Papa Murphy's Holdings, Inc.
Form 10-Q
August 03, 2016
Table of Contents

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

FORM 10-Q

(Mark One)
[X] QUARTERLY REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934.
For the quarterly period ended June 27, 2016
OR
[ ] TRANSITION REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934
For the transition period from to
Commission file number 001-36432

Papa Murphy’s Holdings, Inc.
(Exact name of registrant as specified in its charter)

Delaware (State or Other Jurisdiction of Incorporation or Organization)	27-2349094 (IRS Employer Identification No.)
8000 NE Parkway Drive, Suite 350 Vancouver, WA (Address of principal executive offices)	98662 (Zip Code)

(360) 260-7272
(Registrant’s telephone number, including area code)

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

Large accelerated filer [ ]	Accelerated filer [X]
Non-accelerated filer [ ]	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 [X].
At July 29, 2016, there were 16,957,420 shares of the Registrant’s common stock, $0.01 par value, outstanding.

Table of Contents

TABLE OF CONTENTS

Table of Contents

PART I — FINANCIAL INFORMATION

Item 1. Financial Statements

Papa Murphy’s Holdings, Inc. and Subsidiaries

Unaudited Condensed Consolidated Statements of Net Income (Loss)

	Three Months Ended		Six Months Ended	
(In thousands, except share and per share data)	June 27, 2016	June 29, 2015	June 27, 2016	June 29, 2015
Revenues				
Franchise royalties	$9,538	$ 9,753	$20,034	$ 20,433
Franchise and development fees	574	830	1,528	1,970
Company-owned store sales	19,470	18,156	40,144	35,323
Other	312	382	1,173	564
Total revenues	29,894	29,121	62,879	58,290
Costs and Expenses				
Store operating costs:				
Cost of food and packaging	6,781	6,443	14,053	12,533
Compensation and benefits	5,577	4,722	11,311	9,076
Advertising	1,897	1,753	4,063	3,422
Occupancy	1,503	1,174	2,878	2,176
Other store operating costs	2,555	1,856	4,846	3,301
Selling, general and administrative	5,912	8,162	14,967	15,045
Depreciation and amortization	2,915	2,420	5,630	4,739
(Gain) loss on disposal of property and equipment	(59)	3	(5)	62
Total costs and expenses	27,081	26,533	57,743	50,354
Operating Income	2,813	2,588	5,136	7,936
Interest expense, net	1,208	1,143	2,387	2,273
Loss on impairment of investments	—	4,500	—	4,500
Other expense, net	43	44	85	46
Income (Loss) Before Income Taxes	1,562	(3,099)	2,664	1,117
Provision for (benefit from) income taxes	610	(1,160)	1,070	460
Net Income (Loss)	952	(1,939)	1,594	657
Net loss attributable to noncontrolling interests	—	500	—	500
Net Income (Loss) Attributable to Papa Murphy’s	$952	$ (1,439)	$1,594	$ 1,157
Earnings (loss) per share of common stock				
Basic	$0.06	$ (0.09)	$0.10	$ 0.07
Diluted	$0.06	$ (0.09)	$0.10	$ 0.07
Weighted average common stock outstanding				
Basic	16,744,553	16,629,666	16,730,581	16,616,936
Diluted	16,766,587	16,629,666	16,760,578	16,872,504

See accompanying notes.

Table of Contents

Papa Murphy’s Holdings, Inc. and Subsidiaries
Unaudited Condensed Consolidated Balance Sheets

(In thousands, except par value and share data)	June 27, 2016	December 28, 2015
ASSETS		
Current Assets		
Cash and cash equivalents	$435	$ 6,867
Accounts receivable, net	2,824	4,944
Current portion of notes receivable	85	78
Inventories	967	868
Prepaid expenses and other current assets	5,087	6,139
Total current assets	9,398	18,896
Property and equipment, net	27,816	21,261
Notes receivable, net of current portion	99	143
Goodwill	108,462	106,506
Trade name and trademarks	87,002	87,002
Definite-life intangibles, net	38,844	41,366
Other assets	405	297
Total assets	$272,026	$ 275,471
LIABILITIES AND STOCKHOLDERS’ EQUITY		
Current Liabilities		
Accounts payable	$5,446	$ 9,798
Accrued expenses and other current liabilities	7,789	9,756
Current portion of unearned franchise and development fees	1,630	1,795
Current portion of long-term debt	3,679	2,800
Total current liabilities	18,544	24,149
Long-term debt, net of current portion	107,195	108,237
Unearned franchise and development fees, net of current portion	358	540
Deferred tax liability	42,671	42,439
Other long-term liabilities	3,268	2,450
Total liabilities	172,036	177,815
Commitments and contingencies (Note 14)		
Stockholders’ Equity		
Preferred stock ($0.01 par value; 15,000,000 shares authorized; no shares issued)	—	—
Common stock ($0.01 par value; 200,000,000 shares authorized; 16,957,420 and 16,949,720 shares issued, respectively)	170	169
Additional paid-in capital	119,481	118,842
Stock subscriptions receivable	—	(100)
Accumulated deficit	(19,661)	(21,255)
Total stockholders’ equity	99,990	97,656
Total liabilities and stockholders’ equity	$272,026	$ 275,471

See accompanying notes.

Papa Murphy’s Holdings, Inc. and Subsidiaries
Unaudited Condensed Consolidated Statements of Cash Flows

(In thousands)	Six Months Ended June 27, 2016	June 29, 2015
Operating Activities		
Net income	$1,594	$657
Net loss attributable to noncontrolling interests	—	500
Net income attributable to Papa Murphy’s	1,594	1,157
Adjustments to reconcile to cash from operating activities		
Depreciation and amortization	5,630	4,739
(Gain) loss on disposal of property and equipment	(5)	62
Non-cash employee equity compensation	427	656
Loss on impairment of cost-method investment	—	4,000
Other non-cash items	158	485
Change in operating assets and liabilities		
Accounts receivable	1,984	556
Prepaid expenses and other assets	1,072	(1,050)
Unearned franchise and development fees	(347)	(678)
Accounts payable	(3,840)	1,296
Accrued expenses and other liabilities	(1,520)	(1,025)
Deferred taxes	232	(468)
Net cash from operating activities	5,385	9,730
Investing Activities		
Acquisition of property and equipment	(9,533)	(2,834)
Acquisition of stores, less cash acquired	(2,449)	(9,343)
Proceeds from sale of stores	136	—
Issuance of notes receivable	—	(250)
Payments received on notes receivable	37	32
Investment in cost-method investee	—	(500)
Net cash from investing activities	(11,809)	(12,895)
Financing Activities		
Payments on long-term debt	(3,321)	(1,400)
Advances on revolver, net	3,000	500
Repurchases of common stock	(80)	(10)
Proceeds from exercise of stock options	293	51
Payments received on subscription receivables	100	—
Investment by noncontrolling interest holders	—	56
Net cash from financing activities	(8)	(803)
Net change in cash and cash equivalents	(6,432)	(3,968)
Cash and Cash Equivalents, beginning of year	6,867	5,056
Cash and Cash Equivalents, end of period	$435	$1,088
Supplemental Disclosures of Cash Flow Information		
Cash paid during the period for interest	$2,243	$2,164

Cash paid during the period for income taxes	136	1,422
Noncash Supplemental Disclosures of Investing and Financing Activities		
Acquisition of property and equipment in accounts payable	$2,509	$1,074

See accompanying notes.

Table of Contents

Papa Murphy’s Holdings, Inc. and Subsidiaries
Notes to Unaudited Condensed Consolidated Financial Statements

Note 1 — Description of Business and Basis of Presentation
Description of business
Papa Murphy’s Holdings, Inc. (“Papa Murphy’s” or the “Company”), together with its subsidiaries, is a franchisor and operator of a Take ‘N’ Bake pizza chain. The Company franchises the right to operate Papa Murphy’s Take ‘N’ Bake pizza franchises and operates Papa Murphy’s Take ‘N’ Bake pizza stores owned by the Company. As of June 27, 2016, the Company had 1,570 stores consisting of 1,531 domestic stores (1,375 franchised stores and 156 Company-owned stores) across 38 states, plus 39 franchised stores in Canada and the United Arab Emirates.
Substantially all of the Company’s revenues are derived from retail sales of pizza and other food and beverage products to the general public by Company-owned stores and the collection of franchise royalties and fees associated with franchise and development rights.
Basis of presentation
The accompanying interim unaudited condensed consolidated financial statements have been prepared pursuant to the rules and regulations of the U.S. Securities and Exchange Commission (the “SEC”). Accordingly, they do not include all information and footnotes required by generally accepted accounting principles in the United States (“GAAP”) for complete financial statements. In the Company’s opinion, all necessary adjustments, consisting of only normal recurring adjustments, have been made for the fair statement of the results of the interim periods presented. The results of operations for such interim periods are not necessarily indicative of the results to be expected for the full year. The accompanying interim unaudited condensed consolidated financial statements should be read in conjunction with the audited financial statements and the related notes thereto included in the Company’s Annual Report on Form 10-K for the year ended December 28, 2015.
During the three months ended March 28, 2016, the Company early-adopted ASU No. 2016-09, Compensation — Stock Compensation (Topic 718): Improvements to Employee Share-Based Payment Accounting (“ASU 2016-09”). The Company applied the new guidance on a modified retrospective basis through a cumulative-effect adjustment. As a result, changes have been made to the presentation of Stockholders’ Equity in the Condensed Consolidated Balance Sheets as of December 28, 2015. See Recent Accounting Pronouncements below for additional information. A summary of the changes made to the Condensed Consolidated Balance Sheets as of December 28, 2015, is included in the following table:

