

Fiesta Restaurant Group, Inc.  
Form 10-Q  
November 05, 2013  
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UNITED STATES  
SECURITIES AND EXCHANGE COMMISSION  
WASHINGTON, DC 20549

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FORM 10-Q

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

For the quarterly period ended September 29, 2013  
OR

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

Commission File Number: 001-35373

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FIESTA RESTAURANT GROUP, INC.  
(Exact name of Registrant as specified in its charter)

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Delaware	90-0712224
(State or other jurisdiction of incorporation or organization)	(I.R.S. Employer Identification No.)
14800 Landmark Boulevard, Suite 500 Addison, Texas	75254
(Address of principal executive office)	(Zip Code)

Registrant's telephone number, including area code: (972) 702-9300

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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 ý No ..

Indicate by check mark whether the registrant has submitted electronically and posted on their Corporate Web site, if any, every Interactive Data File required to be submitted and posted pursuant to Rule 405 of Regulation S-T during the preceding 12 months (or for such shorter period that the registrant was required to submit and post such files). Yes ý 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 the definitions of "large accelerated filer", "accelerated filer" and "smaller reporting company" in Rule 12b-2 of the Exchange Act. (Check one):

Large accelerated filer .. Accelerated filer ý

Non-accelerated filer .. Smaller reporting company ..  
(Do not check if smaller reporting company)

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

As of October 31, 2013, Fiesta Restaurant Group, Inc. had 23,638,885 shares of its common stock, \$.01 par value, outstanding.

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 CONDENSED CONSOLIDATED FINANCIAL STATEMENTS  
 QUARTER ENDED SEPTEMBER 29, 2013

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## PART I—FINANCIAL INFORMATION

## ITEM 1—INTERIM CONDENSED CONSOLIDATED FINANCIAL STATEMENTS

## FIESTA RESTAURANT GROUP, INC.

## CONDENSED CONSOLIDATED BALANCE SHEETS

(In thousands of dollars, except share and per share amounts)

(unaudited)

	September 29, 2013	December 30, 2012
<b>ASSETS</b>		
Current assets:		
Cash	\$5,886	\$15,533
Trade receivables	6,997	5,935
Inventories	2,457	2,750
Prepaid rent	2,388	2,094
Prepaid expenses and other current assets	4,617	2,596
Deferred income taxes	2,424	2,049
Total current assets	24,769	30,957
Property and equipment, net	144,407	126,516
Goodwill	123,484	123,484
Intangible assets, net	141	202
Deferred income taxes	12,642	13,101
Deferred financing costs, net	4,511	5,690
Other assets	3,308	3,779
Total assets	\$313,262	\$303,729
<b>LIABILITIES AND STOCKHOLDERS' EQUITY</b>		
Current liabilities:		
Current portion of long-term debt	\$56	\$60
Accounts payable	8,966	10,411
Accrued interest	2,303	6,761
Accrued payroll, related taxes and benefits	12,871	14,719
Accrued real estate taxes	4,648	3,366
Other liabilities	5,968	5,961
Total current liabilities	34,812	41,278
Long-term debt, net of current portion	200,847	200,889
Lease financing obligations (Note 5)	3,035	3,029
Deferred income—sale-leaseback of real estate	34,696	36,096
Other liabilities (Note 3)	11,957	11,933
Total liabilities	285,347	293,225
Commitments and contingencies (Note 10)		
Stockholders' equity:		
Common stock, par value \$.01; authorized 100,000,000 shares; issued 23,643,983 and 23,514,437 shares, respectively, and outstanding 22,999,917 and 22,748,241 shares, respectively	230	227
Additional paid-in capital	12,852	10,254
Retained earnings	14,833	23
Total stockholders' equity	27,915	10,504
Total liabilities and stockholders' equity	\$313,262	\$303,729

The accompanying notes are an integral part of these condensed consolidated unaudited financial statements.

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## FIESTA RESTAURANT GROUP, INC.

## CONDENSED CONSOLIDATED STATEMENTS OF OPERATIONS

THREE AND NINE MONTHS ENDED SEPTEMBER 29, 2013 AND SEPTEMBER 30, 2012

(In thousands of dollars, except share and per share amounts)

(Unaudited)

	Three Months Ended		Nine Months Ended	
	September 29, 2013	September 30, 2012	September 29, 2013	September 30, 2012
Revenues:				
Restaurant sales	\$ 140,069	\$ 127,648	\$ 413,435	\$ 381,422
Franchise royalty revenues and fees	609	525	1,747	1,726
Total revenues	140,678	128,173	415,182	383,148
Costs and expenses:				
Cost of sales	45,162	41,021	132,891	123,106
Restaurant wages and related expenses (including stock-based compensation expense of \$1, \$1, \$2 and \$9, respectively)	36,979	33,860	107,914	101,821
Restaurant rent expense	6,853	6,224	19,699	15,421
Other restaurant operating expenses	18,283	16,529	51,786	48,119
Advertising expense	4,271	3,757	13,275	11,923
General and administrative (including stock-based compensation expense of \$657, \$379, \$1,677 and \$1,594, respectively)	11,685	11,198	35,895	32,800
Depreciation and amortization	5,129	4,486	15,117	13,703
Pre-opening costs	590	232	2,379	1,056
Impairment and other lease charges (Note 2)	(312)	(45)	239	6,816
Other income	(57)	—	(554)	—
Total operating expenses	128,583	117,262	378,641	354,765
Income from operations	12,095	10,911	36,541	28,383
Interest expense	4,457	5,036	14,475	19,334
Income before income taxes	7,638	5,875	22,066	9,049
Provision for income taxes (Note 6)	2,596	2,226	7,256	3,344
Net income	\$ 5,042	\$ 3,649	\$ 14,810	\$ 5,705
Basic and diluted net income per share	\$ 0.21	\$ 0.16	\$ 0.63	\$ 0.25
Basic and diluted weighted average common shares outstanding (Note 9)	22,986,615	22,747,044	22,921,233	22,937,270

The accompanying notes are an integral part of these condensed consolidated unaudited financial statements.

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## FIESTA RESTAURANT GROUP, INC.

CONDENSED CONSOLIDATED STATEMENTS OF CHANGES IN STOCKHOLDERS' EQUITY  
NINE MONTHS ENDED SEPTEMBER 29, 2013 AND SEPTEMBER 30, 2012

(In thousands of dollars, except share amounts)

(Unaudited)

	Number of Common Stock Shares	Common Stock	Additional Paid-In Capital	Retained Earnings (Deficit)	Total Stockholders' Equity
Balance at January 1, 2012	23,161,822	\$ 227	\$ 3,345	\$ (8,244	) \$ (4,672 )
Capital contributions	—	—	4,154	—	4,154
Stock-based compensation	—	—	1,400	—	1,400
Issuance of non-vested shares at spin-off	(434,397	) —	—	—	—
Vesting of restricted shares	20,799	—	—	—	—
Net income	—	—	—	5,705	5,705
Balance at September 30, 2012	22,748,224	\$ 227	\$ 8,899	\$ (2,539	) \$ 6,587
Balance at December 30, 2012	22,748,241	\$ 227	\$ 10,254	\$ 23	\$ 10,504
Capital contributions	—	—	96	—	96
Stock-based compensation	—	—	1,679	—	1,679
Vesting of restricted shares and related tax benefit	251,676	3	823	—	826
Net income	—	—	—	14,810	14,810
Balance at September 29, 2013	22,999,917	\$ 230	\$ 12,852	\$ 14,833	\$ 27,915

The accompanying notes are an integral part of these condensed consolidated unaudited financial statements.

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FIESTA RESTAURANT GROUP, INC.  
 CONDENSED CONSOLIDATED STATEMENTS OF CASH FLOWS  
 NINE MONTHS ENDED SEPTEMBER 29, 2013 AND SEPTEMBER 30, 2012  
 (In thousands of dollars)  
 (Unaudited)

	Nine Months Ended	
	September 29, 2013	September 30, 2012
Cash flows from operating activities:		
Net income	\$14,810	\$ 5,705
Adjustments to reconcile net income to net cash provided by operating activities:		
Loss (gain) on disposals of property and equipment	(261	) 101
Stock-based compensation	1,679	1,401
Impairment and other lease charges	239	6,816
Loss on settlement of lease financing obligations	—	120
Depreciation and amortization	15,117	13,703
Amortization of deferred financing costs	1,194	1,234
Amortization of deferred gains from sale-leaseback transactions	(2,588	) (1,493
Accretion of interest on lease financing obligations	6	220
Deferred income taxes	34	(1,221
Changes in other operating assets and liabilities	(9,921	) (5,308
Net cash provided by operating activities	20,309	21,278
Cash flows from investing activities:		
Capital expenditures:		
New restaurant development	(28,442	) (16,790
Restaurant remodeling	(2,602	) (5,931
Other restaurant capital expenditures	(4,152	) (5,300
Corporate and restaurant information systems	(3,595	) (849
Total capital expenditures	(38,791	) (28,870
Properties purchased for sale-leaseback	(4,438	) (2,082
Proceeds from sale-leaseback transactions	10,774	1,491
Proceeds from sales of other properties	1,734	934
Net cash used in investing activities	(30,721	) (28,527
Cash flows from financing activities:		
Borrowings from Carrols Restaurant Group, Inc., net	—	500
Capital contribution from Carrols Restaurant Group, Inc.	—	2,500
Excess tax benefit from vesting of restricted shares	826	—
Borrowings on revolving credit facility	—	2,100
Repayments on revolving credit facility	—	(2,100
Principal payments on capital leases	(46	) (45
Deferred financing costs	—	(231
Settlement of lease financing obligations	—	(6,047
Other	(15	) —
Net cash provided by (used in) financing activities	765	(3,323
Net decrease in cash	(9,647	) (10,572
Cash, beginning of period	15,533	13,670
Cash, end of period	\$5,886	\$ 3,098
Supplemental disclosures:		
Interest paid on long-term debt	\$18,172	\$ 18,668

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Interest paid on lease financing obligations	\$191	\$ 4,143
Accruals for capital expenditures	\$2,123	\$ 579
Income tax payments, net	\$7,106	\$ 2,601
Non-cash reduction of lease financing obligations	\$—	\$ 114,165
Non-cash reduction of assets subject to lease financing obligations	\$—	\$ 80,419
Non-cash capital contribution from former parent	\$96	\$ 1,654

The accompanying notes are an integral part of these condensed consolidated unaudited financial statements.

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FIESTA RESTAURANT GROUP, INC.

NOTES TO UNAUDITED CONDENSED CONSOLIDATED FINANCIAL STATEMENTS

(In thousands of dollars, except share and per share amounts)

1. Basis of Presentation

**Business Description.** Fiesta Restaurant Group, Inc. ("Fiesta Restaurant Group" or "Fiesta") owns, operates and franchises two fast-casual restaurant brands through its wholly-owned subsidiaries Pollo Operations, Inc., and its subsidiaries, and Pollo Franchise, Inc., (collectively "Pollo Tropical") and Taco Cabana, Inc. and its subsidiaries (collectively "Taco Cabana"). Unless the context otherwise requires, Fiesta and its subsidiaries, Pollo Tropical and Taco Cabana, are collectively referred to as the "Company". At September 29, 2013, Fiesta operated 100 Pollo Tropical® restaurants, of which 94 were located in Florida, four were located in Georgia and two were located in Tennessee, and franchised a total of 38 Pollo Tropical restaurants, including 18 in Puerto Rico, one in Ecuador, two in Honduras, one in the Bahamas, two in Trinidad & Tobago, three in Venezuela, three in Costa Rica, two in Panama, one in the Dominican Republic, one in India and four on college campuses in Florida. At September 29, 2013, the Company also owned and operated 164 Taco Cabana® restaurants, of which 161 were located in Texas and three were located in Oklahoma, and franchised a total of eight Taco Cabana restaurants, including four in New Mexico, one in Georgia and three non-traditional locations (two college campuses and one sports arena) in Texas.

