

DENNYS CORP  
Form 10-Q  
November 01, 2016

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

FORM 10-Q

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

For the Quarterly Period Ended September 28, 2016

Commission File Number 0-18051  
DENNY'S CORPORATION  
(Exact name of registrant as specified in its charter)  
Delaware 13-3487402  
(State or other jurisdiction of (I.R.S. Employer  
incorporation or organization Identification No.)

203 East Main Street  
Spartanburg, South Carolina 29319-0001  
(Address of principal executive offices)  
(Zip Code)

(864) 597-8000  
(Registrant's telephone number, including area code)

Indicate by check mark whether the registrant (1) has filed all reports required to be filed by Section 13 or 15(d) of the Securities Exchange Act of 1934 during the preceding 12 months (or for such shorter period that the registrant was required to file such reports), and (2) has been subject to such filing requirements for the past 90 days.

Yes ☒ No ☐

Indicate by check mark whether the registrant has submitted electronically and posted on its corporate Web site, if any, every Interactive Data File required to be submitted and posted pursuant to Rule 405 of Regulation S-T during the preceding 12 months (or for such shorter period that the registrant was required to submit and post such files).

Yes ☒ No ☐

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

Large accelerated filer ☐ Accelerated filer ☐ Non-accelerated filer ☒ Smaller reporting company ☐

(Do not check if a smaller

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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 ☒

As of October 28, 2016, 73,366,890 shares of the registrant's common stock, par value \$0.01 per share, were outstanding.

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## PART I - FINANCIAL INFORMATION

## Item 1. Financial Statements

Denny's Corporation and Subsidiaries  
Condensed Consolidated Balance Sheets  
(Unaudited)

|                                                                                                                                                                                                             | September 28,<br>2016 | December 30,<br>2015 |
|-------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------|-----------------------|----------------------|
|                                                                                                                                                                                                             | (In thousands)        |                      |
| Assets                                                                                                                                                                                                      |                       |                      |
| Current assets:                                                                                                                                                                                             |                       |                      |
| Cash and cash equivalents                                                                                                                                                                                   | \$ 1,526              | \$ 1,671             |
| Receivables                                                                                                                                                                                                 | 14,175                | 16,552               |
| Inventories                                                                                                                                                                                                 | 3,009                 | 3,117                |
| Assets held for sale                                                                                                                                                                                        | —                     | 931                  |
| Prepaid and other current assets                                                                                                                                                                            | 7,170                 | 14,143               |
| Total current assets                                                                                                                                                                                        | 25,880                | 36,414               |
| Property, net of accumulated depreciation of \$252,981 and \$247,995, respectively                                                                                                                          | 131,537               | 124,816              |
| Goodwill                                                                                                                                                                                                    | 35,270                | 33,454               |
| Intangible assets, net                                                                                                                                                                                      | 53,897                | 46,074               |
| Deferred financing costs, net                                                                                                                                                                               | 2,084                 | 2,529                |
| Deferred income taxes                                                                                                                                                                                       | 23,083                | 29,159               |
| Other noncurrent assets                                                                                                                                                                                     | 25,981                | 24,591               |
| Total assets                                                                                                                                                                                                | \$ 297,732            | \$ 297,037           |
| Liabilities                                                                                                                                                                                                 |                       |                      |
| Current liabilities:                                                                                                                                                                                        |                       |                      |
| Current maturities of capital lease obligations                                                                                                                                                             | \$ 3,311              | \$ 3,246             |
| Accounts payable                                                                                                                                                                                            | 14,877                | 20,759               |
| Other current liabilities                                                                                                                                                                                   | 55,745                | 77,548               |
| Total current liabilities                                                                                                                                                                                   | 73,933                | 101,553              |
| Long-term liabilities:                                                                                                                                                                                      |                       |                      |
| Long-term debt, less current maturities                                                                                                                                                                     | 203,000               | 195,000              |
| Capital lease obligations, less current maturities                                                                                                                                                          | 22,227                | 17,499               |
| Liability for insurance claims, less current portion                                                                                                                                                        | 14,139                | 15,949               |
| Other noncurrent liabilities                                                                                                                                                                                | 38,185                | 27,631               |
| Total long-term liabilities                                                                                                                                                                                 | 277,551               | 256,079              |
| Total liabilities                                                                                                                                                                                           | 351,484               | 357,632              |
| Commitments and contingencies                                                                                                                                                                               |                       |                      |
| Shareholders' equity (deficit)                                                                                                                                                                              |                       |                      |
| Common stock \$0.01 par value; shares authorized - 135,000; September 28, 2016: 107,020 shares issued and 73,977 shares outstanding; December 30, 2015: 106,521 shares issued and 76,862 shares outstanding | \$ 1,070              | \$ 1,065             |
| Paid-in capital                                                                                                                                                                                             | 582,864               | 565,364              |
| Deficit                                                                                                                                                                                                     | (394,117 )            | (402,245 )           |
| Accumulated other comprehensive loss, net of tax                                                                                                                                                            | (9,808 )              | (23,777 )            |