(in thousands)	As Filed	Updated
Additional paid-in capital	$118,801	$118,842
Accumulated deficit	(21,214)	(21,255)

Principles of consolidation
The interim unaudited condensed consolidated financial statements include the accounts of Papa Murphy’s Holdings, Inc., its subsidiaries and certain entities which the Company consolidates as variable interest entities (“VIEs”). All significant intercompany transactions and balances have been eliminated.
Throughout the interim unaudited condensed consolidated financial statements and the related notes thereto, “Papa Murphy’s” and “the Company” refer to Papa Murphy’s Holdings, Inc. and its consolidated subsidiaries.
Fiscal year
The Company uses a 52- or 53-week fiscal year, ending on the Monday nearest to December 31. Fiscal year 2016 is a 53-week year and 2015 was a 52-week year. All three month periods presented herein contain 13 weeks. All references to years and quarters relate to fiscal periods rather than calendar periods. References to 2016 and 2015 are references to fiscal years ending January 2, 2017, and ended December 28, 2015, respectively.
Accounting Pronouncements Recently Adopted
In March 2016, the Financial Accounting Standards Board (“FASB”) issued ASU 2016-09, which simplifies several aspects of the accounting for share-based payment awards to employees, including the accounting for income taxes, forfeitures, statutory tax withholding requirements and classification in the statement of cash flows. The effective date for ASU 2016-09 is for fiscal years, and interim periods within those fiscal years, beginning after December 15, 2016.

Early adoption is permitted in any annual or interim period for which financial statements have not yet been issued. All amendments in ASU 2016-09 that apply must be adopted in the same period. The Company early-adopted ASU 2016-09 at the beginning of fiscal year 2016. As permitted under ASU 2016-09, the Company has elected to account for forfeitures in compensation cost when they occur in order to ease the administrative burden of estimating forfeitures. The effect of adopting ASU 2016-09 is reflected in Stockholders' Equity in the Condensed Consolidated Balance Sheets on a modified retrospective basis through a cumulative-effect adjustment. See Basis of Presentation above for additional information.

Recent Accounting Pronouncements

In May 2014, the FASB issued ASU No. 2014-09, Revenue from Contracts with Customers (Topic 606) ("ASU 2014-09"), a new standard to achieve a consistent application of revenue recognition within the U.S., resulting in a single revenue model to be applied by reporting companies under GAAP. The original effective date for ASU 2014-09 would have required adoption by the Company in the first quarter of fiscal 2017 with early adoption prohibited. In August 2015, the FASB issued ASU No. 2015-14, Revenue from Contracts with Customers (Topic 606) - Deferral of the Effective Date, which defers the effective date of ASU 2014-09 for one year and permits early adoption in accordance with the original effective date of ASU 2014-09. In March 2016, the FASB issued ASU 2016-08, Revenue from Contracts with Customers (Topic 606): Principal versus Agent Considerations (Reporting Revenue Gross versus Net) which is an amendment to the new revenue recognition standard on assessing whether an entity is a principal or an agent in a revenue transaction. This

Table of Contents

amendment addresses implementation issues that were discussed by the Revenue Recognition Transition Resource Group to clarify the principal versus agent assessment and lead to more consistent application. This new standard has the same effective date and transition requirements as ASU 2014-09.

The new revenue standard is required to be applied retrospectively to each prior reporting period presented or retrospectively with the cumulative effect of initially applying the standard recognized at the date of initial application. The Company has not yet selected a transition method. The Company is continuing to evaluate the impact the adoption of this standard will have on the recognition of revenue.

In February 2016, the FASB issued ASU No. 2016-02, Leases (“ASU 2016-02”). This update requires that lessees recognize assets and liabilities on the balance sheet for the rights and obligations created by all leases with terms of more than twelve months. ASU 2016-02 also will require disclosures designed to give financial statement users information on the amount, timing, and uncertainty of cash flows arising from leases. These disclosures include both qualitative and quantitative information. The effective date for ASU 2016-02 is for fiscal years, and interim periods within those fiscal years, beginning after December 15, 2018, with early adoption permitted. The Company is still evaluating the impact of ASU 2016-02 on its financial position and results of operations.

Note 2 — Acquisitions

On April 11, 2016, Papa Murphy’s Company Stores, Inc., a wholly owned subsidiary of the Company, acquired certain assets used in the operation of nine Papa Murphy’s stores in the Joplin, Missouri, and Fort Smith, Arkansas, areas from a franchise owner. The total consideration paid of approximately $2.9 million was funded through existing cash, $0.5 million in insurance proceeds and advances on the Company's Senior Credit Facility (see Note 8 — Financing Arrangements).

The fair values of the assets acquired are summarized below (in thousands):

Cash and cash equivalents	$4
Inventory	23
Prepaid expenses and other current assets	22
Property and equipment	503
Asset retirement obligations	(59)
Total identifiable net assets acquired	493
Goodwill	1,956
Total net assets acquired	2,449
Dispute settlement	500
Total consideration	$2,949

Goodwill represents the excess of the purchase price over the net tangible and intangible assets acquired and is expected to be fully deductible for income tax purposes. This goodwill is primarily attributable to the acquired customer bases and, to a lesser extent, economies of scale expected from combining the operations of the acquired stores with the existing operations of the Company.

The pro forma effects of this acquisition and the operating results of the acquired stores are not presented because the effects were not material to reported results.

Note 3 — Prepaid Expenses and Other Current Assets

Prepaid expenses and other current assets consist of the following:

(in thousands)	June 27, 2016	December 28, 2015
Prepaid media production costs	$ 430	$ 352
Prepaid software and services	964	464
Prepaid rents	557	477
Prepaid insurance	84	602
Taxes receivable	2,170	2,872
POS software licenses for resale	—	660
Assets held for sale	599	605
Advertising cooperative assets, restricted	208	26

Other	75	81
Total prepaid expenses and other current assets	$ 5,087	$ 6,139

The Company recognizes software license revenue upon the resale of Point of Sale (“POS”) software licenses to franchise owners at cost. The income from the sale is included in Other revenues and the related expense is recorded in Selling, general and administrative costs on the Condensed Consolidated Statements of Net Income (Loss). POS software license revenue during the periods reported was as follows:

	Three Months Ended		Six Months Ended	
(in thousands)	June 27, 2016	June 29, 2015	June 27, 2016	June 29, 2015
POS software license revenue	$ —	$ 115	$ 657	$ 301

7

Table of Contents

Note 4 — Property and Equipment

Property and equipment are net of accumulated depreciation of $14.1 million and $13.8 million at June 27, 2016, and December 28, 2015, respectively. Depreciation expense during the periods reported was as follows:

(in thousands)	Three Months Ended		Six Months Ended	
	June 27, 2016	June 29, 2015	June 27, 2016	June 29, 2015
Depreciation expense	$1,664	$ 1,075	$3,108	$ 2,079

Note 5 — Goodwill

The following summarizes changes to the Company's goodwill, by reportable segment:

(in thousands)	Domestic Company Stores	Domestic Franchise	Total
Balance at December 28, 2015	$ 24,960	$ 81,546	$106,506
Acquisitions	1,956	—	1,956
Balance at June 27, 2016	$ 26,916	$ 81,546	$108,462

There is no goodwill associated with the International Segment. The Company has determined that during the three months ended June 27, 2016, there were no triggering events that would require an updated impairment review.

Note 6 — Intangible Assets

Intangible assets are net of accumulated amortization of $24.8 million and $23.0 million as of June 27, 2016, and December 28, 2015, respectively. Amortization expense during the periods reported was as follows:

(in thousands)	Three Months Ended		Six Months Ended	
	June 27, 2016	June 29, 2015	June 27, 2016	June 29, 2015
Amortization expense	$1,251	$ 1,345	$2,522	$ 2,660

Note 7 — Receivables

Notes Receivable

Notes receivable consist of a note maturing in 2020 that is collateralized by store assets. Changes in the account balance represent amortization payments collected pursuant to the terms of the note.

Accounts Receivable

The Company's allowance for doubtful accounts is as follows:

(in thousands)	June 27, 2016	December 28, 2015
Allowance for doubtful accounts	$ 34	$ 31

Note 8 — Financing Arrangements

Long-term debt consists of the following:

(in thousands)	June 27, 2016	December 28, 2015
Term loan	$105,879	$ 109,200
Revolving line of credit	3,000	—
Notes payable	3,000	3,000
Total principal amount of long-term debt	111,879	112,200
Unamortized debt issuance costs	(1,005)	(1,163)
Total long-term debt	110,874	111,037
Less current portion	(3,679)	(2,800)
Total long-term debt, net of current portion	$107,195	$ 108,237

Table of Contents

Senior secured credit facility

On August 28, 2014, PMI Holdings, Inc., a wholly-owned subsidiary of Papa Murphy's Holdings, Inc., entered into a $132.0 million senior secured credit facility (the "Senior Credit Facility") consisting of a $112.0 million term loan and a $20.0 million revolving credit facility, which includes a $2.5 million letter of credit subfacility and a $1.0 million swing-line loan subfacility. The term loan and any loans made under the revolving credit facility mature in August 2019. As of June 27, 2016, the outstanding term loan balance was subject to the LIBOR rate option at 3.70%. As of June 27, 2016, $2.5 million of the revolving credit facility was subject to the LIBOR rate option at 3.70%, and the remaining $0.5 million was subject to the base rate option at 5.75%.