**Spin-Off from Carrols Restaurant Group, Inc.** On May 7, 2012, Carrols Restaurant Group, Inc. ("Carrols Restaurant Group" or "Carrols") completed the spin-off of Fiesta through the distribution of all of the outstanding shares of Fiesta Restaurant Group's common stock to the stockholders of Carrols Restaurant Group (the "Spin-off"). As a result of the Spin-off, Fiesta Restaurant Group is now an independent public company whose common stock is traded on The NASDAQ Global Select Market under the symbol "FRGI."

In connection with the Spin-off, Fiesta and Carrols entered into several agreements that govern Carrols' post Spin-off relationship with Fiesta, including a Separation and Distribution Agreement, Employee Matters Agreement, Tax Matters Agreement and Transition Services Agreement ("TSA"). See Note 4—Former Related Party Transactions.

**Basis of Consolidation.** The unaudited condensed consolidated financial statements presented herein reflect the consolidated financial position, results of operations and cash flows of Fiesta and its wholly-owned subsidiaries. The condensed consolidated financial statements have been prepared as if the Company was in existence for all periods presented.

Through the date of the Spin-off, these unaudited condensed consolidated financial statements have been prepared on a stand-alone basis from the separate records maintained by Carrols and may not necessarily be indicative of the results of operations or cash flows that would have resulted had allocations and other related-party transactions been consummated with unrelated parties or had the Company been an independent, publicly traded company during all of the periods presented. The unaudited interim condensed consolidated financial statements reflect the historical financial position, results of operations and cash flows of the Company as it has historically operated, in conformity with U.S. Generally Accepted Accounting Principles ("GAAP"). All intercompany transactions have been eliminated in consolidation.

In connection with the Spin-off, the board of directors of the Company authorized a 23,161.8 for one split of its outstanding common stock that was effective on April 19, 2012. Accordingly, all references to share and per share amounts related to common stock included in the unaudited condensed consolidated financial statements and accompanying notes have been adjusted to reflect the stock split and change in the number of authorized shares. The stock split has been retroactively applied to the Company's financial statements.

**Fiscal Year.** The Company uses a 52-53 week fiscal year ending on the Sunday closest to December 31. The fiscal year ended December 30, 2012 contained 52 weeks. The three and nine months ended September 29, 2013 and September 30, 2012 each contained thirteen and thirty-nine weeks, respectively.

**Basis of Presentation.** The accompanying unaudited condensed consolidated financial statements for the three and nine months ended September 29, 2013 and September 30, 2012 have been prepared without an audit pursuant to the rules and regulations of the Securities Exchange Commission and do not include certain information and footnotes

required by GAAP for complete financial statements. In the opinion of management, all normal and recurring adjustments considered necessary for a fair presentation of such financial statements have been included. The results of operations for the three and nine months ended September 29, 2013 and September 30, 2012 are not necessarily indicative of the results to be expected for the full year.

These unaudited condensed consolidated financial statements should be read in conjunction with the consolidated financial statements and notes thereto for the year ended December 30, 2012 included in the Company's 2012 Annual Report on Form 10-K. The December 30, 2012 balance sheet data is derived from those audited financial statements.

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FIESTA RESTAURANT GROUP, INC.

NOTES TO UNAUDITED CONDENSED CONSOLIDATED FINANCIAL STATEMENTS—(Continued)

(In thousands of dollars, except share and per share amounts)

Allocations. Through the date of the Spin-off, Carrols provided administrative support to the Company for executive management, information systems and certain accounting, legal and other administrative functions. The cost of these services were allocated to the Company based primarily on a pro-rata share of either the Company's revenues, number of restaurants or number of employees. The allocations may not reflect the expenses the Company would have incurred as an independent, publicly traded company for the periods presented. Following the Spin-off, certain of these functions continue to be provided by Carrols under the TSA, and the Company is performing certain functions using its own resources or purchased services from third parties. Refer to Note 4—Former Related Party Transactions for further discussion related to agreements entered into effective as of the Spin-off.

Management believes that its allocations are reasonable and based on a systematic and rational method; however, they are not necessarily indicative of the actual financial results of the Company, including such expenses that would have been incurred by the Company had it been operating as a separate, stand-alone entity for the periods presented. As a stand-alone entity, the Company expects to incur expenses that may not be comparable in future periods to what is presented for the historical periods presented in the condensed consolidated financial statements. Consequently, the financial information herein may not reflect the financial position, results of operations and cash flows of the Company in the future or if the Company had been an independent stand-alone entity during all periods presented. In our opinion, the condensed consolidated financial statements include all adjustments necessary for a fair presentation of its results of operations.

Fair Value of Financial Instruments. Fair value is defined as the price that would be received to sell an asset or paid to transfer a liability in an orderly transaction between market participants on the measurement date. In determining fair value, the accounting standards establish a three level hierarchy for inputs used in measuring fair value as follows: Level 1 inputs are quoted prices in active markets for identical assets or liabilities; Level 2 inputs are observable for the asset or liability, either directly or indirectly, including quoted prices in active markets for similar assets or liabilities; and Level 3 inputs are unobservable and reflect our own assumptions. The following methods were used to estimate the fair value of each class of financial instruments for which it is practicable to estimate the fair value:

• Current Assets and Liabilities. The carrying values reported on the balance sheet of cash, accounts receivable and accounts payable approximate fair value because of the short maturity of those financial instruments.

• Senior Secured Second Lien Notes. The fair value of outstanding senior secured second lien notes, which was approximately \$212.5 million at September 29, 2013, is based on recent trading values, which are considered Level 1. The senior secured second lien notes are recorded in Long-term debt, net of current portion and had a carrying value of \$200.0 million at September 29, 2013.

See Note 2 for discussion of the fair value measurement of non-financial assets.

Use of Estimates. The preparation of the condensed consolidated financial statements in conformity with GAAP requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities and disclosure of contingent assets and liabilities at the dates of the financial statements. Estimates also affect the reported amounts of expenses during the reporting periods. Significant items subject to such estimates and assumptions include: allocations of Carrols' general and administrative expenses and interest expense on amounts due to Carrols prior to the Spin-off, accrued occupancy costs, insurance liabilities, evaluation for impairment of goodwill and long-lived assets and lease accounting matters. Actual results could differ from those estimates.

Reclassifications. Certain amounts have been reclassified from Restaurant rent expense, Advertising expense and Other restaurant operating expenses to Pre-opening costs in order to conform to the current year presentation.

## 2. Impairment of Long-Lived Assets and Other Lease Charges

The Company reviews its long-lived assets, principally property and equipment, for impairment at the restaurant level. If an indicator of impairment exists for any of its assets, an estimate of undiscounted future cash flows over the life of the primary asset for each restaurant is compared to that long-lived asset's carrying value. If the carrying value is

greater than the undiscounted cash flow, the Company then determines the fair value of the asset and if an asset is determined to be impaired, the loss is measured by the excess of the carrying amount of the asset over its fair value. For closed restaurant locations, the Company reviews the future minimum lease payments and related ancillary costs from the date of the restaurant closure to the end of the remaining lease term and records a lease charge for the lease liabilities to be incurred, net of any estimated sublease recoveries.

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FIESTA RESTAURANT GROUP, INC.

NOTES TO UNAUDITED CONDENSED CONSOLIDATED FINANCIAL STATEMENTS—(Continued)

(In thousands of dollars, except share and per share amounts)

The Company determined the fair value of restaurant equipment, for those restaurants reviewed for impairment, based on current economic conditions and the Company's history of using these assets in the operation of its business. For those restaurants reviewed for impairment where the Company owns the land and building, the Company also utilized third-party information such as a broker market price opinion to determine the fair value of the property. These fair value asset measurements rely on significant unobservable inputs and are considered Level 3 in the fair value hierarchy. The Level 3 assets measured at fair value associated with impairment charges recorded during the nine months ended September 29, 2013 totaled less than \$0.1 million.

Impairment of long-lived assets for the Company's segments and other lease charges recorded were as follows:

	Three Months Ended		Nine Months Ended	
	September 29,	September 30,	September 29,	September 30,
	2013	2012	2013	2012
Pollo Tropical	\$(37	) \$94	\$(99	) \$ 5,931
Taco Cabana	(275	) (139	) 338	885
	\$(312	) \$(45	) \$239	\$ 6,816

During the three and nine months ended September 29, 2013, the Company recorded lease charge recoveries, net of other lease charges, of \$(0.3) million and \$(0.2) million, respectively, related to previously closed locations. The Company also recorded an impairment charge of \$0.4 million related to a Taco Cabana restaurant during the nine months ended September 29, 2013.

During the nine months ended September 30, 2012, the Company recorded other lease charges, net of recoveries, of \$1.5 million and impairment charges of \$4.1 million associated with the closure of the Company's five Pollo Tropical restaurants in New Jersey in the first quarter of 2012. The Company also recorded an impairment charge of \$0.5 million related to a Pollo Tropical restaurant and \$1.0 million related to two Taco Cabana restaurants and a recovery of other lease charges of \$(0.2) million related to a non-operating Pollo Tropical restaurant during the nine months ended September 30, 2012.

### 3. Other Liabilities, Long-Term

Other liabilities, long-term, consisted of the following:

	September 29, 2013	December 30, 2012
Accrued occupancy costs	\$9,288	\$8,493
Accrued workers' compensation and general liability claims	935	1,270
Deferred compensation	487	812
Other	1,247	1,358
	\$11,957	\$11,933

Accrued occupancy costs include obligations pertaining to closed restaurant locations and accruals to expense operating lease rental payments on a straight-line basis over the lease term.

The following table presents the activity in the closed-store reserve, of which \$1.2 million and \$1.7 million are included in long-term accrued occupancy costs above at September 29, 2013 and December 30, 2012, respectively, with the remainder in other current liabilities:

	Nine Months Ended September 29, 2013	Year Ended December 30, 2012
Balance, beginning of period	\$2,432	\$2,246
Provisions for restaurant closures	—	1,796
Recoveries, net of additional lease charges	(158	) (377
Payments, net	(834	) (1,496

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Other adjustments	105	263
Balance, end of period	\$1,545	\$2,432

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FIESTA RESTAURANT GROUP, INC.

NOTES TO UNAUDITED CONDENSED CONSOLIDATED FINANCIAL STATEMENTS—(Continued)

(In thousands of dollars, except share and per share amounts)

4. Former Related Party Transactions

Effective upon the completion of the Spin-off, Fiesta Restaurant Group ceased to be a related party of Carrols.

Prior to the date of the Spin-off, the Company's expenses included allocations from Carrols of costs associated with administrative support functions which included executive management, information systems, finance, legal, accounting, internal audit and human resources and certain other administrative functions. The Company's allocated administrative expenses from Carrols were \$4.2 million for the pre-spin period in 2012.

As discussed in Note 1, the Company believes the assumptions and methodologies underlying the allocation of administrative expenses are reasonable. However, such expenses may not be indicative of the actual expenses that would have been or will be incurred by the Company now that it is operating as a stand-alone company. As such, the financial information herein may not necessarily reflect the consolidated financial position, results of operations, and cash flows of the Company in the future or if the Company had been a stand-alone entity during the periods presented. In the first quarter of 2012, Carrols made a capital contribution in cash to the Company of \$2.5 million. The capital contribution in cash was a portion of the excess cash proceeds from debt financings completed in August 2011. In 2012, and prior to the Spin-off, Carrols made non-cash contributions of \$1.7 million to the Company, which related to the transfer of income tax-related assets and liabilities. In 2013, Carrols made additional non-cash contributions of \$0.1 million to the Company, which also related to the transfer of income tax-related assets and liabilities for periods prior to the Spin-off.

As of September 29, 2013 and December 30, 2012, the Company owed \$0.8 million and \$2.7 million, respectively, to Carrols, which is included in accounts payable in the accompanying condensed consolidated balance sheets.

All intercompany transactions between the Company and Carrols prior to the Spin-off were included in the Company's historical financial statements and were considered to be effectively settled at the time of the Spin-off.