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|                                                                 |            |            |
|-----------------------------------------------------------------|------------|------------|
| Shareholders' equity before treasury stock                      | 180,009    | 140,407    |
| Treasury stock, at cost, 33,043 and 29,659 shares, respectively | (233,761 ) | (201,002 ) |
| Total shareholders' deficit                                     | (53,752 )  | (60,595 )  |
| Total liabilities and shareholders' deficit                     | \$297,732  | \$ 297,037 |
| See accompanying notes                                          |            |            |

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Denny's Corporation and Subsidiaries  
Condensed Consolidated Statements of Income  
(Unaudited)

|                                                  | Quarter Ended<br>September 30,<br>2016 |           | Three Quarters Ended<br>September 30,<br>2016 |            |
|--------------------------------------------------|----------------------------------------|-----------|-----------------------------------------------|------------|
|                                                  | 2015                                   |           | 2015                                          |            |
| (In thousands, except per share amounts)         |                                        |           |                                               |            |
| Revenue:                                         |                                        |           |                                               |            |
| Company restaurant sales                         | \$93,122                               | \$ 89,279 | \$272,718                                     | \$ 263,890 |
| Franchise and license revenue                    | 35,264                                 | 34,499    | 104,625                                       | 103,378    |
| Total operating revenue                          | 128,386                                | 123,778   | 377,343                                       | 367,268    |
| Costs of company restaurant sales:               |                                        |           |                                               |            |
| Product costs                                    | 22,819                                 | 23,289    | 67,253                                        | 66,609     |
| Payroll and benefits                             | 35,999                                 | 34,249    | 104,548                                       | 101,118    |
| Occupancy                                        | 4,928                                  | 5,164     | 14,721                                        | 14,972     |
| Other operating expenses                         | 13,372                                 | 12,388    | 37,544                                        | 36,019     |
| Total costs of company restaurant sales          | 77,118                                 | 75,090    | 224,066                                       | 218,718    |
| Costs of franchise and license revenue           | 10,275                                 | 10,649    | 31,037                                        | 32,843     |
| General and administrative expenses              | 17,558                                 | 16,008    | 50,691                                        | 49,771     |
| Depreciation and amortization                    | 5,609                                  | 5,422     | 16,207                                        | 15,760     |
| Operating (gains), losses and other charges, net | 249                                    | 886       | 24,365                                        | 1,722      |
| Total operating costs and expenses, net          | 110,809                                | 108,055   | 346,366                                       | 318,814    |
| Operating income                                 | 17,577                                 | 15,723    | 30,977                                        | 48,454     |
| Interest expense, net                            | 3,117                                  | 2,327     | 8,905                                         | 6,678      |
| Other nonoperating (income) expense, net         | (543)                                  | ) 592     | (635)                                         | ) 538      |
| Net income before income taxes                   | 15,003                                 | 12,804    | 22,707                                        | 41,238     |
| Provision for income taxes                       | 5,277                                  | 3,854     | 14,579                                        | 14,021     |
| Net income                                       | \$9,726                                | \$ 8,950  | \$8,128                                       | \$ 27,217  |
| Basic net income per share                       | \$0.13                                 | \$ 0.11   | \$0.11                                        | \$ 0.32    |
| Diluted net income per share                     | \$0.13                                 | \$ 0.11   | \$0.10                                        | \$ 0.32    |
| Basic weighted average shares outstanding        | 74,851                                 | 82,923    | 76,214                                        | 83,952     |
| Diluted weighted average shares outstanding      | 76,791                                 | 85,056    | 78,052                                        | 86,067     |

See accompanying notes

Denny's Corporation and Subsidiaries  
Condensed Consolidated Statements of Comprehensive Income  
(Unaudited)

|                                                                                                                     | Quarter Ended      |                    | Three Quarters Ended |                    |
|---------------------------------------------------------------------------------------------------------------------|--------------------|--------------------|----------------------|--------------------|
|                                                                                                                     | September 28, 2016 | September 30, 2015 | September 28, 2016   | September 30, 2015 |
|                                                                                                                     | (In thousands)     |                    |                      |                    |
| Net income                                                                                                          | \$9,726            | \$ 8,950           | \$8,128              | \$ 27,217          |
| Other comprehensive income, net of tax:                                                                             |                    |                    |                      |                    |
| Minimum pension liability adjustment, net of tax of \$8, \$169, \$2,168 and \$507                                   | 13                 | 265                | 21,851               | 793                |
| Recognition of unrealized gain (loss) on hedge transactions, net of tax of \$20, \$(2,266), \$(5,034) and \$(1,303) | 32                 | (3,542)            | (7,882)              | (2,037)            |
| Other comprehensive income (loss)                                                                                   | 45                 | (3,277)            | 13,969               | (1,244)            |
| Total comprehensive income                                                                                          | \$9,771            | \$ 5,673           | \$22,097             | \$ 25,973          |