With a maturity date of over one year from June 27, 2016, balances outstanding under the Senior Credit Facility are classified as non-current on the Condensed Consolidated Balance Sheets, except for mandatory, minimum term loan amortization payments due on the last day of each fiscal quarter. Minimum term loan amortization payments are $0.7 million, increasing to $1.4 million in the third fiscal quarter of 2016. A portion of the Company's future term loan amortization payments have been made in advance of their due dates.

The weighted average interest rate for all borrowings under our Senior Credit Facility for the second quarter of 2016 was 3.79%.

Notes payable

Papa Murphy's Company Stores, Inc., a wholly owned subsidiary of Papa Murphy's Holdings, Inc., has a $3.0 million note payable which bears interest at 5% and matures in December 2018. This note is subordinated to the Senior Credit Facility.

Note 9 — Fair Value Measurement

The Company determines the fair value of assets and liabilities based on the price that would be received to sell the asset or paid to transfer the liability to a market participant. GAAP defines a fair value hierarchy that prioritizes the assumptions used to measure fair value. The three levels of the fair value hierarchy are defined as follows:

Level 1 — Quoted prices in active markets for identical assets or liabilities that the entity has the ability to access.

Level 2 — Observable inputs other than prices included in Level 1, such as quoted prices for similar assets and liabilities in active markets; quoted prices for identical or similar assets and liabilities in markets that are not active; or other inputs that are observable or can be corroborated with observable market data.

Level 3 — Unobservable inputs that are supported by little or no market activity and that are significant to the fair value of the assets and liabilities. This includes certain pricing models, discounted cash flow methodologies, and similar techniques that use significant unobservable inputs.

The following table presents information about the Company's assets and liabilities measured at fair value on a recurring basis:

(in thousands)	June 27, 2016 Carrying Value	June 27, 2016 Fair Value	December 28, 2015 Carrying Value	December 28, 2015 Fair Value	Fair Value Measurement
Financial assets					
Notes receivable (1)	$ 184	$ 186	$ 221	$ 224	Level 3

(1) The fair value of notes receivable was estimated primarily using a discounted cash flow method based on a discount rate, reflecting the applicable credit spread.

Financial instruments not included in the table above consist of cash and cash equivalents, accounts receivable, accounts payable and long-term debt. The fair values of cash and cash equivalents, accounts receivable and accounts payable approximate carrying value because of the short-term nature of the accounts. The fair value of long-term debt approximates carrying value because the borrowings are made with variable market rates and negotiated terms and conditions that are consistent with current market rates.

Note 10 — Accrued Expenses and Other Current Liabilities

Accrued expenses and other current liabilities consist of the following:

(in thousands)	June 27, 2016	December 28, 2015
Accrued compensation and related costs	$ 3,235	$ 3,699

Gift cards payable	2,312	2,902
Accrued interest and non-income taxes payable	656	855
Convention fund balance	803	626
Unearned product rebates	55	922
Advertising cooperative liabilities	295	137
Other	433	615
Total accrued expenses and other current liabilities	$ 7,789	$ 9,756

9

Table of Contents

Note 11 — Income Taxes

Information on the Company's income taxes for the periods reported is as follows:

(in thousands)	Three Months Ended		Six Months Ended	
	June 27, 2016	June 29, 2015	June 27, 2016	June 29, 2015
Provision for (benefit from) income taxes	$610	$(1,160)	$1,070	$460
Income (loss) before income taxes	1,562	(3,099)	2,664	1,117
Effective income tax rate	39.1 %	37.4 %	40.2 %	41.2 %

The effective income tax rate for the three months ended June 27, 2016 includes the effect of an adjustment for a tax benefit shortfall created by share-based payments at settlement that were made during the period. The effective income tax rate for the three months ended June 29, 2015, includes the effect of a discrete adjustment for the accelerated vesting of restricted stock during the period.

The effective income tax rate for the six months ended June 27, 2016 includes the effect of an adjustment for a tax benefit shortfall created by share-based payments at settlement that were made during the period. The effective income tax rate for the six months ended June 29, 2015, includes the effect of a discrete adjustment for the accelerated vesting of restricted stock during the period.

Note 12 — Share-based Compensation

In May 2010, the Company's Board of Directors approved the 2010 Amended Management Incentive Plan (the "2010 Plan"). In May 2014, the Company's Board of Directors adopted the 2014 Equity Incentive Plan (the "2014 Plan," and together with the 2010 Plan, the "Incentive Plans"). The Incentive Plans reserve 2,116,747 common shares for equity incentive awards consisting of incentive stock options, non-qualified stock options, restricted stock awards and unrestricted stock awards. Equity incentive awards may be issued from either the 2014 Plan or the 2010 Plan.

Under the Incentive Plans, the Company has awarded 562,434 and 584,017 shares of restricted common stock to eligible employees as of June 27, 2016, and December 28, 2015, respectively. In addition, the Company has issued 1,213,151 and 1,076,555 stock options under the Incentive Plans to eligible employees as of June 27, 2016, and December 28, 2015, respectively.

During the three months ended March 28, 2016, the Company early adopted ASU 2016-09. As permitted under ASU 2016-09, the Company has elected to account for forfeitures in compensation cost when they occur in order to ease the administrative burden of estimating forfeitures. See Recent Accounting Pronouncements in Note 1 — Description of Business and Basis of Presentation for additional information.

Restricted common shares

Information with respect to restricted stock activity is as follows:

	Number of Shares of Restricted Common Stock		Weighted Average Sale/Grant Date Fair Value Per Share
	Time Vesting	Performance Vesting	
Unvested, December 28, 2015	49,513	186,515	$ 3.11
Granted	15,000	—	7.90
Vested	(9,764)	—	12.22
Repurchased	(15,086)	(18,858)	2.27
Unvested, June 27, 2016	39,663	167,657	$ 2.77

The weighted average fair value of share-based compensation awards granted and the fair values of awards granted and vested during the periods reported were as follows:

(in thousands, except per share amounts)	Three Months Ended		Six Months Ended	
	June 27, 2016	June 29, 2015	June 27, 2016	June 29, 2015

Weighted average grant date fair value per share	$7.90	$ 18.81	$7.90	$ 18.81
Total fair value of shares granted	119	90	119	90
Total fair value of shares vested	103	35	119	52

10

Table of Contents

Stock options

Information with respect to stock option activity is as follows:

	Number of Shares Subject to Options Time Vesting	Number of Shares Subject to Options Performance Vesting	Weighted Average Exercise Price Per Share	Weighted Average Remaining Contractual Term	Aggregate Intrinsic Value (thousands)
Outstanding, December 28, 2015	841,956	200,481	$ 11.55		
Granted	173,450	—	11.04		
Exercised	(26,644)	—	11.00		
Forfeited	(22,213)	(14,641)	11.44		
Outstanding, June 27, 2016	966,549	185,840	$ 11.49	8.2 years	$ —
Exercisable, June 27, 2016	506,017	—	$ 11.38	7.9 years	$ —

Fair value information for options granted and vested and the intrinsic value of options exercised during the periods reported are as follows:

(in thousands, except per share amounts)	Three Months Ended June 27, 2016	Three Months Ended June 29, 2015	Six Months Ended June 27, 2016	Six Months Ended June 29, 2015
Weighted average grant date fair value per share	$3.80	N/A	$3.70	$ 5.41
Total fair value of awards granted	13	N/A	642	1,039
Total fair value of awards vested	151	314	480	324
Total intrinsic value of options exercised	25	N/A	25	32

Compensation cost and valuation

Total compensation costs recognized in connection with the Incentive Plans during the periods reported were as follows:

(in thousands)	Three Months Ended June 27, 2016	Three Months Ended June 29, 2015	Six Months Ended June 27, 2016	Six Months Ended June 29, 2015
Stock compensation expense	$196	$ 500	$427	$ 656
Associated income tax benefits	71	166	143	218

As of June 27, 2016, the total unrecognized stock-based compensation expense was $2.7 million, with $2.0 million associated with time vesting awards and $0.7 million associated with performance vesting awards. The remaining weighted average contractual life for unrecognized stock-based compensation expense was 2.8 years as of June 27, 2016.

The fair value of the stock option awards granted during the periods reported was estimated using the Black-Scholes model with the following weighted-average assumptions:

	Three Months Ended June 27, 2016	Three Months Ended June 29, 2015	Six Months Ended June 27, 2016	Six Months Ended June 29, 2015
Risk free rate	1.7%	N/A	1.8%	1.9%
Expected volatility	30.4%	N/A	30.4%	37.9%
Expected term	6.3 years	N/A	6.3 years	6.3 years
Expected dividend yield	0.0%	N/A	0.0%	0.0%

Note 13 — Earnings per Share (EPS)

The number of shares and earnings per share (“EPS”) data for all periods presented are based on the historical weighted-average shares of common stock outstanding. Basic EPS is calculated by dividing income available to common stockholders by the weighted-average number of shares of common stock outstanding during each period. Diluted EPS is calculated using income available to common stockholders divided by diluted weighted-average shares of common stock outstanding during each period, which includes unvested restricted common stock and outstanding stock options. Diluted EPS considers the impact of potentially dilutive securities except in periods in which there is a loss because the inclusion of the potential common shares would have an anti-dilutive effect.