Relationship Between Fiesta and Carrols After the Spin-Off

For purposes of governing certain of the ongoing relationships between the Company and Carrols at and after the Spin-off, the Company and Carrols have entered into the following agreements:

**Tax Matters Agreement.** The tax matters agreement dated April 24, 2012, (the "Tax Matters Agreement"), (1) governs the allocation of the tax assets and liabilities between Fiesta and Carrols and Carrols Corporation, a subsidiary of Carrols ("Carrols Corp."), (2) provides for certain restrictions and indemnities in connection with the tax treatment of the Spin-off and (3) addresses certain other tax related matters, including, without limitation, those relating to (a) the obligations of Carrols, Carrols Corp. and the Company with respect to the preparation or filing of tax returns for all periods, and (b) the control of any income tax audits and any indemnities with respect thereto. The Tax Matters Agreement provides that if the Company takes any actions after Carrols' distribution of our shares in the Spin-off that result in or cause the distribution to be taxable to Carrols, the Company will be responsible under the Tax Matters Agreement for any resulting taxes imposed on the Company or on Carrols or Carrols Corp. Further, the Tax Matters Agreement provides that the Company will be responsible for 50% of the losses and taxes of Carrols and its affiliates resulting from the Spin-off not attributable to any such action of the Company or an equivalent action by Carrols.

**Transition Services Agreement.** Under the TSA, Carrols and Carrols Corp. agreed to provide certain support services (including accounting, tax accounting, treasury management, internal audit, financial reporting and analysis, human resources and employee benefits management, information systems, restaurant systems support, legal, property management and insurance and risk management services) to the Company, and the Company agreed to provide certain limited management services (including certain legal services) to Carrols and Carrols Corp. The charge for transition services is intended to allow Carrols to recover its direct and indirect costs incurred in providing those services. The TSA became effective upon consummation of the Spin-off and will continue for a period of three years provided that the Company may extend the term of the TSA by one additional year upon 90 days prior written notice to Carrols or may terminate the TSA with respect to any service provided thereunder at any time upon 90 days prior written notice to Carrols. During the three and nine months ended September 29, 2013, the Company recognized

expenses of \$0.3 million and \$2.7 million, respectively, related to the TSA. The Company incurred costs of \$1.5 million and \$2.6 million in the three and nine months ended September 30, 2012 related to the TSA.



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FIESTA RESTAURANT GROUP, INC.

NOTES TO UNAUDITED CONDENSED CONSOLIDATED FINANCIAL STATEMENTS—(Continued)

(In thousands of dollars, except share and per share amounts)

5. Lease Financing Obligations

The Company entered into sale-leaseback transactions in various years that did not qualify for sale-leaseback accounting due to certain forms of continuing involvement and, as a result, the leases were classified as financing transactions in the Company's consolidated financial statements.

Under the financing method, the assets remain on the consolidated balance sheet and the net proceeds received by the Company from these transactions are recorded as a lease financing liability. Payments under these leases are applied as payments of imputed interest and deemed principal on the underlying financing obligations.

These leases generally provide for an initial term of 20 years plus renewal options. The rent payable under such leases includes a minimum rent provision and in some cases, includes rent based on a percentage of sales. These leases also require payment of property taxes, insurance and utilities.

During the second quarter of 2012, the Company exercised its purchase options under the leases for five restaurant properties previously accounted for as lease financing obligations and purchased these properties from the lessor. As a result, the Company reduced its lease financing obligations by \$6.0 million in the second quarter of 2012.

Subsequently, four of the five properties have been sold in qualifying sale-leaseback transactions.

For certain of the Company's historical sale-leaseback transactions, Carrols has guaranteed the lease payments on an unsecured basis or is the primary lessee on the leases associated with certain of the Company's sale-leaseback transactions. Prior to the Spin-off, Accounting Standards Codification 840-40 "Sale-Leaseback Transactions" required the Company to classify these leases as lease financing transactions in the Company's consolidated financial statements because the guarantee from a related party constituted continuing involvement and caused the sale to not qualify for sale-leaseback accounting.

At the time of the Spin-off, these sale-leaseback transactions qualified for sale-leaseback accounting (and the treatment of such related leases as operating leases) due to the cure or elimination of the provisions that previously precluded sale-leaseback accounting in the Company's financial statements. As a result of the qualification for sale-leaseback accounting during the second quarter of 2012, the Company removed the associated lease financing obligations, property and equipment, and deferred financing costs from its balance sheet, and recognized deferred gains on sale-leaseback transactions related to the qualification of \$32.1 million that is being amortized as a reduction of rent expense over the individual remaining lease terms. This resulted in a decrease in lease financing obligations of \$114.2 million, a decrease in assets under lease financing obligations of \$80.4 million, and a decrease of \$1.6 million in deferred financing fees.

The interest rates on the remaining lease financing obligations ranged from 8.6% to 8.8% at September 29, 2013. Interest expense associated with lease financing obligations was \$0.1 million for the three months ended September 29, 2013 and September 30, 2012 and \$0.2 million and \$4.4 million, respectively, for the nine months ended September 29, 2013 and September 30, 2012.

6. Income Taxes

Prior to the Spin-off, the Company's taxable income was included in the consolidated U.S. federal income tax return of Carrols and in income tax returns filed by Carrols on a consolidated basis with certain state taxing jurisdictions. Subsequent to the Spin-off, the Company is responsible for filing its own consolidated U.S. federal and state tax returns. Prior to the Spin-off, the Company determined its provision for income taxes on a separate return basis.

The Tax Matters Agreement governs the methodology for allocating responsibility for federal, state, local and foreign income and other taxes related to taxable periods prior to and subsequent to the Spin-off. Under the Tax Matters Agreement, Carrols is generally responsible for Federal income taxes related to the Company for all periods prior to the date of the Spin-off and the Company is responsible for Federal income taxes for periods after the date of the Spin-off. The Company is also responsible for all state taxes that were filed on a consolidated basis both before and after the date of Spin-off, specifically Florida and Texas, and any other states where the Company was filing or will file separate state tax returns.

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The Company's income tax provision was comprised of the following for the three and nine months ended September 29, 2013 and September 30, 2012:

	Three Months Ended		Nine Months Ended	
	September 29, 2013	September 30, 2012	September 29, 2013	September 30, 2012
Current	\$2,539	\$ 683	\$7,222	\$ 4,565
Deferred	57	1,543	34	(1,221 )
	\$2,596	\$ 2,226	\$7,256	\$ 3,344

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FIESTA RESTAURANT GROUP, INC.

NOTES TO UNAUDITED CONDENSED CONSOLIDATED FINANCIAL STATEMENTS—(Continued)

(In thousands of dollars, except share and per share amounts)

The American Taxpayer Relief Act of 2013 (the "Act") was signed into law on January 2, 2013. The Act included a provision to retroactively restore several expired business tax provisions, including the Work Opportunity Tax Credit, as of January 1, 2012, with a new expiration date of December 31, 2013. Because a change in tax law is accounted for in the period of enactment, and the Act was enacted after Fiesta's fiscal year-end, the retroactive effect of renewing the Work Opportunity Tax Credit was recorded as a discrete item in the first quarter of 2013.

The provision for income taxes for the three and nine months ended September 29, 2013 was derived using an estimated effective annual income tax rate for 2013 of 36.5%, which excludes any discrete tax adjustments. The discrete tax adjustment for the retroactive effect of renewing the Work Opportunity Tax Credit decreased the provision for income taxes by \$0.6 million in the nine months ended September 29, 2013. Other discrete tax adjustments decreased the provision for income taxes by \$0.2 million in the three and nine months ended September 29, 2013.

The provision for income taxes for the three and nine months ended September 30, 2012 was derived using an estimated effective annual income tax rate for 2012 of 39.3%, which excludes any discrete tax adjustments. Discrete tax adjustments increased the provision for income taxes by \$25 thousand for three months ended September 30, 2012 and decreased the provision for income taxes by \$0.2 million in the nine months ended September 30, 2012.

#### 7. Stock-Based Compensation

Prior to the Spin-off, certain of the Company's employees participated in the Carrols Restaurant Group, Inc. 2006 Stock Incentive Plan, as amended (the "Carrols Plan"). In conjunction with the Spin-off, the Company established the Fiesta Restaurant Group, Inc. 2012 Stock Incentive Plan (the "Fiesta Plan") in order to be able to compensate its employees and directors by issuing stock options, stock appreciation rights, or stock awards to them under this plan. For the three and nine months ended September 29, 2013 and the period May 7, 2012 through September 30, 2012, the condensed consolidated statements of operations include expenses related to the Company's employees' and directors' participation in both the Carrols Plan and the Fiesta Plan. For the period from January 2, 2012 through the Spin-off, the condensed consolidated statement of operations includes expenses related to the Company's employees' and directors' participation in the Carrols Plan.

Effective as of the completion of the Spin-off, all holders of Carrols non-vested restricted stock (awarded under the Carrols Plan) on April 26, 2012, the record date of the Spin-off, received one share of Fiesta Restaurant Group non-vested restricted stock for every one share of Carrols non-vested restricted stock held, with terms and conditions substantially similar to the terms and conditions applicable to the Carrols non-vested restricted stock. Future stock compensation expense on all non-vested restricted Carrols and Fiesta stock awards held by the Company's employees will be recorded by the Company.

During the three months ended March 31, 2013, the Company granted in the aggregate 152,703 non-vested restricted shares under the Fiesta Plan to certain employees. These shares vest and become non-forfeitable over a four year vesting period and will be expensed according to the vesting period. The weighted average fair value at the grant date for restricted non-vested shares issued during the three months ended March 31, 2013 was \$20.54. During the three months ended June 30, 2013, the Company granted 8,843 non-vested restricted shares to directors. The weighted average fair value at the grant date was \$35.36. These shares vest and become non-forfeitable over a one year vesting period.

Stock-based compensation expense for the three and nine months ended September 29, 2013 was \$0.7 million and \$1.7 million, respectively. Stock-based compensation expense for the three and nine months ended September 30, 2012 was \$0.4 million and \$1.6 million, respectively, and included \$0.4 million of expense in the nine months ended September 30, 2012 related to the accelerated vesting of the non-vested restricted shares of the former Chairman of the Company's board of directors upon his departure from the Company's board of directors in the first quarter of 2012. As of September 29, 2013, the total unrecognized stock-based compensation expense relating to non-vested

restricted shares was approximately \$6.6 million. At September 29, 2013, the remaining weighted average vesting period for non-vested restricted shares was 2.3 years.

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FIESTA RESTAURANT GROUP, INC.

NOTES TO UNAUDITED CONDENSED CONSOLIDATED FINANCIAL STATEMENTS—(Continued)

(In thousands of dollars, except share and per share amounts)

## Non-vested Shares

A summary of all non-vested restricted share activity for the nine months ended September 29, 2013 was as follows:

	Shares	Weighted Average Grant Date Price
Non-vested at December 30, 2012	766,196	\$ 12.49
Granted	161,546	21.35
Vested	(251,676	) 12.07
Forfeited	(32,000	) 12.98
Non-vested at September 29, 2013	644,066	\$ 14.85

The fair value of the non-vested restricted shares is based on the closing price on the date of grant.

## 8. Business Segment Information

The Company is engaged in the fast-casual restaurant industry, with two restaurant concepts (each of which is an operating segment): Pollo Tropical and Taco Cabana. Pollo Tropical is a fast-casual restaurant brand offering a wide variety of freshly prepared Caribbean inspired food, while our Taco Cabana restaurants offer a broad selection of hand-made, fresh and authentic Mexican food.

The accounting policies of each segment are the same as those described in the summary of significant accounting policies discussed in Note 1. The Company reports more than one measure of segment profit or loss to the chief operating decision maker for the purposes of allocating resources to the segments and assessing their performance. Prior to January 2013, the primary measure of segment profit or loss used to assess performance and allocate resources was Adjusted EBITDA, which is defined as earnings attributable to the applicable operating segment before interest, income taxes, depreciation and amortization, impairment and other lease charges, stock-based compensation expense, other income and expense and gains and losses on extinguishment of debt. Beginning in January 2013, the primary measures of segment profit or loss used to assess performance and allocate resources are income before taxes and Adjusted EBITDA. Although the chief operating decision maker continues to use Adjusted EBITDA as a measure of segment profitability, in accordance with Accounting Standards Codification 280, Segment Reporting, the following table includes segment income before taxes, which is the measure of segment profit or loss determined in accordance with the measurement principles that are most consistent with the principles used in measuring the corresponding amounts in the consolidated financial statements. The Company has included the presentation of income before tax for all periods presented.

