial statements. Based upon the information available to us

LIFE TIME FITNESS, INC. AND SUBSIDIARIES
NOTES TO UNAUDITED CONSOLIDATED FINANCIAL STATEMENTS

(Table amounts in thousands, except share and per share data)

and discussions with legal counsel, it is our opinion that the outcome of the various legal actions and claims that are incidental to our business will not have a material adverse impact on our consolidated financial position, results of operations or cash flows. Such matters are subject to many uncertainties, and the outcome of individual matters are not predictable with assurance.

7. Derivative Instruments

As part of our financial risk management program, we may periodically use interest rate swaps to manage known market exposures. Terms of derivative instruments are structured to match the terms of the risk being managed and are generally held to maturity.

In August 2011, we entered into an interest rate swap contract that effectively fixed the rates paid on a total of \$200.0 million of variable rate borrowings at 1.32% plus the applicable spread (which depends on our EBITDAR leverage ratio) until June 2016. EBITDAR is a non-GAAP, non-cash measure which consists of net income plus interest expense, net, provision for income taxes, depreciation and amortization and rent expense. We pay 1.32% and receive LIBOR on the notional amount of \$200.0 million. The contract has been designated a cash flow hedge against interest rate volatility. In accordance with applicable accounting guidance, changes in the fair value of the swap contract are recorded in accumulated other comprehensive (loss) income, net of tax. As of March 31, 2014, the \$2.0 million fair value loss, net of tax, of the swap contract was recorded as accumulated other comprehensive loss in the shareholders' equity section of our consolidated balance sheets and the \$3.4 million gross fair value of the swap contract was included in long-term debt.

On an ongoing basis, we assess whether the interest rate swap used in this hedging transaction is "highly effective" in offsetting changes in the fair value or cash flow of the hedged item by comparing the current terms of the swap and the debt to assure they continue to coincide and through an evaluation of the continued ability of the counterparty to the swap to honor its obligations under the swap. No ineffectiveness was experienced in the interest rate swap during the three months ended March 31, 2014. If it is determined that the derivative is not highly effective as a hedge or hedge accounting is discontinued, any change in fair value of the derivative since the last date at which it was determined to be effective would be recognized in earnings.

For more information on the swap contract, see Notes 8 and 9.

8. Fair Value Measurements

The accounting guidance establishes a framework for measuring fair value and expanded disclosures about fair value measurements. The guidance applies to all assets and liabilities that are measured and reported on a fair value basis. This enables the reader of the financial statements to assess the inputs used to develop those measurements by establishing a hierarchy for ranking the quality and reliability of the information used to determine fair values. The guidance requires that each asset and liability carried at fair value be classified into one of the following categories:

Level 1: Quoted market prices in active markets for identical assets or liabilities.

Level 2: Observable market based inputs or unobservable inputs that are corroborated by market data.

Level 3: Unobservable inputs that are not corroborated by market data.

Fair Value Measurements on a Recurring Basis

The fair value of the interest rate swap is determined using observable current market information such as the prevailing Eurodollar interest rates, Eurodollar yield curve rates and current fair values as quoted by recognized dealers, and also includes consideration of counterparty credit risk. The following table presents the fair value of our derivative financial instrument as of March 31, 2014 and December 31, 2013:

LIFE TIME FITNESS, INC. AND SUBSIDIARIES
 NOTES TO UNAUDITED CONSOLIDATED FINANCIAL STATEMENTS

(Table amounts in thousands, except share and per share data)

| | Total Fair Value | Fair Value Measurements Using: | | |
|---|------------------------|---|--|--|
| | | Quoted Prices in Active Markets for Identical Assets (Level 1) | Significant Other Observable Inputs (Level 2) | Significant Unobservable Inputs (Level 3) |
| Interest rate swap liability as of March 31, 2014 | \$3,400 | \$— | \$3,400 | \$— |
| Interest rate swap liability as of December 31, 2013 | \$3,762 | \$— | \$3,762 | \$— |

Fair Value Measurements on a Nonrecurring Basis

Assets and liabilities that are measured at fair value on a nonrecurring basis relate primarily to our tangible fixed assets, goodwill and intangible assets, which are remeasured when the derived fair value is below carrying value on our consolidated balance sheets. For these assets, we do not periodically adjust carrying value to fair value except in the event of impairment. If we determine that impairment has occurred, the carrying value of the asset would be reduced to fair value and the difference would be recorded as a loss within operating income in our consolidated statements of operations.

We had no remeasurements of such assets or liabilities to fair value during the three months ended March 31, 2014 or March 31, 2013.

Financial Assets and Liabilities Not Measured at Fair Value

The carrying amounts related to cash and cash equivalents (Level 1), accounts receivable, income tax receivable, accounts payable and accrued liabilities approximate fair value due to the relatively short maturities of such instruments.

The fair value of our long-term debt and capital leases are estimated based on estimated current rates for debt with similar terms, credit worthiness and the same remaining maturities. For variable rate loans that re-price frequently, fair values are based on carrying values. The fair value of fixed rate loans is estimated based on the discounted cash flows of the loans using current market rates, which are estimated based on recent financing transactions (Level 3). The fair value estimates presented are based on information available to us as of March 31, 2014. These fair value estimates have not been comprehensively revalued for purposes of these consolidated financial statements since that date, and current estimates of fair values may differ significantly.

The following table presents the carrying value and the estimated fair value of long-term debt:

| | March 31, 2014 | | December 31, 2013 | |
|----------------------------------|----------------|----------------------|-------------------|----------------------|
| | Carrying Value | Estimated Fair Value | Carrying Value | Estimated Fair Value |
| Fixed-rate debt | \$564,506 | \$569,344 | \$487,556 | \$488,441 |
| Obligations under capital leases | 14,843 | 15,044 | 14,965 | 15,150 |
| Floating-rate debt | 349,769 | 349,769 | 346,077 | 346,077 |
| Total | \$929,118 | \$934,157 | \$848,598 | \$849,668 |

LIFE TIME FITNESS, INC. AND SUBSIDIARIES
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 (Table amounts in thousands, except share and per share data)

9. Changes in Accumulated Other Comprehensive Income by Component

The following table presents information about accumulated other comprehensive income (loss) by component (net of tax):

| | Gains (Losses) on Cash Flows Hedge | Foreign Currency Translation Adjustments | Accumulated Other Comprehensive Loss |
|-----------------------------------|---------------------------------------|--|--|
| Balance at December 31, 2013 | \$(2,257 |) \$(3,358 |) \$(5,615 |
| Other comprehensive income (loss) | 215 | (884 |) (669 |