Table of Contents

The following table sets forth the computations of basic and dilutive EPS:

(in thousands, except per share data)	Three Months Ended June 27, 2016	Three Months Ended June 29, 2015	Six Months Ended June 27, 2016	Six Months Ended June 29, 2015
Earnings:				
Net income (loss)	$952	$(1,939)	$1,594	$ 657
Less: Net loss attributable to noncontrolling interests	—	500	—	500
Net income (loss) attributable to Papa Murphy's	952	(1,439)	1,594	1,157
Shares:				
Weighted average common shares outstanding	16,745	16,630	16,731	16,617
Dilutive effect of restricted equity awards (1)	22	—	30	256
Diluted weighted average number of shares outstanding	16,767	16,630	16,761	16,873
Earnings (loss) per share:				
Basic earnings (loss) per share	$0.06	$(0.09)	$0.10	$ 0.07
Diluted earnings (loss) per share	$0.06	$(0.09)	$0.10	$ 0.07

(1) The Company's potential common stock instruments such as stock options and restricted stock were not included in the computation of diluted EPS for the three months ended June 29, 2015, as the effect of including these shares in the calculation would have been anti-dilutive.

For the three months ended June 27, 2016, and June 29, 2015, an aggregated total of 491,000 shares and 390,000 shares, respectively, have been excluded from the diluted EPS calculation because their effect would have been anti-dilutive. For the six months ended June 27, 2016, and June 29, 2015, an aggregated total of 414,000 shares and 88,000 shares, respectively, have been excluded from the diluted EPS calculation because their effect would have been anti-dilutive.

Note 14 — Commitments and Contingencies

Operating lease commitments

The Company leases facilities and various office equipment under non-cancelable operating leases which expire through December 2025. Lease terms for its store units are generally for five years with renewal options and generally require the Company to pay a proportionate share of real estate taxes, insurance, common area maintenance and other operating costs.

The Company has entered into operating leases that it has subleased to three franchised stores. These operating leases have minimum base rent terms, contingent rent terms if individual franchised store sales exceed certain levels and have terms expiring on various dates from May 2020 to October 2020.

Lease guarantees

The Company is the guarantor for operating leases of 17 franchised stores that have terms expiring on various dates from August 2016 to April 2021. The obligations from these leases will generally continue to decrease over time as the leases expire. The applicable franchise owners continue to have primary liability for these operating leases. As of June 27, 2016, the Company does not believe it is probable it would be required to perform under the outstanding guarantees.

Legal proceedings

There have been no material developments in the legal proceedings described in Part II, Item 1, of the Company's Quarterly Report on Form 10-Q for the quarter ended March 28, 2016.

Note 15 — Related Party Transactions

Employee loans related to share purchases

In connection with share-based compensation, the Company previously made loans to certain non-officer employees of the Company (see Note 12 — Share-based Compensation). Loans made in connection with the issuance of the Company's equity are recognized in Stock subscriptions receivable as a reduction of total equity. As of June 27, 2016, the Company had no outstanding stock subscription receivables. As of December 28, 2015, the Company had stock subscription receivables of $0.1 million.

Note 16 — Segment Information

The Company has the following reportable segments: (i) Domestic Franchise; (ii) Domestic Company Stores; and (iii) International. The Domestic Franchise segment includes operations with respect to franchised stores in the United States and derives its revenues primarily from franchise and development fees and franchise royalties from franchised stores in the United States. The Domestic Company Stores segment includes operations with respect to Company-owned stores in the United States and derives its revenues from retail sales of pizza and side items to the general public. The International segment includes operations related to the Company’s operations outside the United States and derives its revenues from franchise and development fees and franchise royalties from franchised stores outside the United States.

Table of Contents

The following tables summarize information on profit or loss and assets for each of the Company's reportable segments:

(in thousands)	Three Months Ended June 27, 2016	Three Months Ended June 29, 2015	Six Months Ended June 27, 2016	Six Months Ended June 29, 2015
Revenues				
Domestic Franchise	$10,337	$10,878	$22,552	$22,813
Domestic Company Stores	19,470	18,156	40,144	35,323
International	87	87	183	154
Total	$29,894	$29,121	$62,879	$58,290
Segment Operating Income (Loss)				
Domestic Franchise	$4,455	$4,208	$8,282	$10,135
Domestic Company Stores	(716)	552	(808)	1,688
International	73	54	126	78
Corporate and unallocated	(999)	(2,226)	(2,464)	(3,965)
Total	$2,813	$2,588	$5,136	$7,936
Depreciation and amortization				
Domestic Franchise	$1,605	$1,288	$3,068	$2,589
Domestic Company Stores	1,305	1,124	2,546	2,135
International	5	8	16	15
Total	$2,915	$2,420	$5,630	$4,739

(in thousands)	June 27, 2016	December 28, 2015
Total Assets		
Domestic Franchise	$131,358	$ 139,705
Domestic Company Stores	51,052	45,217
International	379	438
Other [1]	89,237	90,111
Total	$272,026	$ 275,471

(1) Other assets which are not allocated to the individual segments primarily include trade names and trademarks and taxes receivable.

Item 2. Management's Discussion and Analysis of Financial Condition and Results of Operations

The following discussion and analysis of our financial condition and results of operations should be read in conjunction with the accompanying unaudited condensed consolidated financial statements and related notes in Item 1 and with the audited consolidated financial statements and the related notes included in our Annual Report on Form 10-K for the fiscal year ended December 28, 2015. To match our operating cycle, we use a 52- or 53-week fiscal year, ending on the Monday nearest to December 31. Our fiscal quarters each contain 13 operating weeks, with the exception of the fourth quarter of a 53-week fiscal year, which contains 14 operating weeks. Fiscal year 2016 is a 53-week period ending on January 2, 2017, and 2015 was a 52-week period ended on December 28, 2015.

Cautionary Note Regarding Forward-Looking Statements

In addition to historical information, this discussion and analysis contains forward-looking statements that involve risks and uncertainties. Our actual results may differ materially from those anticipated in these forward-looking statements as a result of certain factors including, but not limited to, those discussed in the sections entitled "Risk Factors" in our Annual Report on Form 10-K for the fiscal year ended December 28, 2015, as revised by risk factors disclosed under the section title "Risk Factors" in our Quarterly Report on Form 10-Q for the quarter ended March 28, 2016. All statements other than statements of historical fact or relating to present facts or current conditions included in this discussion and analysis are forward-looking statements. Forward-looking statements give our current expectations and projections relating to our financial condition, results of operations, plans, objectives, future performance and business. You can identify forward-looking statements by the fact that they do not relate strictly to historical or current facts. Examples of forward-looking statements include those regarding our future financial or operating results, cash flows, sufficiency of liquidity, financing resources, business strategies and priorities, resolution of litigation and claims, expectations for reducing operating costs through the use of our POS system terminals, expansion and growth opportunities, the number and mix of new store openings, exposure to foreign currency and interest rate risk, synergies and economies of scale resulting from acquisitions, the deductibility of goodwill for income tax purposes, as well as industry trends and outlooks. These statements may include words such as “anticipate,” “estimate,” “expect,” “project,” “plan,” “intend,” “believe,” “may,” “should,” “can have,” “likely” and other words and terms o meaning in connection with any discussion of the timing or nature of future operating or financial performance or other events.

The forward-looking statements contained in this discussion and analysis are based on assumptions that we have made in light of our industry experience and our perceptions of historical trends, current conditions, expected future developments and other factors we believe are appropriate in the circumstances. As you read and consider this discussion and analysis, you should understand that these statements are not guarantees of performance or results. They involve risks, uncertainties (many of which are beyond our control) and assumptions. Although we believe that these forward-looking statements are based on reasonable assumptions, you should be aware that many factors could affect our actual operating and financial performance and cause our performance to differ materially from the performance anticipated in the forward-looking statements. We believe these factors include, but are not limited to, those described under the section entitled “Risk Factors” in this Quarterly Report on Form 10-Q and in our Annual Report on Form 10-K for the fiscal year ended December 28, 2015, as revised by those described under the section entitled “Risk Factors” in our Quarterly Report on Form 10-Q for the fiscal quarter ended

Table of Contents

March 28, 2016. Should one or more of these risks or uncertainties materialize, or should any of these assumptions prove incorrect, our actual operating and financial performance may vary in material respects from expectations based on these forward-looking statements.

Any forward-looking statement made by us in this discussion and analysis speaks only as of the date on which we make it. Factors or events that could cause our actual operating and financial performance to differ may emerge from time to time, and it is not possible for us to predict all of them. We undertake no obligation to publicly update any forward-looking statement, whether as a result of new information, future developments or otherwise, except as may be required by law.