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## FIESTA RESTAURANT GROUP, INC.

## NOTES TO UNAUDITED CONDENSED CONSOLIDATED FINANCIAL STATEMENTS—(Continued)

(In thousands of dollars, except share and per share amounts)

The “Other” column includes corporate related items not allocated to reportable segments and consists primarily of corporate owned property and equipment and capitalized costs associated with the issuance of indebtedness.

Three Months Ended	Pollo Tropical	Taco Cabana	Other	Consolidated
September 29, 2013:				
Restaurant sales	\$65,994	\$74,075	\$—	\$140,069
Franchise revenue	484	125	—	609
Cost of sales	21,960	23,202	—	45,162
Restaurant wages and related expenses <sup>(1)</sup>	14,966	22,013	—	36,979
Restaurant rent expense	2,625	4,228	—	6,853
Other restaurant operating expenses	8,236	10,047	—	18,283
Advertising expense	1,710	2,561	—	4,271
General and administrative expense <sup>(2)</sup>	6,106	5,579	—	11,685
Depreciation and amortization	2,367	2,762	—	5,129
Pre-opening costs	476	114	—	590
Impairment and other lease charges	(37	) (275	) —	(312
Interest expense	1,937	2,520	—	4,457
Income before taxes	6,132	1,506	—	7,638
Capital expenditures	6,832	2,892	1,298	11,022
September 30, 2012:				
Restaurant sales	\$57,354	\$70,294	\$—	\$127,648
Franchise revenue	430	95	—	525
Cost of sales	18,998	22,023	—	41,021
Restaurant wages and related expenses <sup>(1)</sup>	13,254	20,606	—	33,860
Restaurant rent expense	2,298	3,926	—	6,224
Other restaurant operating expenses	6,893	9,636	—	16,529
Advertising expense	1,846	1,911	—	3,757
General and administrative expense <sup>(2)</sup>	5,550	5,648	—	11,198
Depreciation and amortization	2,008	2,473	5	4,486
Pre-opening costs	48	184	—	232
Impairment and other lease charges	94	(139	) —	(45
Interest expense	2,274	2,762	—	5,036
Income before taxes	4,523	1,357	(5	) 5,875
Capital expenditures	4,149	7,045	252	11,446

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## FIESTA RESTAURANT GROUP, INC.

## NOTES TO UNAUDITED CONDENSED CONSOLIDATED FINANCIAL STATEMENTS—(Continued)

(In thousands of dollars, except share and per share amounts)

Nine Months Ended	Pollo Tropical	Taco Cabana	Other	Consolidated
September 29, 2013:				
Restaurant sales	\$ 192,372	\$ 221,063	\$—	\$ 413,435
Franchise revenue	1,380	367	—	1,747
Cost of sales	63,803	69,088	—	132,891
Restaurant wages and related expenses <sup>(1)</sup>	43,466	64,448	—	107,914
Restaurant rent expense	7,220	12,479	—	19,699
Other restaurant operating expenses	22,849	28,937	—	51,786
Advertising expense	4,432	8,843	—	13,275
General and administrative expense <sup>(2)</sup>	18,573	17,322	—	35,895
Depreciation and amortization	6,780	8,337	—	15,117
Pre-opening costs	1,706	673	—	2,379
Impairment and other lease charges	(99	) 338	—	239
Interest expense	6,436	8,039	—	14,475
Income before taxes	19,083	2,983	—	22,066
Capital expenditures	21,527	13,985	3,279	38,791
September 30, 2012:				
Restaurant sales	\$ 171,327	\$ 210,095	\$—	\$ 381,422
Franchise revenue	1,481	245	—	1,726
Cost of sales	56,895	66,211	—	123,106
Restaurant wages and related expenses <sup>(1)</sup>	39,745	62,076	—	101,821
Restaurant rent expense	5,386	10,035	—	15,421
Other restaurant operating expenses	20,234	27,885	—	48,119
Advertising expense	3,963	7,960	—	11,923
General and administrative expense <sup>(2)</sup>	15,852	16,948	—	32,800
Depreciation and amortization	6,191	7,507	5	13,703
Pre-opening costs	735	321	—	1,056
Impairment and other lease charges	5,931	885	—	6,816
Interest expense	8,249	11,085	—	19,334
Income (loss) before taxes	9,626	(572	) (5	) 9,049
Capital expenditures	13,409	15,034	427	28,870
Identifiable Assets:				
September 29, 2013:	\$ 139,505	\$ 162,393	\$ 11,364	\$ 313,262
December 30, 2012	128,593	167,348	7,788	303,729

(1) Includes stock-based compensation expense of \$1 and \$2 for the three and nine months ended September 29, 2013, respectively, and \$1 and \$9 for the three and nine months ended September 30, 2012, respectively.

(2) Includes stock-based compensation expense of \$657 and \$1,677 for the three and nine months ended September 29, 2013, respectively, and \$379 and \$1,594 for the three and nine months ended September 30, 2012, respectively.

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FIESTA RESTAURANT GROUP, INC.

NOTES TO UNAUDITED CONDENSED CONSOLIDATED FINANCIAL STATEMENTS—(Continued)

(In thousands of dollars, except share and per share amounts)

## 9. Net Income per Share

We compute basic net income per share by dividing net income applicable to common shares by the weighted average number of common shares outstanding during each period. Our non-vested restricted shares contain a non-forfeitable right to receive dividends on a one-to-one per share ratio to common shares and are thus considered participating securities. The impact of the participating securities is included in the computation of basic net income per share pursuant to the two-class method. The two-class method of computing earnings per share is an earnings allocation formula that determines earnings attributable to common shares and participating securities according to dividends declared (whether paid or unpaid) and participation rights in undistributed earnings. Net income per common share was computed by dividing undistributed earnings allocated to common shareholders by the weighted average number of common shares outstanding for the period. In applying the two-class method, undistributed earnings are allocated to both common shares and non-vested restricted shares based on the weighted average shares outstanding during the period.

For 2012, in determining the weighted average number of shares outstanding for basic net income per share, the 23.2 million shares distributed from Carrols on May 7, 2012 were assumed to be outstanding for the period from January 2, 2012 through May 7, 2012.

The computation of basic and diluted net income per share for the three and nine months ended September 29, 2013 and September 30, 2012 is as follows:

	Three Months Ended		Nine Months Ended	
	September 29, 2013	September 30, 2012	September 29, 2013	September 30, 2012
Basic and diluted net income per share:				
Net income	\$5,042	\$ 3,649	\$14,810	\$ 5,705
Less: income allocated to participating securities	(140 )	(82 )	(451 )	(96 )
Net income available to common stockholders	\$4,902	\$ 3,567	\$14,359	\$ 5,609
Basic and diluted weighted average common shares outstanding	22,986,615	22,747,044	22,921,233	22,937,270
Basic and diluted net income per share	\$0.21	\$ 0.16	\$0.63	\$ 0.25

## 10. Commitments and Contingencies

The Company is a party to various litigation matters incidental to the conduct of business. The Company does not believe that the outcome of any of these matters will have a material effect on its consolidated financial statements.



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ITEM 2-MANAGEMENT'S DISCUSSION AND ANALYSIS OF FINANCIAL CONDITION AND RESULTS OF OPERATIONS

Throughout this Management's Discussion and Analysis of Financial Condition and Results of Operations ("MD&A"), we refer to Fiesta Restaurant Group, Inc. as "Fiesta Restaurant Group" or "Fiesta" and, together with its consolidated subsidiaries, as "we," "our" and "us" unless otherwise indicated or the context otherwise requires. Any reference to "Carrols Restaurant Group" refers to Carrols Restaurant Group, Inc., a Delaware corporation and our former indirect parent company, and its consolidated subsidiaries (other than Fiesta Restaurant Group and its subsidiaries after the distribution date, as defined below), unless otherwise indicated or the context otherwise requires. Any reference to "Carrols" refers to Carrols Corporation, a Delaware corporation and our former direct parent company prior to the Spin-off, as defined below, and its consolidated subsidiaries (other than Fiesta Restaurant Group and its subsidiaries after the distribution date), unless otherwise indicated or the context otherwise requires. Any reference to "Carrols LLC" refers to Carrols' direct subsidiary, Carrols LLC, a Delaware limited liability company, unless otherwise indicated or the context otherwise requires.

The following MD&A is written to help the reader understand our company. The MD&A is provided as a supplement to, and should be read in conjunction with our Unaudited Condensed Consolidated Financial Statements and the accompanying financial statement notes appearing elsewhere in this report.

On May 7, 2012 (the "distribution date"), Carrols Restaurant Group completed the spin-off of Fiesta through the distribution of all of the outstanding shares of Fiesta Restaurant Group's common stock to the stockholders of Carrols (the "Spin-off"). As a result of the Spin-off, we are now an independent public company and our common stock is traded on The NASDAQ Global Select Market under the symbol "FRGI."

We use a 52-53 week fiscal year ending on the Sunday closest to December 31. The fiscal year ended December 30, 2012 contained 52 weeks. The three and nine months ended September 29, 2013 and September 30, 2012 each contained thirteen and thirty-nine weeks, respectively.

Company Overview

We own, operate and franchise two fast-casual restaurant brands, Pollo Tropical® and Taco Cabana®, which have over 25 years and 35 years, respectively, of operating history and loyal customer bases. Our Pollo Tropical restaurants offer a wide variety of freshly prepared Caribbean inspired food, while our Taco Cabana restaurants offer a broad selection of hand-made, fresh and authentic Mexican food. We believe that both brands are differentiated from other restaurant concepts and offer a unique dining experience. We are positioned within the value-oriented fast-casual restaurant segment, which combines the convenience and value of quick-service restaurants with the variety, food quality, décor and atmosphere more typical of casual dining restaurants. Our open display kitchen format allows guests to view and experience our food being freshly-prepared and cooked to order. Additionally, nearly all of our restaurants offer the convenience of drive-thru service. As of September 29, 2013, our company-owned restaurants included 100 Pollo Tropical restaurants and 164 Taco Cabana restaurants.

We franchise our Pollo Tropical restaurants primarily internationally and as of September 29, 2013, we had 38 franchised Pollo Tropical restaurants located in Puerto Rico, Ecuador, Honduras, Trinidad & Tobago, the Bahamas, Venezuela, Costa Rica, Panama, the Dominican Republic, India and on college campuses in Florida. We have agreements for the continued development of franchised Pollo Tropical restaurants in the existing markets of Venezuela, North India, Trinidad & Tobago, Honduras, Costa Rica and Panama, and we have agreements to develop new restaurants in the additional markets of Aruba, Curacao, Bonaire and Guatemala. While we are currently not actively franchising our Taco Cabana restaurants beyond non-traditional locations such as airports and universities, we had eight Taco Cabana franchised restaurants as of September 29, 2013, located in Texas, New Mexico and Georgia.

Recent and Future Events Affecting our Results of Operations

Spin-off of Fiesta Restaurant Group, Inc.

On May 7, 2012, Carrols Restaurant Group completed the Spin-off of Fiesta in the form of a pro rata dividend of all of our issued and outstanding common stock to Carrols Restaurant Group's stockholders whereby each holder of Carrols Restaurant Group common stock of record on April 26, 2012 received one share of our common stock for every one

share of Carrols Restaurant Group common stock held.

In connection with the Spin-off, on April 24, 2012, Carrols Restaurant Group and Carrols entered into several agreements with us that govern the transition and Carrols Restaurant Group's post Spin-off relationship with us, including a Separation and Distribution Agreement, Tax Matters Agreement, Employee Matters Agreement and Transition Services Agreement (the "TSA").