2016 Highlights

Revenue Growth

Total revenues for the three months ended June 27, 2016, compared to the three months ended June 29, 2015, grew 2.7% from $29.1 million to $29.9 million, and total revenues for the six months ended June 27, 2016, compared to the six months ended June 29, 2015, grew 7.9% from $58.3 million to $62.9 million, in each case, due primarily to the strategic acquisition of franchised stores and new store openings, partially offset by a decline in comparable store sales.

System-wide sales for the three months ended June 27, 2016, compared to the three months ended June 29, 2015, decreased 0.2% from $215.8 million to $215.3 million. System-wide sales for the six months ended June 27, 2016, compared to the six months ended June 29, 2015, increased 0.4% from $450.4 million to $452.1 million.

Comparable store sales in 2016 compared to 2015 for selected segments were as follows:

	Three Months Ended		Six Months Ended	
	June 27, 2016	June 29, 2015	June 27, 2016	June 29, 2015
Domestic Franchise	(3.7)%	4.5 %	(3.3)%	5.0 %
Domestic Company Stores	(6.6)%	4.9 %	(4.7)%	5.6 %
Total domestic stores	(4.0)%	4.5 %	(3.4)%	5.1 %

As of June 27, 2016, we had achieved positive comparable store sales growth in 42 of the last 50 quarters.

Comparable store sales for the three and six months ended June 27, 2016 were impacted by an increasingly competitive landscape, including significantly more aggressive value offerings across pizza and other food service, lower seasonal and absolute media levels, and the impact of shifting our marketing efforts to promote online ordering starting in March and extending into the current quarter.

Store Development

We and our franchise owners opened 28 stores, all in the United States, in the three months ended June 27, 2016. In the six months ended June 27, 2016, we and our franchise owners opened 55 stores, including 53 in the United States. While we plan to strategically expand our Company-owned store base in select markets, we may also refranchise select Company-owned stores over time as opportunities arise. We expect the majority of our new store expansion will continue to be from new franchised store openings.

Technology Investments

Our POS system is an important technology platform and tool for our future growth. Future precision marketing tools and mobile coupon capabilities necessitate POS system terminals in our stores. POS system terminals have been installed in nearly all stores as of June 27, 2016. We believe that an opportunity remains for many of our franchise owners to reduce their operating costs by increased utilization of the POS system. We continue to implement an integrated online ordering platform coupled with the latest version of our POS system software.

Table of Contents

Our Segments

We operate in three business segments: Domestic Franchise, Domestic Company Stores and International. Our Domestic Franchise segment consists of our domestic franchised stores, which represent the majority of our system-wide stores. Our Domestic Company Stores segment consists of our Company-owned stores in the United States. Our International segment consists of our stores outside of the United States, all of which are franchised. The following table sets forth our Revenues, Operating Income and Depreciation and amortization for each of our segments for the periods presented:

	Three Months Ended		Six Months Ended	
(in thousands)	June 27, 2016	June 29, 2015	June 27, 2016	June 29, 2015
Revenues				
Domestic Franchise	$10,337	$10,878	$22,552	$22,813
Domestic Company Stores	19,470	18,156	40,144	35,323
International	87	87	183	154
Total	$29,894	$29,121	$62,879	$58,290
Segment Operating Income (Loss)				
Domestic Franchise	$4,455	$4,208	$8,282	$10,135
Domestic Company Stores	(716)	552	(808)	1,688
International	73	54	126	78
Corporate and unallocated	(999)	(2,226)	(2,464)	(3,965)
Total	$2,813	$2,588	$5,136	$7,936
Depreciation and amortization				
Domestic Franchise	$1,605	$1,288	$3,068	$2,589
Domestic Company Stores	1,305	1,124	2,546	2,135
International	5	8	16	15
Total	$2,915	$2,420	$5,630	$4,739

Key Operating Metrics

We evaluate the performance of our business using a variety of operating and performance metrics. Set forth below is a description of our key operating metrics.

	Three Months Ended		Six Months Ended	
	June 27, 2016	June 29, 2015	June 27, 2016	June 29, 2015
Domestic store average weekly sales	$10,759	$11,342	$11,342	$11,868
Domestic comparable store sales	(4.0)%	4.5%	(3.4)%	5.1%
Domestic comparable stores	1,410	1,363	1,410	1,363
System-wide sales (in thousands)	$215,253	$215,752	$452,104	$450,385
System-wide stores	1,570	1,485	1,570	1,485
Adjusted EBITDA (in thousands)	$6,470	$6,432	$12,199	$14,447

Average Weekly Sales

Average Weekly Sales (“AWS”) consists of the average weekly sales of domestic franchised and Company-owned stores over a specified period of time. AWS is calculated by dividing the total net sales of our domestic system-wide stores for the relevant time period by the number of weeks those same stores were open during that time period. This measure allows management to assess changes in customer traffic and spending patterns at our domestic system-wide stores.

Comparable Store Sales

Comparable store sales represents the change in year-over-year sales for comparable stores. A comparable store is a store open for at least 52 full weeks from the comparable date (the Tuesday following the opening date). This measure highlights the performance of existing stores, while excluding the effect of newly opened or closed stores.

Comparable store sales reflects changes in the number of transactions and in customer spend per transaction at existing stores. Customer spend per transaction is affected by changes in menu prices, sales mix and the number of items sold per customer.

System-Wide Sales

System-wide sales include net sales by all of our system-wide stores. This measure allows management to assess the health of our brand, our relative position to competitors and changes in our revenues.

Store Openings, Closures, Acquisitions and Divestitures

We review the number of new stores, the number of closed stores, and the number of acquisitions and divestitures of stores to assess growth in system-wide sales, royalty revenues and Company-owned store sales. We operate through a footprint of 1,570 stores as of June 27, 2016, of which 90.1% are franchised,

Table of Contents

located in 38 states plus Canada and the Middle East. The following table presents the changes in the number of stores in our system for the six months ended June 27, 2016.

	Domestic Company Stores	Domestic Franchise	Total Domestic	International	Total
Store count at December 28, 2015	127	1,369	1,496	40	1,536
Openings	20	33	53	2	55
Closings	—	(18)	(18)	(3)	(21)
Net transfers [(1)]	9	(9)	—	—	—
Store count at June 27, 2016	156	1,375	1,531	39	1,570

(1) Net transfers are the number of franchised stores acquired by the Company, less the number of Company-owned stores refranchised.

EBITDA and Adjusted EBITDA

To supplement our condensed consolidated financial statements presented in accordance with generally accepted accounting principles in the U.S. (“GAAP”), we consider certain financial measures that are not prepared in accordance with GAAP. These non-GAAP financial measures are not based on any standardized methodology prescribed by GAAP and are not necessarily comparable to similarly-titled measures presented by other companies.

“Adjusted EBITDA” is calculated as net income (loss) before interest expense, income taxes, depreciation and amortization (“EBITDA”) as adjusted for:

all non-cash losses or expenses (including non-cash share-based compensation expenses and the non-cash portion of rent expenses relating to the difference between GAAP and cash rent expenses), excluding any non-cash loss or expense that is an accrual of a reserve for a cash expenditure or payment to be made, or anticipated to be made, in a future period;

non-cash gains on disposal of property and equipment;

non-recurring or unusual cash fees, costs, charges, losses and expenses;

fees, costs and expenses related to acquisitions; and

pre-opening costs with respect to new stores.

Adjusted EBITDA eliminates the effects of items that we do not consider indicative of our operating performance. Adjusted EBITDA is a supplemental measure of operating performance that does not represent and should not be considered as an alternative to net income (loss), as determined by GAAP, and our calculation of Adjusted EBITDA may not be comparable to that reported by other companies.

Adjusted EBITDA is a non-GAAP financial measure. Management believes that this financial measure, when viewed with our results of operations in accordance with GAAP and our reconciliation of Adjusted EBITDA to net income (loss), provides additional information to investors about certain material non-cash items and about unusual items that we do not expect to continue at the same level in the future. By providing this non-GAAP financial measure, we believe we are enhancing investors’ understanding of our business and our results of operations, as well as assisting investors in evaluating how well we are executing strategic initiatives. We believe Adjusted EBITDA is used by investors as a supplemental measure to evaluate the overall operating performance of companies in our industry.

Management uses Adjusted EBITDA and other similar measures:

in comparing our operating performance on a consistent basis;

to calculate incentive compensation for our employees;

for planning purposes, including the preparation of our internal annual operating budget; and

to evaluate the performance and effectiveness of our operational strategies.

Adjusted EBITDA has limitations as an analytical tool, and you should not consider it in isolation, or as a substitute for analysis of our results as reported under GAAP. Some of the limitations are:

Adjusted EBITDA does not reflect the significant interest expense, or the cash requirements necessary to service interest or principal payments, on our debt;

Adjusted EBITDA excludes pre-opening costs and non-cash GAAP rent expense with respect to new stores, which we will continue to incur in the future as we open new stores consistent with our growth strategy;

although depreciation and amortization are non-cash charges, the assets being depreciated and amortized may have to be replaced in the future, and Adjusted EBITDA does not reflect the cash requirements for such replacements; and Adjusted EBITDA does not reflect our tax expense or the cash requirements to pay our taxes.

To address these limitations, we reconcile Adjusted EBITDA to the most directly comparable GAAP measure, net income. Further, we also review GAAP measures and evaluate individual measures that are not included in Adjusted EBITDA.