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During the three and nine months ended September 29, 2013, we incurred costs of \$0.3 million and \$2.7 million related to the TSA, which became effective on May 7, 2012. We recognized expenses of \$1.5 million and \$2.6 million in the three and nine months ended September 30, 2012 related to the TSA. In October 2013, the Company terminated the TSA with respect to substantially all of the remaining services provided under the TSA with the exception of certain information technology services and other miscellaneous services. We currently expect to terminate the remaining services under the TSA by December 29, 2013.

**Lease Financing Obligations**

For certain of our sale-leaseback transactions, Carrols Restaurant Group has guaranteed the lease payments on an unsecured basis or is the primary lessee on the leases. Prior to the Spin-off, Accounting Standards Codification 840-40 "Sale-Leaseback Transactions" required us to classify these leases as lease financing transactions because the guarantee from a related party constituted continuing involvement and caused the sale to not qualify for sale-leaseback accounting. Under the financing method, the assets remain on our consolidated balance sheet and continue to be depreciated, and the net proceeds received by us from these transactions are recorded as a lease financing liability. Payments under these leases were applied as payments of imputed interest and deemed principal on the underlying financing obligations rather than as rent expense.

Such leases qualified for sale-leaseback accounting upon the Spin-off due to the cure or elimination of certain provisions that previously precluded sale-leaseback accounting (and the treatment of such leases as operating leases) in our consolidated financial statements, primarily the guarantees from Carrols Restaurant Group. As a result of the qualification for sale-leaseback accounting during the second quarter of 2012 due to the Spin-off, such leases were treated as operating leases and we removed the associated lease financing obligations, property and equipment, and deferred financing costs from our balance sheet, and recognized deferred gains on sale-leaseback transactions related to the qualification of \$32.1 million that is being amortized as a reduction of rent expense over the individual remaining lease terms. This resulted in a decrease in lease financing obligations of \$114.2 million, a decrease in assets under lease financing obligations of \$80.4 million, and a decrease of \$1.6 million in deferred financing fees.

Additionally in the second quarter of 2012, we exercised purchase options associated with the leases for five restaurant properties previously accounted for as lease financing obligations and purchased these properties from the lessor. As a result, we reduced our lease financing obligations by \$6.0 million during the second quarter of 2012. Subsequently, four of the five properties have been sold in qualifying sale-leaseback transactions.

As a result of the qualification of these leases discussed above and purchase of the five properties mentioned above, restaurant rent expense was \$2.8 million higher, depreciation expense was \$0.7 million lower and interest expense was \$3.9 million lower in the nine months ended September 29, 2013 compared to the same period in 2012.

**Executive Summary-Consolidated Operating Performance for the Three Months Ended September 29, 2013**  
Our third quarter 2013 results and highlights include the following:

- Net income increased \$1.4 million to \$5.0 million in the third quarter of 2013, or \$0.21 per diluted share, compared to a net income of \$3.6 million, or \$0.16 per diluted share in the third quarter of 2012, primarily due to the net impact of the growth in revenues discussed below.
- Total revenues increased 9.8% in the third quarter of 2013 to \$140.7 million compared to \$128.2 million in the third quarter of 2012, driven primarily by an increase in the number of our company-owned restaurants and an increase in comparable restaurant sales of 6.5% for our Pollo Tropical restaurants and 1.8% for our Taco Cabana restaurants. The growth in comparable restaurant sales resulted primarily from an increase in average check of 3.3% at Pollo Tropical and 1.9% at Taco Cabana and an increase in transactions at Pollo Tropical of 3.2% and a decrease in transactions at Taco Cabana of 0.1%.
- During the third quarter of 2013, we opened four new company-owned Pollo Tropical restaurants.
- Adjusted EBITDA increased \$1.8 million in the third quarter of 2013 to \$17.5 million compared to \$15.7 million in the third quarter of 2012, primarily due to the net impact of the increase in revenues, partially offset by increased

general and administrative expenses as a result of the Spin-off. Adjusted EBITDA is a non-GAAP financial measure of performance. For a discussion of our use of Adjusted EBITDA and a reconciliation to net income, see the heading entitled "Management's Use of Non-GAAP Financial Measures".

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## Results of Operations

Three Months Ended September 29, 2013 Compared to Three Months Ended September 30, 2012

The following table sets forth, for the three months ended September 29, 2013 and September 30, 2012, selected consolidated operating results as a percentage of consolidated restaurant sales:

	Three Months Ended		
	September 29, 2013	September 30, 2012	
Restaurant sales:			
Pollo Tropical	47.1	% 44.9	%
Taco Cabana	52.9	% 55.1	%
Consolidated restaurant sales	100.0	% 100.0	%
Costs and expenses:			
Cost of sales	32.2	% 32.1	%
Restaurant wages and related expenses	26.4	% 26.5	%
Restaurant rent expense	4.9	% 4.9	%
Other restaurant operating expenses	13.1	% 12.9	%
Advertising expense	3.0	% 2.9	%
Pre-opening costs	0.4	% 0.2	%

The following table summarizes the changes in the number and mix of Pollo Tropical and Taco Cabana company-owned and franchised restaurants:

	Pollo Tropical			Taco Cabana			
	Owned	Franchised	Total	Owned	Franchised	Total	
December 30, 2012	91	35	126	160	8	168	
New	2	1	3	2	—	2	
Closed	—	—	—	—	—	—	
March 31, 2013	93	36	129	162	8	170	
New	4	3	7	3	—	3	
Closed	(1	) (1	) (2	) (1	) —	(1	)
June 30, 2013	96	38	134	164	8	172	
New	4	2	6	—	—	—	
Closed	—	(2	) (2	) —	—	—	
September 29, 2013	100	38	138	164	8	172	
January 1, 2012	91	31	122	158	5	163	
New	—	2	2	—	—	—	
Closed	(5	) —	(5	) (1	) —	(1	)
April 1, 2012	86	33	119	157	5	162	
New	3	2	5	1	—	1	
Closed	—	—	—	—	—	—	
July 1, 2012	89	35	124	158	5	163	
New	1	—	1	2	—	2	
Closed	—	—	—	—	—	—	
September 30, 2012	90	35	125	160	5	165	

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Consolidated Revenues. Revenues include restaurant sales, which consist of food and beverage sales, net of discounts, at our company-owned restaurants, and franchise royalty revenues and fees, which represent ongoing royalty payments that are determined based on a percentage of franchisee sales, franchise fees associated with new restaurant openings, and development fees associated with the opening of new franchised restaurants in a given market. Restaurant sales are influenced by new restaurant openings and closures of restaurants, and changes in comparable restaurant sales.

Total revenues increased 9.8% to \$140.7 million in the third quarter of 2013 from \$128.2 million in the third quarter of 2012. Restaurant sales increased 9.7% to \$140.1 million in the third quarter of 2013 from \$127.6 million in the third quarter of 2012. The following table presents the primary drivers of the increase in restaurant sales for both Pollo Tropical and Taco Cabana for the third quarter of 2013 compared to the third quarter of 2012 (in millions):

## Pollo Tropical:

Increase in comparable restaurant sales	\$3.5
Impact of new stores, net of closed stores	5.1
Total increase	\$8.6

## Taco Cabana:

Increase in comparable restaurant sales	\$1.2
Impact of new stores, net of closed stores	2.6
Total increase	\$3.8

Comparable restaurant sales for Pollo Tropical increased 6.5% in the third quarter of 2013. Comparable restaurant sales for Taco Cabana in the third quarter of 2013 increased 1.8%. Restaurants are included in comparable restaurant sales after they have been open for 18 months. Increases in comparable restaurant sales result from an increase in guest traffic and an increase in average check. The increase in average check is primarily driven by menu price increases. For Pollo Tropical, menu price increases drove an increase in restaurant sales of 2.3% in the third quarter of 2013 as compared to the third quarter of 2012. For Taco Cabana, menu price increases drove an increase in restaurant sales of 1.9% in the third quarter of 2013 as compared to the third quarter of 2012.

Franchise revenues increased slightly to \$0.6 million in the third quarter of 2013 from \$0.5 million in the third quarter of 2012.

Operating costs and expenses. Operating costs and expenses include cost of sales, restaurant wages and related expenses, other restaurant expenses and advertising expenses. Cost of sales consists of food, paper and beverage costs including packaging costs, less purchase discounts. Cost of sales is generally influenced by changes in commodity costs, the sales mix of items sold and the effectiveness of our restaurant-level controls to manage food and paper costs. Key commodities, including chicken and beef, are generally purchased under contracts for future periods of up to one year.

Restaurant wages and related expenses include all restaurant management and hourly productive labor costs, employer payroll taxes, restaurant-level bonuses and related benefits. Payroll and related taxes and benefits are subject to inflation, including minimum wage increases and increased costs for health insurance, workers' compensation insurance and state unemployment insurance.

Other restaurant operating expenses include all other restaurant-level operating costs, the major components of which are utilities, repairs and maintenance, real estate taxes and credit card fees.

Advertising expense includes all promotional expenses including television, radio, billboards and other sponsorships and promotional activities.

Pre-opening costs include costs incurred prior to opening a restaurant, including restaurant employee wages and related expenses, travel expenditures, recruiting, training, promotional costs associated with the restaurant opening and rent, including any non-cash rent expense recognized during the construction period. Pre-opening costs are generally incurred beginning four to six months prior to a restaurant opening.

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The following tables present the primary drivers of the changes in the components of restaurant operating margins for Pollo Tropical and Taco Cabana for the third quarter of 2013 compared to the third quarter of 2012. All percentages are stated as a percentage of applicable segment restaurant sales.

## Pollo Tropical:

## Cost of sales:

Higher commodity costs	0.9	%
Menu price increases	(0.8)	)%
Sales mix and waste	0.2	%
Discounts and promotions	(0.2)	)%
Other	0.1	%
Net increase in cost of sales as a percentage of restaurant sales	0.2	%

## Restaurant wages and related expenses:

Impact of higher sales volumes on fixed labor costs	(0.3)	)%
Lower workers' compensation claim costs	(0.3)	)%
Other	0.2	%
Net decrease in restaurant wages and related costs as a percentage of restaurant sales	(0.4)	)%

## Other operating expenses:

Lower utility costs	(0.1)	)%
Higher insurance costs	0.6	%
Net increase in other restaurant operating expenses as a percentage of restaurant sales	0.5	%

## Advertising expense:

Timing of promotions	(0.6)	)%
Net decrease in advertising expense as a percentage of restaurant sales	(0.6)	)%

## Pre-opening expense:

Increase in number of restaurants opened	0.6	%
Net increase in pre-opening expense as a percentage of restaurant sales	0.6	%

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## Taco Cabana:

## Cost of sales:

Higher commodity costs	0.3	%
Menu price increases	(0.6)	)%
Sales mix and waste	0.5	%
Other	(0.2)	)%
Net change in cost of sales as a percentage of restaurant sales	—	%

## Restaurant wages and related expenses:

Impact of higher sales volumes on fixed labor costs	(0.4)	)%
Higher medical and other benefit costs	0.7	%
Other	0.1	%
Net increase in restaurant wages and related costs as a percentage of restaurant sales	0.4	%

## Other operating expenses:

Lower repairs and maintenance costs	(0.1)	)%
Net decrease in other restaurant operating expenses as a percentage of restaurant sales	(0.1)	)%

## Advertising expense:

Timing of promotions	0.8	%
Net increase in advertising expense as a percentage of restaurant sales	0.8	%

## Pre-opening expense:

Decrease in number of restaurants opened	(0.1)	)%
Net decrease in pre-opening expense as a percentage of restaurant sales	(0.1)	)%

Consolidated Restaurant Rent Expense. Restaurant rent expense includes base rent and contingent rent on our leases characterized as operating leases, reduced by amortization of gains on sale-leaseback transactions. Restaurant rent expense, as a percentage of total restaurant sales, was 4.9% in the third quarter of 2013 and 4.9% the third quarter of 2012.