The following table provides a reconciliation of our net income (loss) to Adjusted EBITDA for the periods presented:

Table of Contents

(in thousands)	Three Months Ended		Six Months Ended	
	June 27, 2016	June 29, 2015	June 27, 2016	June 29, 2015
Net Income (Loss)	$952	$(1,939)	$1,594	$657
Net loss attributable to noncontrolling interests	—	500	—	500
Net Income (Loss) Attributable to Papa Murphy's	952	(1,439)	1,594	1,157
Depreciation and amortization	2,915	2,420	5,630	4,739
Provision for (benefit from) income taxes	610	(1,160)	1,070	460
Interest expense, net	1,208	1,143	2,387	2,273
EBITDA	5,685	964	10,681	8,629
(Gain) loss on disposal of property and equipment (1)	(59)	3	(5)	62
Expenses not indicative of future operations:				
Secondary offering costs (2)	—	345	—	345
Loss on Project Pie impairment and disposal (3)	—	4,325	—	4,325
Transaction costs (4)	—	29	—	63
New store pre-opening expenses (5)	476	176	766	246
Non-cash expenses and non-income based state taxes (6)	368	590	757	777
Adjusted EBITDA	$6,470	$6,432	$12,199	$14,447

(1) Represents non-cash gains and losses resulting from disposal of property and equipment, including divested Company-owned stores.

(2) Represents offering costs related to the secondary offering of the Company's common stock.

(3) Represents a $4 million loss recognized upon impairment of Project Pie, a cost-method investment, and its subsequent disposal, and the write-off as bad debt receivables totaling $325,000.

(4) Represents transaction costs relating to the acquisition of multiple franchised stores.

(5) Represents expenses directly associated with the opening of new stores and incurred primarily in advance of the store opening, including wages, benefits and travel for training of opening teams, grand opening marketing costs and other store operating costs.

(6) Represents (i) non-cash expenses related to equity-based compensation; (ii) non-cash expenses related to the difference between GAAP and cash rent expense; and (iii) state revenue taxes levied in lieu of an income tax.

Table of Contents

Results of Operations

The following table sets forth our results of operations in dollars and as a percentage of total revenues for the three and six months ended June 27, 2016, and June 29, 2015.

	Three Months Ended				Six Months Ended			
	June 27, 2016		June 29, 2015		June 27, 2016		June 29, 2015	
(in thousands)	$	Total % of Revenues	$	Total % of Revenues	$	Total % of Revenues	$	Total % of Revenues
Revenues								
Franchise royalties	$9,538	32.0 %	$9,753	33.5 %	$20,034	31.9 %	$20,433	35.0 %
Franchise and development fees	574	1.9 %	830	2.9 %	1,528	2.4 %	1,970	3.4 %
Company-owned store sales	19,470	65.1 %	18,156	62.3 %	40,144	63.8 %	35,323	60.6 %
Other	312	1.0 %	382	1.3 %	1,173	1.9 %	564	1.0 %
Total revenues	29,894	100.0 %	29,121	100.0 %	62,879	100.0 %	58,290	100.0 %
Costs and Expenses								
Store operating costs:								
Cost of food and packaging (1)	6,781	22.7 %	6,443	22.1 %	14,053	22.3 %	12,533	21.5 %
Compensation and benefits (1)	5,577	18.7 %	4,722	16.2 %	11,311	18.0 %	9,076	15.6 %
Advertising (1)	1,897	6.3 %	1,753	6.0 %	4,063	6.5 %	3,422	5.9 %
Occupancy (1)	1,503	5.0 %	1,174	4.0 %	2,878	4.6 %	2,176	3.7 %
Other store operating costs (1)	2,555	8.5 %	1,856	6.4 %	4,846	7.7 %	3,301	5.7 %
Selling, general and administrative	5,912	19.8 %	8,162	28.0 %	14,967	23.8 %	15,045	25.8 %
Depreciation and amortization	2,915	9.8 %	2,420	8.3 %	5,630	9.0 %	4,739	8.1 %
(Gain) loss on disposal of property and equipment	(59)	(0.2)%	3	— %	(5)	— %	62	0.1 %
Total costs and expenses	27,081	90.6 %	26,533	91.1 %	57,743	91.8 %	50,354	86.4 %
Operating Income	2,813	9.4 %	2,588	8.9 %	5,136	8.2 %	7,936	13.6 %
Interest expense, net	1,208	4.0 %	1,143	3.9 %	2,387	3.8 %	2,273	3.9 %
Loss on impairment of investments	—	— %	4,500	15.5 %	—	— %	4,500	7.7 %
Other expense, net	43	0.1 %	44	0.2 %	85	0.1 %	46	0.1 %
Income (Loss) Before Income Taxes	1,562	5.2 %	(3,099)	(10.6)%	2,664	4.2 %	1,117	1.9 %
Provision for (benefit from) income taxes	610	2.0 %	(1,160)	(4.0)%	1,070	1.7 %	460	0.8 %
Net Income (Loss)	952	3.2 %	(1,939)	(6.7)%	1,594	2.5 %	657	1.1 %
Net loss attributable to noncontrolling interests	—	— %	500	1.7 %	—	— %	500	0.9 %
Net Income (Loss) Attributable to Papa Murphy’s	$952	3.2 %	$(1,439)	(4.9)%	$1,594	2.5 %	$1,157	2.0 %

(1) Please see the table presented in Costs and Expenses below, which presents Company-owned store expenses as a percentage of Company-owned store revenue for the three and six months ended June 27, 2016, and June 29, 2015.

Revenues

Total revenues. In the three months ended June 27, 2016, Total revenues grew primarily from the acquisition of franchised stores in 2015 by our Domestic Company Stores segment and net new store openings, partially offset by a decline in domestic comparable store sales of 4.0%. In the six months ended June 27, 2016, Total revenues grew primarily from the acquisition of franchised stores in 2015 by our Domestic Company Stores segment and net new store openings, partially offset by a decline in domestic comparable store sales of 3.4%.

Franchise royalties. Franchise royalties decreased in the three months ended June 27, 2016, compared to the three months ended June 29, 2015, primarily due to a decline in Domestic Franchise comparable store sales of 3.7%. These declines were offset, in part, by a 2.7% increase in royalties as a result of an increase of 42 franchised stores, net of

closures and transfers, since June 29, 2015.
Franchise royalties decreased in the six months ended June 27, 2016, compared to the six months ended June 29, 2015, primarily due to a decline in Domestic Franchise comparable store sales of 3.3%. These declines were offset, in part, by a 2.9% increase in royalties as a result of an increase of 33 franchised stores, net of closures and transfers, since December 29, 2014.
The decrease in Franchise royalties as a percentage of Total revenues for the three and six months ended June 27, 2016, compared to the three and six months ended June 29, 2015, was the result of increases in the number of Company-owned stores period over period.
Franchise and development fees. Franchise and development fees decreased in the three months ended June 27, 2016, compared to the three months ended June 29, 2015, due to a reduction in forfeited fees and transfer fees, partially offset by increased initial fees from opening six more franchised stores than in the comparative period.
Franchise and development fees decreased in the six months ended June 27, 2016, compared to the six months ended June 29, 2015, due to a reduction in forfeited fees and decreased initial fees from franchised store openings, partially offset by an increase in transfer fees.
Company-owned store sales. Company-owned store sales increased in the three months ended June 27, 2016, compared to the three months ended June 29, 2015, due to the acquisition of 11 stores from franchise owners and the opening of 31 Company-owned stores since June 29, 2015, partially offset

Table of Contents

by the divestiture of four stores since June 29, 2015 and a decline in comparable store sales of 6.6% in the three months ended June 27, 2016, compared to the three months ended June 29, 2015.

Company-owned store sales increased in the six months ended June 27, 2016, compared to the six months ended June 29, 2015, due to the acquisition of 32 stores from franchise owners and the opening of 38 Company-owned stores since December 29, 2014, partially offset by the divestiture of four stores and the closure of one store since December 29, 2014 and a decline in comparable store sales of 4.7% in the six months ended June 27, 2016, compared to the six months ended June 29, 2015.

Other. Other revenue decreased in the three months ended June 27, 2016, compared to the three months ended June 29, 2015, due to a decrease of $0.1 million from the resale of POS software licenses to franchise owners at cost. An equal and offsetting cost related to the resale of the POS software licenses is included in Selling, general and administrative expenses as discussed below.

Other revenue increased in the six months ended June 27, 2016, compared to the six months ended June 29, 2015, due to an increase of $0.4 million from the resale of POS software licenses to franchise owners at cost. An equal and offsetting cost related to the resale of the POS software licenses is included in Selling, general and administrative expenses as discussed below.

Costs and Expenses

Total costs and expenses. Total costs and expenses increased in the three and six months ended June 27, 2016, compared to the three and six months ended June 29, 2015, primarily as a result of the increase in the number of Company-owned stores period over period.

Store operating costs. Store operating costs as a percentage of total revenues increased in the three and six months ended June 27, 2016, compared to the three and six months ended June 29, 2015, primarily as a result of the increase in the number of Company-owned stores period over period, including many stores in less developed markets with lower average sales volumes.

The following table presents the components of Store operating costs as a percentage of Company-owned store sales for the periods reported:

	Three Months Ended		Six Months Ended	
	June 27, 2016	June 29, 2015	June 27, 2016	June 29, 2015
Store operating costs as a % of Company-owned store revenue:				
Cost of food and packaging	34.8%	35.5 %	35.0%	35.5 %
Compensation and benefits	28.6%	26.0 %	28.2%	25.7 %
Advertising	9.7 %	9.7 %	10.1%	9.7 %
Occupancy	7.7 %	6.5 %	7.2 %	6.2 %
Other store operating costs	13.3%	10.1 %	12.0%	9.3 %
Total store operating costs	94.1%	87.8 %	92.5%	86.4 %

Total store operating costs as a percentage of Company-owned store sales increased 630 basis points in the three months ended June 27, 2016, compared to the three months ended June 29, 2015, due primarily to the effect of store portfolio changes as we increased our Company-owned store ownership in less developed markets (as described in more detail below) and a decline in comparable store sales of 6.6% in the three months ended June 27, 2016, compared to the three months ended June 29, 2015. Additional factors during the comparable periods that increased Total store operating costs were pre-opening labor inefficiencies and lease expenses associated with new stores that generate below-average sales volumes.

Total store operating costs as a percentage of Company-owned store sales increased 610 basis points in the six months ended June 27, 2016, compared to the six months ended June 29, 2015, due primarily to the effect of store portfolio changes as we increased our Company-owned store ownership in less developed markets and a decline in comparable store sales of 4.7% in the six months ended June 27, 2016, compared to the six months ended June 29, 2015. Additional factors during the comparable periods that increased Total store operating costs were pre-opening labor

inefficiencies and lease expenses associated with new stores that generate below-average sales volumes.
Store Portfolio Changes. We acquired 32 stores from franchise owners, opened 38 new stores, closed one store and refranchised four stores since December 29, 2014. This shift in our store portfolio is the primary driver behind the increase in Total store operating costs as a percentage of Company-owned store sales for the three and six months ended June 27, 2016, compared to the three and six months ended June 29, 2015, because most of the stores acquired and all of the new stores opened have sales volumes currently lower than the average store sales for the rest of our portfolio.
Compensation and benefits. As we open or acquire stores in less developed markets with lower average sales volumes, we realize lower efficiencies in labor due to minimum labor demands for a store, regardless of volume. As we invest in these new stores and develop the markets, we expect AWS to grow and Compensation and benefits to approach that of our broader portfolio of stores. Compensation and benefits have also been impacted by the significant growth in new Company-owned stores, since labor costs for newly opened stores typically approach our portfolio average 12-18 months after a store is opened.
Other store operating costs. New store opening costs of $476,000 and $766,000 were recognized in Other store operating costs for the three and six months ended June 27, 2016, compared to $176,000 and $246,000 in the three and six months ended June 29, 2015. Opening costs have historically averaged around $40,000 per store with the majority of the costs incurred within two months of the store opening. In 2016, the Company had opened 20 new stores as of June 27, 2016, with more nearing completion. Excluding the impact of pre-opening costs in 2016, Other store operating costs as a percentage of Company-owned store sales would have been 10.7% and 10.2% for the three and six months ended June 27, 2016, respectively.
Selling, general and administrative. Selling, general and administrative costs decreased in the three months ended June 27, 2016, compared to the three months ended June 29, 2015, primarily due to year over year reductions of $1.0 million in compensation and benefits and $0.5 million in marketing expenses in excess of available funds in our advertising fund, partially offset by a year over year increase of $0.3 million in costs associated with our new e-commerce and online ordering platform.
Selling, general and administrative costs decreased in the six months ended June 27, 2016, compared to the six months ended June 29, 2015, primarily due to year over year reductions of $0.7 million in compensation and benefits, partially offset by year over year increases of $0.7 million in marketing expenses in excess of available funds in our advertising fund and $0.6 million in costs associated with our new e-commerce and online ordering platform.

Table of Contents

Depreciation and amortization. Depreciation and amortization increased in the three and six months ended June 27, 2016, compared to the three and six months ended June 29, 2015, due primarily to the depreciation associated with an increased number of Company-owned stores and increased capital expenditures for business technology projects.

Interest expense, net. Interest expense, net increased in the three and six months ended June 27, 2016, compared to the three and six months ended June 29, 2015, as a result of increased borrowing rates, partially offset by a reduction in long-term debt outstanding.

Income Taxes. The Provision for (benefit from) income taxes increased in the three and six months ended June 27, 2016, due primarily to a change in Income (Loss) Before Income Taxes.

The effective tax rate for the three months ended June 27, 2016, was 39.1% compared to 37.4% for the three months ended June 29, 2015. The effective tax rate increased primarily due to the effect of an adjustment for a tax benefit shortfall created by share-based payments at settlement. The effective tax rate for the six months ended June 27, 2016, was 40.2% compared to 41.2% for the six months ended June 29, 2015. The effective tax rate decreased primarily due to the effect in the prior year of a discrete adjustment for the accelerated vesting of restricted stock. Our income taxes have varied from what would be expected from the application of prevailing statutory rates mainly due to the impact of meal and entertainment expenses and share-based compensation expenses.

Segment Results

Domestic Franchise. Total revenues for the Domestic Franchise segment decreased $0.5 million in the three months ended June 27, 2016, compared to the three months ended June 29, 2015, due mainly to a period-over-period decline in comparable store sales of 3.7%. Total revenues for the Domestic Franchise segment decreased $0.3 million in the six months ended June 27, 2016, compared to the six months ended June 29, 2015, due to a period-over-period decline in segment comparable store sales of 3.3%, partially offset by increased revenue related to the POS system software licenses of $0.4 million.

Operating Income for the Domestic Franchise segment increased $0.2 million in the three months ended June 27, 2016, compared to the three months ended June 29, 2015, due to a $1.1 million decrease in Selling, general and administrative costs, partially offset by a $0.5 million decline in segment revenues. Operating Income for the Domestic Franchise segment decreased $1.9 million in the six months ended June 27, 2016, compared to the six months ended June 29, 2015, due to a $1.2 million increase in Selling, general and administrative costs, a $0.5 million increase in Depreciation and amortization and a $0.3 million decline in segment revenues.

Domestic Company Stores. Total revenues for the Domestic Company Stores segment increased $1.3 million in the three months ended June 27, 2016, compared to the three months ended June 29, 2015, as a result of the acquisition of 11 stores from franchise owners and the opening of 31 stores, partially offset by a period-over-period decline in comparable store sales of 6.6%. Total revenues for the Domestic Company Stores segment increased $4.8 million in the six months ended June 27, 2016, compared to the six months ended June 29, 2015, primarily due to the opening of 38 stores and the acquisition of 32 stores from franchise owners since December 29, 2014, partially offset by a period-over-period decline in comparable store sales of 4.7%, the refranchising of four stores and the closure of one store in the same period.

Operating (Loss) Income for the Domestic Company Stores segment decreased $1.3 million in the three months ended June 27, 2016, compared to the three months ended June 29, 2015, as a result of lower margins from stores acquired and newly opened in the past twelve months, most of which are in lesser developed markets, a period-over-period decline in comparable store sales of 6.6% and an increase in pre-opening costs of $0.3 million. Operating (Loss) Income for the segment decreased $2.5 million in the six months ended June 27, 2016, compared to the six months ended June 29, 2015, as a result of lower margins from stores acquired and newly opened in the past twelve months, most of which are in lesser developed markets, a period-over-period decline in comparable store sales of 4.7% and an increase in pre-opening costs of $0.5 million.

International. Total revenues for the International segment remained constant for the three months ended June 27, 2016, compared to the three months ended June 29, 2015. Total revenues for the segment increased for the six months ended June 27, 2016, compared to the six months ended June 29, 2015 primarily due to the opening of 11 net stores since December 29, 2014.

Operating Income for the International segment increased for the three months ended June 27, 2016, compared to the three months ended June 29, 2015, primarily due to the opening of five net stores since June 29, 2015. Operating Income for the International segment increased for the six months ended June 27, 2016, compared to the six months ended June 29, 2015, primarily due to the opening of 11 net stores since December 29, 2014.

Liquidity and Capital Resources

Our primary sources of liquidity are cash flows from operating activities and proceeds from the incurrence of debt, which together are sufficient to fund our operations, tax payments, capital expenditures, interest, fees and principal payments on our debt as well as support our growth strategy. If the need arises, we may seek additional funding. Our ability to obtain additional financing will depend on many factors, including prevailing market conditions, our financial condition and our ability to negotiate favorable terms and conditions. Financing may not be available on terms that are acceptable or favorable to us, if at all.

As of June 27, 2016, we had Cash and cash equivalents of $0.4 million and $20.0 million of available borrowings under a revolving credit facility, of which $3.0 million was drawn. As of June 27, 2016, we had $111.9 million of outstanding indebtedness. Principal payments under our Senior Credit Facility are due on the last day of each fiscal quarter through the life of the Senior Credit Facility. We believe that our cash flows from operations, available cash and cash equivalents and available borrowings under our revolving credit facility will be sufficient to meet our liquidity needs for at least the next 12 months.

As of June 27, 2016, we were in compliance with all of our covenants and other obligations under our Senior Credit Facility.