Consolidated General and Administrative Expenses. General and administrative expenses are comprised primarily of (1) salaries and expenses associated with the development and support of our Company and brands and the management oversight of the operation of our restaurants; (2) legal, auditing and other professional fees and stock-based compensation expense; and (3) subsequent to the Spin-off, costs incurred under the TSA for administrative support services.

General and administrative expenses increased to \$11.7 million in the third quarter of 2013 from \$11.2 million in the third quarter of 2012 but, as a percentage of total revenues, decreased to 8.3% compared to 8.7% in the third quarter of 2012. The increase was due primarily to Fiesta management additions and other costs related to the transition to a separate infrastructure.

Adjusted EBITDA. Adjusted EBITDA, which is one of the measures of segment profit or loss used by our chief operating decision maker for purposes of allocating resources to our segments and assessing their performance, is defined as earnings attributable to the applicable segment before interest, income taxes, depreciation and amortization, impairment and other lease charges, stock-based compensation expense and other income and expense. Adjusted EBITDA may not be necessarily comparable to other similarly titled captions of other companies due to differences in methods of calculation. Adjusted EBITDA for each of our segments includes an allocation of general and administrative expenses associated with administrative support for executive management, information systems and certain accounting, legal and other administrative functions. Adjusted EBITDA is a non-GAAP financial measure of performance. For a discussion of our use of Adjusted EBITDA and a reconciliation to net income, see the heading entitled "Management's Use of Non-GAAP Financial Measures".



Adjusted EBITDA for Pollo Tropical increased to \$10.7 million in the third quarter of 2013 from \$9.1 million in the third quarter of 2012 due primarily to the net impact of the increase in revenues, partially offset by an increase in pre-opening costs and insurance costs and an increase in general and administrative expense. Adjusted EBITDA for Taco Cabana increased to \$6.8 million in the third quarter of 2013 from \$6.7 million in the third quarter of 2012 primarily due to the net impact of the increase in revenues and a decrease in general and administrative expense.

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**Depreciation and Amortization.** Depreciation and amortization expense increased to \$5.1 million in the third quarter of 2013 from \$4.5 million in the third quarter of 2012 due primarily to increased depreciation relating to new company-owned restaurant openings.

**Impairment and Other Lease Charges.** Impairment and other lease charges in the third quarter of 2013 consisted of \$0.3 million of lease charge recoveries related to previously closed locations. Impairment and other lease charges for the third quarter of 2012 included an impairment charge of \$0.5 million related to a Pollo Tropical restaurant, offset by recoveries of additional sub-lease income related to two Pollo Tropical restaurants and one Taco Cabana restaurant totaling \$0.6 million.

**Interest Expense.** Interest expense decreased \$0.6 million to \$4.5 million in the third quarter of 2013 from \$5.0 million in the third quarter 2012 primarily due to the year-to-date capitalization of interest in the third quarter of 2013 driven by an increase in new store construction.

**Provision for Income Taxes.** The provision for income taxes for the third quarter of 2013 was derived using an estimated effective annual income tax rate for 2013 of 36.5%, excluding discrete items, while the provision for income taxes for the third quarter of 2012 was derived using an estimated effective annual income tax rate for 2012 of 39.3%, also excluding discrete items. The estimated effective annual income tax rate for 2013 is lower than the effective annual income tax rate estimated in the third quarter of 2012, primarily due to the effect of the Work Opportunity Tax Credit that was renewed in early 2013.

Discrete tax adjustments decreased the provision for income taxes by \$0.2 million in the third quarter of 2013 and increased the provision for income taxes by \$25,000 in the third quarter of 2012.

**Net Income.** As a result of the foregoing, we had net income of \$5.0 million in the third quarter of 2013 compared to net income of \$3.6 million in the third quarter of 2012.

#### Nine Months Ended September 29, 2013 Compared to Nine Months Ended September 30, 2012

The following table sets forth, for the nine months ended September 29, 2013 and September 30, 2012, selected consolidated operating results as a percentage of consolidated restaurant sales:

	Nine Months Ended			
	September 29, 2013		September 30, 2012	
Restaurant sales:				
Pollo Tropical	46.5	%	44.9	%
Taco Cabana	53.5	%	55.1	%
Consolidated restaurant sales	100.0	%	100.0	%
Costs and expenses:				
Cost of sales	32.1	%	32.3	%
Restaurant wages and related expenses	26.1	%	26.7	%
Restaurant rent expense	4.8	%	4.0	%
Other restaurant operating expenses	12.5	%	12.6	%
Advertising expense	3.2	%	3.1	%
Pre-opening costs	0.6	%	0.3	%

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Consolidated Revenues. Total revenues increased 8.4% to \$415.2 million in the nine months ended September 29, 2013 from \$383.1 million in the nine months ended September 30, 2012. Restaurant sales also increased 8.4% to \$413.4 million in the nine months ended September 29, 2013 from \$381.4 million in the nine months ended September 30, 2012. The following table presents the primary drivers of the increase in restaurant sales for both Pollo Tropical and Taco Cabana for the nine months ended September 29, 2013 compared to the nine months ended September 30, 2012 (in millions):

## Pollo Tropical:

Increase in comparable restaurant sales	\$9.1	
Impact of new stores, net of closed stores	12.2	
Other	(0.3	)
Total increase	\$21.0	

## Taco Cabana:

Increase in comparable restaurant sales	\$3.3
Impact of new stores, net of closed stores	7.6
Other	0.1
Total increase	\$11.0

Comparable restaurant sales for Pollo Tropical increased 5.5% in the nine months ended September 29, 2013.

Comparable restaurant sales for Taco Cabana increased 1.6% in the nine months ended September 29, 2013. For Pollo Tropical, menu price increases drove an increase in restaurant sales of 2.3% in the nine months ended September 29, 2013 as compared to the nine months ended September 30, 2012. For Taco Cabana, menu price increases drove an increase in restaurant sales of 2.1% in the nine months ended September 29, 2013 as compared to the nine months ended September 30, 2012.

Franchise revenues were \$1.7 million in the nine months ended September 29, 2013 and September 30, 2012.

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Operating costs and expenses. The following tables present the primary drivers of the changes in the components of restaurant operating margins for Pollo Tropical and Taco Cabana for the nine months ended September 29, 2013 compared to the nine months ended September 30, 2012. All percentages are stated as a percentage of applicable segment restaurant sales.

## Pollo Tropical:

## Cost of sales:

Higher commodity costs	0.8	%
Menu price increases	(0.8)	)%
Sales mix and waste	0.2	%
Discounts and promotions	(0.2)	)%
Net change in cost of sales as a percentage of restaurant sales	—	%

## Restaurant wages and related expenses:

Impact of higher sales volumes on fixed labor costs	(0.2)	)%
Lower workers' compensation claim costs	(0.3)	)%
Lower medical and other benefit costs	(0.1)	)%
Net decrease in restaurant wages and related costs as a percentage of restaurant sales	(0.6)	)%

## Other operating expenses:

Lower utility costs	(0.2)	)%
Lower repairs and maintenance costs	(0.1)	)%
Higher insurance costs	0.3	%
Other	0.1	%
Net increase in other restaurant operating expenses as a percentage of restaurant sales	0.1	%

## Advertising expense:

Net change in advertising expense as a percentage of restaurant sales	—	%
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## Pre-opening expense:

Increase in number of restaurants opened	0.5	%
Net increase in pre-opening expense as a percentage of restaurant sales	0.5	%

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## Taco Cabana:

## Cost of sales:

Higher commodity costs	0.2	%
Menu price increases	(0.5)	)%
Sales mix and waste	0.2	%
Other	(0.1)	)%
Net decrease in cost of sales as a percentage of restaurant sales	(0.2)	)%

## Restaurant wages and related expenses:

Impact of higher sales volumes on fixed labor costs	(0.4)	)%
Higher workers' compensation claim costs	0.1	%
Net decrease in restaurant wages and related costs as a percentage of restaurant sales	(0.3)	)%

## Other operating expenses:

Lower repairs and maintenance costs	(0.3)	)%
Other	0.1	%
Net decrease in other restaurant operating expenses as a percentage of restaurant sales	(0.2)	)%

## Advertising expense:

Timing of promotions	0.2	%
Net increase in advertising expense as a percentage of restaurant sales	0.2	%

## Pre-opening expense:

Increase in number of restaurants opened	0.1	%
Net increase in pre-opening expense as a percentage of restaurant sales	0.1	%

Consolidated Restaurant Rent Expense. Restaurant rent expense, as a percentage of total restaurant sales, increased to 4.8% in the nine months ended September 29, 2013 from 4.0% in the nine months ended September 30, 2012 due primarily to the qualification for sale treatment of the sale-leaseback transactions discussed above which increased rent expense in the nine months ended September 29, 2013 by \$2.8 million compared to the nine months ended September 30, 2012.

Consolidated General and Administrative Expenses. General and administrative expenses increased to \$35.9 million in the nine months ended September 29, 2013 from \$32.8 million in the nine months ended September 30, 2012 and, as a percentage of total revenues, was 8.6% in the nine months ended September 29, 2013 and September 30, 2012. The increase is due primarily to Fiesta management additions and related costs and other costs related to the transition to a separate infrastructure. In addition, general and administrative expenses in the nine months ended September 29, 2013 includes \$0.4 million of expenses associated with the underwritten secondary public equity offering completed in March 2013. General and administrative expenses in the nine months ended September 30, 2012 includes stock-based compensation expense and other costs of \$1.1 million related to the conversion of Carrols Restaurant Group outstanding stock options into either shares of Carrols Restaurant Group common stock or restricted stock in connection with the Spin-off and the acceleration of vesting of restricted stock awards of our former Chairman upon his departure from our board of directors.

Adjusted EBITDA. Adjusted EBITDA, which is one of the measures of segment profit or loss used by our chief operating decision maker for purposes of allocating resources to our segments and assessing their performance, is defined as earnings attributable to the applicable segment before interest, income taxes, depreciation and amortization, impairment and other lease charges, stock-based compensation expense and other income and expense. Adjusted EBITDA may not be necessarily comparable to other similarly titled captions of other companies due to differences in methods of calculation. Adjusted EBITDA for each of our segments includes an allocation of general and

administrative expenses associated with administrative support for executive management, information systems and certain accounting, legal and other administrative functions. Adjusted EBITDA is a non-GAAP financial measure of performance. For a discussion of our use of Adjusted EBITDA and a reconciliation to net income, see the heading entitled "Management's Use of Non-GAAP Financial Measures".

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Adjusted EBITDA for Pollo Tropical increased to \$32.5 million in the nine months ended September 29, 2013 from \$30.7 million in the nine months ended September 30, 2012 due primarily to the net impact of the increase in revenue, offset by an increase in rent expense, insurance costs and pre-opening costs and an increase in general and administrative expense. Adjusted EBITDA for Taco Cabana increased to \$20.5 million in the nine months ended September 29, 2013 from \$19.8 million in the nine months ended September 30, 2012 also primarily due to the net impact of the increase in revenues, partially offset by the increase in rent expense and the increase in general and administrative expense. Adjusted EBITDA for Pollo Tropical and Taco Cabana was negatively impacted by an increase in rent expense of \$1.1 million and \$1.8 million, respectively, in the nine months ended September 29, 2013 compared to the nine months ended September 30, 2012 due to the qualification for sale treatment of sale-leaseback transactions, as discussed above.

**Depreciation and Amortization.** Depreciation and amortization expense increased to \$15.1 million in the nine months ended September 29, 2013 from \$13.7 million in the nine months ended September 30, 2012 due primarily to increased depreciation due to new company-owned restaurant openings, partially offset by the qualification for sale treatment of the sale-leaseback transactions discussed above, which decreased depreciation expense by \$0.7 million in the nine months ended September 29, 2013.