Table of Contents

Cash Flows

The following table presents a summary of cash flows from operating, investing and financing activities for the periods presented:

(in thousands)	Six Months Ended June 27, 2016	June 29, 2015
Cash flows from operating activities	$5,385	$9,730
Cash flows from investing activities	(11,809)	(12,895)
Cash flows from financing activities	(8)	(803)
Total cash flows	$(6,432)	$(3,968)

Cash Flows from Operating Activities

Net cash provided by operating activities of $5.4 million for the six months ended June 27, 2016, resulted primarily from net income of $1.6 million, adjusted for items such as depreciation and amortization and working capital changes. The $4.3 million decrease over the six months ended June 29, 2015 was primarily driven by a $4.0 million decrease in asset impairments and a net decrease of $1.1 million from changes in operating assets and liabilities, partially offset by a $0.9 million increase in net income.

Cash Flows from Investing Activities

Net cash used by investing activities was $11.8 million in the six months ended June 27, 2016, compared to net cash used of $12.9 million in the six months ended June 29, 2015. The $1.1 million decrease in cash used by investing activities was due primarily to a year over year decrease of $6.9 million for the acquisition of stores, partially offset by a year over year increase of $6.7 million in capital expenditures for property, plant, and equipment compared to the six months ended June 29, 2015.

Cash Flows from Financing Activities

Net cash used by financing activities was $8,000 in the six months ended June 27, 2016, compared to net cash used of $0.8 million in the six months ended June 29, 2015. The $0.8 million decrease in net cash used compared to the six months ended June 29, 2015 was primarily due to a net reduction in payments made on our outstanding long-term debt.

Critical Accounting Policies

Our discussion and analysis of our financial condition and results of operations are based upon our financial statements, which have been prepared in accordance with GAAP. The preparation of these financial statements requires us to make estimates and judgments that affect the reported amounts of assets, liabilities, revenues and expenses. On an ongoing basis, we evaluate our judgments and estimates including those related to revenue recognition, impairment of goodwill and intangible assets, income taxes, advertising expense and share-based compensation. We base our estimates on historical experience and on various other assumptions that are believed to be reasonable under the circumstances. Actual results may differ from these estimates under different assumptions or conditions.

The accounting policies we believe to be most critical to understanding our financial results and condition and that require complex and subjective management judgments and estimates are identified and described in our annual consolidated financial statements and the notes included in our Annual Report on Form 10-K.

JOBS Act

We qualify as an “emerging growth company” pursuant to the provisions of the Jumpstart Our Business Startup Act of 2012 (the “JOBS Act”). For as long as we are an “emerging growth company,” we may take advantage of certain exemptions from various reporting requirements that are applicable to other public companies that are not “emerging growth companies,” including, but not limited to, not being required to comply with the auditor attestation requirements of Section 404(b) of the Sarbanes-Oxley Act, reduced disclosure obligations regarding executive compensation in our periodic reports and proxy statements, reduced disclosure obligations relating to the presentation of financial statements in Management’s Discussion and Analysis of Financial Condition and Results of Operations, exemptions from the requirements of holding advisory “say-on-pay” votes on executive compensation and shareholder advisory votes on golden parachute compensation. We have availed ourselves of these reduced reporting and

disclosure requirements in our existing filings and expect to continue to avail ourselves of the reduced reporting and disclosure requirements available to emerging growth companies in future filings.
In addition, an emerging growth company can delay its adoption of certain accounting standards until those standards would otherwise apply to private companies. However, we are choosing to “opt out” of this extended transition period, and as a result, we plan to comply with any new or revised accounting standards on the relevant dates on which non-emerging growth companies must adopt the standards. Section 107 of the JOBS Act provides that our decision to opt out of the extended transition period for complying with new or revised accounting standards is irrevocable.

Table of Contents

Item 3. Quantitative and Qualitative Disclosures about Market Risk

Commodity Price Risk

We are exposed to market risks from changes in commodity prices. During the normal course of the year, we enter into national pricing commitments for cheese and other food products that are affected by changes in commodity prices and, as a result, our franchise and Company-owned stores are subject to volatility in food costs. We also maintain relationships with multiple suppliers for certain key products, such as cheese. We do not engage in speculative transactions nor do we hold or issue financial instruments for trading purposes. In instances when we use fixed pricing agreements with our suppliers, these agreements cover our physical commodity needs, are not net-settled and are accounted for as normal purchases.

Interest Rate Risk

We are subject to interest rate risk on indebtedness under our Senior Credit Facility. Interest rates on loans made under our Senior Credit Facility are based on LIBOR, and under specified circumstances we may be required by our lenders to enter into interest rate swap arrangements. A hypothetical 1.0% increase or decrease in the interest rate associated with our Senior Credit Facility would have resulted in a $1.1 million impact to interest expense on an annualized basis.

Foreign Currency Exchange Rate Risk

Our international franchise owners use the local currency as their functional currency. Royalty payments from our franchise owners in the Middle East are generally remitted to us in U.S. dollars and royalty payments from our Canadian franchise owners are generally remitted to us in Canadian dollars. Because our international activities do not account for a significant portion of our revenues, we believe our exposure to foreign currency risk is minimal.

Item 4. Controls and Procedures

Evaluation of Disclosure Controls and Procedures

Our management, with the participation of our Chief Executive Officer and Chief Financial Officer, has evaluated the effectiveness of our disclosure controls and procedures as of the end of the period covered by this report, pursuant to Rule 13a-15 under the Securities Exchange Act of 1934 (the “Exchange Act”). Based on that evaluation, our Chief Executive Officer and Chief Financial Officer concluded that, as of the end of the period covered by this report, our disclosure controls and procedures are effective to provide reasonable assurance that information we are required to disclose in reports that we file or submit under the Exchange Act is recorded, processed, summarized and reported within the time periods specified in SEC rules and forms, and that such information is accumulated and communicated to our management, including our Chief Executive Officer and Chief Financial Officer, as appropriate, to allow timely decisions regarding required disclosure.

Changes in Internal Control over Financial Reporting

There have been no changes in our internal control over financial reporting (as defined in Rule 13a-15(f) of the Exchange Act) that occurred during our last fiscal quarter that have materially affected, or are reasonably likely to materially affect, our internal control over financial reporting.

Table of Contents

PART II — OTHER INFORMATION

Item 1. Legal Proceedings

There have been no material developments in the legal proceedings described in Part II, Item 1, of our Quarterly Report on Form 10-Q for the quarter ended March 28, 2016.

Item 1A. Risk Factors

An investment in our common stock involves a high degree of risk. A detailed discussion of our risk factors is included under the section title “Risk Factors” on our Annual Report on Form 10-K for the fiscal year ended December 28, 2015, as revised by those risk factors disclosed under the section title “Risk Factors” in our Quarterly Report on Form 10-Q for the quarter ended March 28, 2016. Other than the revisions set forth in our Quarterly Report on Form 10-Q for the quarter ended March 28, 2016, 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 28, 2015. If any of these risks, as well as other risks and uncertainties that are not yet identified or that we currently think are immaterial, actually occur, our business, results of operations or financial condition could be materially and adversely affected. In such an event, the trading price of our common stock could decline and you could lose part or all of your investment. The risk factors and other information included in our Annual Report on Form 10-K for the year ended December 28, 2015, as revised by our Quarterly Report on Form 10-Q for the quarter ended March 28, 2016, should be carefully considered before making an investment decision relating to our common stock.

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

Repurchases of Common Stock

During the three months ended June 27, 2016, the Company repurchased the following shares:

	Total Number of Shares Purchased		Average Price Paid per Share	Total Number of Shares Purchased as Part of Publicly Announced Plans or Programs	Maximum Number of Shares that May Yet Be Purchased Under the Plans or Programs
March 29, 2016 to April 30, 2016	27,156	(1)	$ 2.60	—	N/A
May 1 to May 31, 2016	—		—	—	N/A
June 1 to June 27, 2016	—		—	—	N/A
Total	27,156		$ 2.60	—	N/A

(1) The Company repurchased unvested restricted shares from a former employee whose employment with the Company had terminated. The unvested shares were repurchased by the Company at the historical price paid by the former employee for the unvested shares.

Item 6. Exhibits.

Exhibit Number	Description of Exhibits
31.1*	Certification of the Chief Executive Officer Pursuant to Rule 13a-14(a) or 15d-14(a) of the Securities Exchange Act of 1934, as amended, as Adopted Pursuant to Section 302 of the Sarbanes-Oxley Act of 2002.
31.2*	Certification of the Chief Financial Officer Pursuant to Rule 13a-14(a) or 15d-14(a) of the Securities Exchange Act of 1934, as amended, as Adopted Pursuant to Section 302 of the Sarbanes-Oxley Act of 2002.
32.1*	Certificate of the Chief Executive Officer Pursuant to 18 U.S.C. Section 1350, as Adopted Pursuant to Section 906 of the Sarbanes-Oxley Act of 2002.
32.2*	

	Certificate of the Chief Financial Officer Pursuant to 18 U.S.C. Section 1350, as Adopted Pursuant to Section 906 of the Sarbanes-Oxley Act of 2002.
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

* Filed herewith

23

Table of Contents

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, hereunto duly authorized

PAPA MURPHY'S HOLDINGS, INC.

By: /s/ Mark Hutchens
Name: Mark Hutchens
Title: Chief Financial Officer

Date: August 3, 2016