**Impairment and Other Lease Charges.** Impairment and other lease charges in the nine months ended September 29, 2013 consisted of a \$0.4 million impairment charge for a Taco Cabana location and recoveries, net of other lease charges related to previously closed locations of \$0.2 million. Impairment and other lease charges of \$6.8 million in the nine months ended September 30, 2012 consisted of asset impairment charges of \$4.1 million and lease charges, net of recoveries, of \$1.3 million associated with the closure of our five Pollo Tropical restaurants in New Jersey in the first quarter of 2012, a recovery of other lease charges of \$0.2 million related to a non-operating Pollo Tropical restaurant and \$1.0 million of asset impairment charges for two Taco Cabana restaurants and \$0.5 million for one Pollo Tropical restaurant. Two of the five closed Pollo Tropical restaurants' assets were previously impaired in 2011.

**Other Income.** Other income of \$0.6 million in the nine months ended September 29, 2013 consists primarily of the gain on sale of a previously closed location.

**Interest Expense.** Interest expense decreased \$4.9 million to \$14.5 million in the nine months ended September 29, 2013 from \$19.3 million in the nine months ended September 30, 2012 primarily due to the elimination of interest expense of \$3.9 million in the nine months ended September 29, 2013 as a result of the qualification for sale treatment of sale-leaseback transactions and the prospective treatment of payments under the related real property leases as rent, as discussed above and the capitalization of interest driven by the increase in new store construction.

**Provision for Income Taxes.** The provision for income taxes for the nine months ended September 29, 2013 was derived using an estimated effective annual income tax rate for 2013 of 36.5%, excluding discrete items, while the provision for income taxes for the nine months ended September 30, 2012 was derived using an estimated effective annual income tax rate for 2012 of 39.3%, also excluding discrete items. The estimated effective annual income tax rate for 2013 is lower than the effective annual income tax rate estimated in the prior year period, primarily due to the effect of the Work Opportunity Tax Credit that was renewed in early 2013.

Discrete tax adjustments, which include the retroactive effect of renewing the Work Opportunity Tax Credit in 2013, decreased the provision for income taxes by \$0.8 million in the nine months ended September 29, 2013. The American Taxpayer Relief Act of 2013 (the "Act") was signed into law on January 2, 2013. The Act included a provision to retroactively restore several expired business tax provisions, including the Work Opportunity Tax Credit, as of January 1, 2012, with a new expiration date of December 31, 2013. Because a change in tax law is accounted for in the period of enactment, and the Act was enacted after Fiesta's fiscal year-end, the retroactive effect of renewing the Work Opportunity Tax Credit is recorded as a discrete item in the nine months ended September 29, 2013.

Discrete tax adjustments decreased the provision for income taxes by \$0.2 million in the nine months ended September 30, 2012.

**Net Income.** As a result of the foregoing, we had net income of \$14.8 million in the nine months ended September 29, 2013 compared to net income of \$5.7 million in the nine months ended September 30, 2012.

Liquidity and Capital Resources

We do not have significant receivables or inventory and receive trade credit based upon negotiated terms in purchasing food products and other supplies. We are able to operate with a substantial working capital deficit because:

- restaurant operations are primarily conducted on a cash basis;
- rapid turnover results in a limited investment in inventories; and
- cash from sales is usually received before related liabilities for food, supplies and payroll become due.



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On August 5, 2011, we and Carrols Restaurant Group entered into new financing arrangements, the proceeds from which were used to distribute funds to Carrols Restaurant Group to enable Carrols Restaurant Group to repay its existing indebtedness, as well as to pay accrued interest and all related fees and expenses. On August 5, 2011 we sold \$200.0 million of our 8.875% Senior Secured Second Lien Notes due 2016 (the "Notes") and entered into a \$25.0 million senior secured revolving credit facility which was undrawn at closing. Excess cash generated from the financings in August 2011 was approximately \$9.5 million. Carrols Restaurant Group transferred \$2.5 million of the excess cash from the financings to us in the first quarter of 2012.

Interest payments under our debt obligations, capital expenditures and payments related to our lease obligations represent significant liquidity requirements for us. We believe cash generated from our operations, availability of revolving credit borrowings under our senior credit facility and proceeds from any sale-leaseback transactions which we may choose to do will provide sufficient cash availability to cover our anticipated working capital needs, capital expenditures and debt service requirements for the next twelve months.

Operating Activities. Net cash provided by operating activities for the first nine months of 2013 and 2012 was \$20.3 million and \$21.3 million, respectively. The decrease in net cash provided by operating activities was driven by the change in operating assets and liabilities primarily as a result of the timing of tax payments and payments under the TSA, partially offset by the increase in net income before impairments.

Investing Activities. Net cash used for investing activities in the first nine months of 2013 and 2012 was \$30.7 million and \$28.5 million, respectively. Capital expenditures are the largest component of our investing activities and include: (1) new restaurant development, which may include the purchase of real estate; (2) restaurant remodeling, which includes the renovation or rebuilding of the interior and exterior of our existing restaurants; (3) other restaurant capital expenditures, which include capital maintenance expenditures for the ongoing reinvestment and enhancement of our restaurants; and (4) corporate and restaurant information systems.

The following table sets forth our capital expenditures for the periods presented (in thousands):

	Pollo Tropical	Taco Cabana	Other	Consolidated
Nine Months Ended September 29, 2013:				
New restaurant development	\$ 19,169	\$ 9,273	\$—	\$ 28,442
Restaurant remodeling	496	2,106	—	2,602
Other restaurant capital expenditures (1)	1,707	2,445	—	4,152
Corporate and restaurant information systems	155	161	3,279	3,595
Total capital expenditures	\$ 21,527	\$ 13,985	\$ 3,279	\$ 38,791
Number of new restaurant openings	10	5		15
Nine Months Ended September 30, 2012:				
New restaurant development	\$ 10,317	\$ 6,473	\$—	\$ 16,790
Restaurant remodeling	557	5,374	—	5,931
Other restaurant capital expenditures (1)	2,442	2,858	—	5,300
Corporate and restaurant information systems	93	329	427	849
Total capital expenditures	\$ 13,409	\$ 15,034	\$ 427	\$ 28,870
Number of new restaurant openings	4	3		7

Excludes restaurant repair and maintenance expenses included in other restaurant operating expenses in our 1) consolidated financial statements. For the nine months ended September 29, 2013 and September 30, 2012, total restaurant repair and maintenance expenses were approximately \$8.8 million in both periods.

For the full year 2013, we anticipate that total capital expenditures will range from \$45 million to \$50 million which includes costs to open 18 company-owned restaurants, although the actual amount of capital expenditures may differ from these estimates. In 2014, we anticipate that total capital expenditures will range from \$60 million to \$65 million which includes costs to open 22 to 26 additional company-owned restaurants.

In the first nine months of 2013, investing activities also included four sale-leaseback transactions related to our restaurant properties, the net proceeds from which were \$10.8 million, as well as the sale of an excess Pollo Tropical property, the net proceeds from which were \$1.7 million. In the first nine months of 2012, investing activities included sale-leaseback transactions related to our restaurant properties, the net proceeds from which were \$1.5 million, and the sale of an excess property, the net proceeds from which were \$0.9 million. The net proceeds from the sales were used to fund additional new restaurant development. In the

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first nine months of 2013, we purchased for \$4.4 million two of our existing Taco Cabana restaurant properties and one of our existing Pollo Tropical properties to be sold in future sale-leaseback transactions, and in the first nine months of 2012 we purchased for \$2.1 million one of our existing Pollo Tropical restaurant properties to be sold in a future sale-leaseback transaction.

Financing Activities. Net cash provided by financing activities in the first nine months of 2013 was \$0.8 million and included the excess tax benefit from vesting of restricted shares of \$0.8 million. Net cash used in financing activities in the first nine months of 2012 was \$3.3 million, and included the purchase of five restaurant properties previously accounted for as lease financing obligations from the lessor for \$6.0 million, net borrowings on intercompany debt of \$0.5 million prior to the Spin-off and the transfer from Carrols to us of \$2.5 million of the excess cash proceeds from the 2011 financings.

Senior Secured Credit Facility. We have a senior secured credit facility providing for aggregate revolving credit borrowings of up to \$25.0 million (including \$10.0 million available for letters of credit). The senior credit facility also provides for incremental increases of up to \$5.0 million, in the aggregate, to the revolving credit borrowings available under the senior credit facility, and matures on February 5, 2016. On September 29, 2013, there were no outstanding borrowings under our senior credit facility.

Borrowings under the senior credit facility bear interest at a per annum rate, at our option, of either the (all terms as defined in the senior credit facility):

- 1) Alternate Base Rate plus the applicable margin of 2.00% to 2.75% based on our Adjusted Leverage Ratio (with a margin of 2.00% at September 29, 2013); or
- 2) LIBOR Rate plus the applicable margin of 3.00% to 3.75% based on our Adjusted Leverage Ratio (with a margin of 3.00% at September 29, 2013).

Our obligations under our senior credit facility are guaranteed by all of our material subsidiaries and are secured by a first priority lien on substantially all of our assets and of our material subsidiaries (including a pledge of all of the capital stock and equity interests of our material subsidiaries).

Our senior credit facility contains certain covenants, including without limitation, those limiting our and our guarantor subsidiaries' ability to, among other things, incur indebtedness, incur liens, sell or acquire assets or businesses, change the character of our business in all material respects, engage in transactions with related parties, make certain investments, make certain restricted payments or pay dividends. In addition, the senior credit facility requires us to meet certain financial ratios, including a Fixed Charge Coverage Ratio and Adjusted Leverage Ratio (all as defined under the senior credit facility).

Our senior credit facility contains customary default provisions, including without limitation, a cross default provision pursuant to which it is an event of default under this facility if there is a default under any of our indebtedness having an outstanding principal amount of \$2.5 million or more which results in the acceleration of such indebtedness prior to its stated maturity or is caused by a failure to pay principal when due. As of September 29, 2013, we were in compliance with the covenants under our senior credit facility. After reserving \$8.4 million for letters of credit guaranteed by the senior credit facility, \$16.6 million was available for borrowing under the senior credit facility at September 29, 2013.

Notes. On August 5, 2011, we issued \$200.0 million of Notes pursuant to an indenture dated as of August 5, 2011 governing such Notes. The proceeds from the issuance of the Notes were used by Carrols Restaurant Group to repay amounts outstanding under Carrols LLC's prior senior credit facility and Carrols' 9% senior subordinated notes due 2013, as well as to pay related fees and expenses. The Notes mature and are payable on August 15, 2016. Interest is payable semi-annually on February 15 and August 15. The Notes are guaranteed by all of our material subsidiaries and are secured by second-priority liens on substantially all of our and our material subsidiaries' assets (including a pledge of all of the capital stock and equity interests of our material subsidiaries).

The indenture governing the Notes and the security agreement provide that any capital stock and equity interests of any of our material subsidiaries will be excluded from the collateral to the extent that the par value, book value or market value of such capital stock or equity interests exceeds 20% of the aggregate principal amount of the Notes then outstanding.

The Notes are redeemable at our option in whole or in part at any time after February 15, 2014 at a price of 104.438% of the principal amount plus accrued and unpaid interest, if any, if redeemed before February 15, 2015, 102.219% of the principal amount plus accrued and unpaid interest, if any, if redeemed after February 15, 2015 but before February 15, 2016 and 100% of the principal amount plus accrued and unpaid interest, if any, if redeemed after February 15, 2016. Prior to February 15, 2014, we may redeem some or all of the Notes at a redemption price of 100% of the principal amount of each note plus accrued and unpaid interest, if any, and a make-whole premium. In addition, at any time prior to February 15, 2014, we may redeem up to 35% of the Notes with the net cash proceeds from specified equity offerings at a redemption price equal to 108.875% of the principal amount of each note to be redeemed, plus accrued and unpaid interest, if any, to the date of redemption.

The Notes are jointly and severally guaranteed, unconditionally and in full by all of our material subsidiaries which are directly or indirectly wholly-owned by us. Separate condensed consolidating information is not included because we are a holding company with all of our operations conducted through the guarantor subsidiaries. There are no significant restrictions on our ability

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or the ability of any of the guarantor subsidiaries to obtain funds from our respective subsidiaries. All consolidated amounts in our financial statements are representative of the combined guarantors.

The indenture governing the Notes includes certain covenants, including limitations and restrictions on us and our material subsidiaries who are guarantors under such indenture to incur additional debt, issue preferred stock, pay dividends or make distributions in respect of capital stock or make certain other restricted payments or investments, incur liens, sell assets, enter into transactions with affiliates, agree to payment restrictions affecting certain of our material subsidiaries and enter into mergers, consolidations or sales of all or substantially all of our or our material subsidiaries' assets.

The indenture governing the Notes contains customary default provisions, including without limitation, a cross default provision pursuant to which it is an event of default under the Notes and the indenture if there is a default under any indebtedness of ours having an outstanding principal amount of \$15.0 million or more which results in the acceleration of such indebtedness prior to its stated maturity or is caused by a failure to pay principal when due. We were in compliance as of September 29, 2013 with the restrictive covenants of the indenture governing the Notes.

**Off-Balance Sheet Arrangements**

We have no off-balance sheet arrangements other than our operating leases, which are primarily for our restaurant properties and not recorded on our consolidated balance sheet.

**Application of Critical Accounting Policies**

Our unaudited interim condensed consolidated financial statements and accompanying notes are prepared in accordance with accounting principles generally accepted in the United States of America. Preparing consolidated financial statements requires us to make estimates and assumptions that affect the reported amounts of assets, liabilities, revenue and expenses. These estimates and assumptions are affected by the application of our accounting policies. Our significant accounting policies are described in the "Significant Accounting Policies" footnote in the notes to our Consolidated Financial Statements for the year ended December 30, 2012 included in our 2012 Annual Report on Form 10-K. Critical accounting estimates are those that require application of management's most difficult, subjective or complex judgments, often as a result of matters that are inherently uncertain and may change in subsequent periods. There have been no material changes affecting our critical accounting policies for the nine months ended September 29, 2013.

**Management's Use of Non-GAAP Financial Measures**

Adjusted EBITDA is a non-GAAP financial measure. We use Adjusted EBITDA in addition to net income, income from operations, and income before income taxes to assess our performance, and we believe it is important for investors to be able to evaluate the Company using the same measures used by management. We believe this measure is an important indicator of our operational strength and the performance of our business. Adjusted EBITDA as calculated by us is not necessarily comparable to similarly titled measures reported by other companies, and should not be considered as an alternative to net income, earnings per share, cash flows from operating activities or other financial information determined under GAAP.

Adjusted EBITDA is defined as earnings before interest, income taxes, depreciation and amortization, impairment and other lease charges, stock-based compensation expense and other income and expense. Adjusted EBITDA for each of our segments includes an allocation of general and administrative expenses associated with administrative support for executive management, information systems and certain accounting, legal and other administrative functions.

Management believes that such financial measures, when viewed with our results of operations calculated in accordance with GAAP and our reconciliation of Adjusted EBITDA for each of our Pollo Tropical and Taco Cabana segments and Consolidated Adjusted EBITDA to net income (i) provide useful information about our operating performance and period-over-period growth, (ii) provide additional information that is useful for evaluating the operating performance of our business and (iii) permit investors to gain an understanding of the factors and trends affecting our ongoing earnings, from which capital investments are made and debt is serviced. However, such measures are not measures of financial performance or liquidity under GAAP and, accordingly, should not be considered as alternatives to net income or cash flow from operating activities as indicators of operating performance or liquidity. Also these measures may not be comparable to similarly titled captions of other companies.

All of such non-GAAP financial measures have important limitations as analytical tools. These limitations include the following:

- such financial information does not reflect our capital expenditures, future requirements for capital expenditures or contractual commitments to purchase capital equipment;
- such financial information does not reflect interest expense or the cash requirements necessary to service principal or interest payments on our debt;

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although depreciation and amortization are non-cash charges, the assets that we currently depreciate and amortize will likely have to be replaced in the future, and such financial information does not reflect the cash required to fund such replacements; and such financial information does not reflect the effect of earning or charges resulting from matters that our management does not consider to be indicative of our ongoing operations. However, some of these charges (such as impairment and other lease charges, other income and expense and stock-based compensation expense) have recurred and may recur.

A reconciliation of Adjusted EBITDA to consolidated net income follows:

	Three Months Ended		Nine Months Ended	
	September 29, 2013	September 30, 2012	September 29, 2013	September 30, 2012
Adjusted EBITDA:				
Pollo Tropical	\$ 10,709	\$ 9,079	\$ 32,487	\$ 30,743
Taco Cabana	6,804	6,653	20,535	19,762
Consolidated	17,513	15,732	53,022	50,505
Less:				
Depreciation and amortization	5,129	4,486	15,117	13,703
Impairment and other lease charges	(312)	(45)	239	6,816
Interest expense	4,457	5,036	14,475	19,334
Provision for income taxes	2,596	2,226	7,256	3,344
Stock-based compensation expense	658	380	1,679	1,603
Other income	(57)	—	(554)	—
Net income	\$ 5,042	\$ 3,649	\$ 14,810	\$ 5,705

## Forward Looking Statements

This Quarterly Report on Form 10-Q contains “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.

“Forward-looking statements” are any statements that are not based on historical information. Statements other than statements of historical facts included herein, including, without limitation, statements regarding our future financial position and results of operations, business strategy, budgets, projected costs and plans and objectives of management for future operations, are “forward-looking statements.” Forward-looking statements generally can be identified by the use of forward-looking terminology such as “may,” “will,” “expect,” “anticipate,” “intend,” “plan,” “believe,” “seek,” “estimate,” “continue” or the negative of such words or variations of such words and similar expressions. These statements are not guarantees of future performance and involve certain risks, uncertainties and assumptions, which are difficult to predict. Therefore, actual outcomes and results may differ materially from what is expressed or forecasted in such forward-looking statements and we can give no assurance that such forward-looking statements will prove to be correct. Important factors that could cause actual results to differ materially from those expressed or implied by the forward-looking statements, or “cautionary statements,” include, but are not limited to:

- The effect of the Spin-off;
- The potential tax liability associated with the Spin-off;
- Increases in food and other commodity costs;
- Competitive conditions;
- Regulatory factors;
- Environmental conditions and regulations;
- General economic conditions, particularly in the retail sector;
- Weather conditions;
- Fuel prices;
- Significant disruptions in service or supply by any of our suppliers or distributors;

Changes in consumer perception of dietary health and food safety;

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• Labor and employment benefit costs;

• The outcome of pending or future legal claims or proceedings;

• Our ability to manage our growth and successfully implement our business strategy;

• Risks associated with the expansion of our business;

• Our borrowing costs and credit ratings, which may be influenced by the credit ratings of our competitors;

• The availability and terms of necessary or desirable financing or refinancing and other related risks and uncertainties;

• The risk of an act of terrorism or escalation of any insurrection or armed conflict involving the United States or any other national or international calamity; and

Factors that affect the restaurant industry generally, including product recalls, liability if our products cause injury, ingredient disclosure and labeling laws and regulations, reports of cases of food borne illnesses such as “mad cow” disease and avian flu, and the possibility that consumers could lose confidence in the safety and quality of certain food products, as well as negative publicity regarding food quality, illness, injury or other health concerns.

**Inflation**

The inflationary factors that have historically affected our results of operations include increases in food and paper costs, labor and other operating expenses and energy costs. Labor costs in our restaurants are impacted by changes in the Federal and state hourly minimum wage rates as well as changes in payroll related taxes, including Federal and state unemployment taxes. We typically attempt to offset the effect of inflation, at least in part, through periodic menu price increases and various cost reduction programs. However, no assurance can be given that we will be able to fully offset such inflationary cost increases in the future.

**ITEM 3—QUANTITATIVE AND QUALITATIVE DISCLOSURES ABOUT MARKET RISK**

There were no material changes from the information presented in Item 7A included in our Annual Report on Form 10-K for the year ended December 30, 2012 with respect to our market risk sensitive instruments.

**ITEM 4—CONTROLS AND PROCEDURES**

**Disclosure Controls and Procedures.** Our senior management is responsible for establishing and maintaining disclosure controls and procedures (as defined in Rules 13a-15(e) and 15d-15(e) under the Securities Exchange Act of 1934, as amended (the “Exchange Act”)), designed to ensure that information required to be disclosed by us in the reports that we file or submit under the Exchange Act is recorded, processed, summarized and reported, within the time periods specified in the Securities and Exchange Commission's rules and forms. Disclosure controls and procedures include, without limitation, controls and procedures designed to ensure that information required to be disclosed by an issuer in the reports that it files or submits under the Exchange Act is accumulated and communicated to the issuer's management, including its principal executive officer or officers and principal financial officer or officers, or persons performing similar functions, as appropriate to allow timely decisions regarding required disclosure.

**Evaluation of Disclosure Controls and Procedures.** We have evaluated the effectiveness of our disclosure controls and procedures (as defined in Rules 13a-15(e) and 15d-15(e) under the Exchange Act) as of the end of the period covered by this report, with the participation of our Chief Executive Officer and Chief Financial Officer, as well as other key members of our management. Based on this evaluation, our Chief Executive Officer and Chief Financial Officer concluded that our disclosure controls and procedures were effective as of September 29, 2013.

No change occurred in our internal control over financial reporting during the third quarter of 2013 that materially affected, or is reasonably likely to materially affect, our internal control over financial reporting.

Subsequent to September 29, 2013, the Company completed the implementation of its enterprise resource planning system as part of the transition from Carrols.

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PART II—OTHER INFORMATION

Item 1. Legal Proceedings

None

Item 1A. Risk Factors

Part 1 - Item 1A of our Annual Report on Form 10-K for the fiscal year ended December 30, 2012 describes important factors that could cause our actual operating results to differ materially from those indicated or suggested by forward-looking statements made in this Form 10-Q or presented elsewhere by management from time-to-time. There have been no material changes from the risk factors previously disclosed in our Annual Report on Form 10-K for the fiscal year ended December 30, 2012.

Item 2. Unregistered Sales of Equity Securities and Use of Proceeds

None

Item 3. Defaults Upon Senior Securities

None

Item 4. Mine Safety Disclosures

Not applicable

Item 5. Other Information

None

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Item 6. Exhibits

(a) The following exhibits are filed as part of this report.

Exhibit  
No.

31.1	Chief Executive Officer's Certificate Pursuant to Section 302 of the Sarbanes-Oxley Act of 2002 for Fiesta Restaurant Group, Inc.
31.2	Chief Financial Officer's Certificate Pursuant to Section 302 of the Sarbanes-Oxley Act of 2002 for Fiesta Restaurant Group, Inc.
32.1	Chief Executive Officer's Certificate Pursuant to 18 U.S.C. Section 1350, As Adopted Pursuant to Section 906 of the Sarbanes-Oxley Act of 2002 for Fiesta Restaurant Group, Inc.
32.2	Chief Financial Officer's Certificate Pursuant to 18 U.S.C. Section 1350, As Adopted Pursuant to Section 906 of the Sarbanes-Oxley Act of 2002 for Fiesta Restaurant Group, Inc.
*101.INS	XBRL Instance Document
*101.SCH	XBRL Taxonomy Extension Schema Document
*101.CAL	XBRL Taxonomy Extension Calculation Linkbase Document
*101.DEF	XBRL Taxonomy Extension Definition Linkbase Document
*101.LAB	XBRL Taxonomy Extension Label Linkbase Document
*101.PRE	XBRL Taxonomy Extension Presentation Linkbase Document

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As provided in Rule 406T of Regulation S-T, this information is deemed furnished and not filed for purposes of \*Sections 11 and 12 of the Securities Act of 1933, as amended, and Section 18 of the Securities Exchange Act of 1934, as amended.

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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.

FIESTA RESTAURANT GROUP, INC.

Date: November 5, 2013 /S/ TIMOTHY P. TAFT  
(Signature)  
Timothy P. Taft  
Chief Executive Officer

Date: November 5, 2013 /S/ LYNN S. SCHWEINFURTH  
(Signature)  
Lynn S. Schweinfurth  
Vice President, Chief Financial Officer and Treasurer

Date: November 5, 2013 /S/ ANGELA J. NEWELL  
(Signature)  
Angela J. Newell  
Vice President, Corporate Controller