See accompanying notes

Denny's Corporation and Subsidiaries  
Condensed Consolidated Statement of Shareholders' Deficit  
(Unaudited)

|                                                       | Common Stock   |          | Treasury Stock |             | Paid-in   | Deficit     | Accumulated                   | Total                 |
|-------------------------------------------------------|----------------|----------|----------------|-------------|-----------|-------------|-------------------------------|-----------------------|
|                                                       | Shares         | Amount   | Shares         | Amount      | Capital   |             | Other Comprehensive Loss, Net | Shareholders' Deficit |
|                                                       | (In thousands) |          |                |             |           |             |                               |                       |
| Balance, December 30, 2015                            | 106,521        | \$ 1,065 | (29,659)       | \$(201,002) | \$565,364 | \$(402,245) | \$ (23,777 )                  | \$ (60,595 )          |
| Net income                                            | —              | —        | —              | —           | —         | 8,128       | —                             | 8,128                 |
| Other comprehensive income                            | —              | —        | —              | —           | —         | —           | 13,969                        | 13,969                |
| Share-based compensation on equity classified awards  | —              | —        | —              | —           | 4,212     | —           | —                             | 4,212                 |
| Purchase of treasury stock                            | —              | —        | (1,866 )       | (19,648 )   | —         | —           | —                             | (19,648 )             |
| Equity forward contract settlement                    | —              | —        | (1,518 )       | (13,111 )   | 13,111    | —           | —                             | —                     |
| Issuance of common stock for share-based compensation | 383            | 4        | —              | —           | (4 )      | —           | —                             | —                     |
| Exercise of common stock options                      | 116            | 1        | —              | —           | 491       | —           | —                             | 492                   |
| Tax expense from share-based compensation             | —              | —        | —              | —           | (310 )    | —           | —                             | (310 )                |
| Balance, September 28, 2016                           | 107,020        | \$ 1,070 | (33,043)       | \$(233,761) | \$582,864 | \$(394,117) | \$ (9,808 )                   | \$ (53,752 )          |

See accompanying notes



Denny's Corporation and Subsidiaries  
Condensed Consolidated Statements of Cash Flows  
(Unaudited)

|                                                                                     | Three Quarters Ended<br>September 28, 2016<br>(In thousands) | September 30, 2015 |
|-------------------------------------------------------------------------------------|--------------------------------------------------------------|--------------------|
| Cash flows from operating activities:                                               |                                                              |                    |
| Net income                                                                          | \$ 8,128                                                     | \$ 27,217          |
| Adjustments to reconcile net income to cash flows provided by operating activities: |                                                              |                    |
| Depreciation and amortization                                                       | 16,207                                                       | 15,760             |
| Operating (gains), losses and other charges, net                                    | 24,365                                                       | 1,722              |
| Amortization of deferred financing costs                                            | 445                                                          | 366                |
| (Gain) loss on early extinguishments of debt                                        | (3 )                                                         | 260                |
| Deferred income tax expense                                                         | 8,942                                                        | 9,013              |
| Share-based compensation                                                            | 5,625                                                        | 5,505              |
| Tax expense from share-based compensation                                           | (310 )                                                       | —                  |
| Changes in assets and liabilities:                                                  |                                                              |                    |
| Decrease (increase) in assets:                                                      |                                                              |                    |
| Receivables                                                                         | 2,582                                                        | 4,626              |
| Inventories                                                                         | 108                                                          | 44                 |
| Other current assets                                                                | 6,972                                                        | (358 )             |
| Other assets                                                                        | (1,800 )                                                     | 726                |
| Increase (decrease) in liabilities:                                                 |                                                              |                    |
| Accounts payable                                                                    | (83 )                                                        | 1,134              |
| Accrued salaries and vacations                                                      | (11,006 )                                                    | (2,278 )           |
| Accrued taxes                                                                       | 1,647                                                        | 1,389              |
| Other accrued liabilities                                                           | (16,627 )                                                    | (6,655 )           |
| Other noncurrent liabilities                                                        | (2,060 )                                                     | (1,544 )           |
| Net cash flows provided by operating activities                                     | 43,132                                                       | 56,927             |
| Cash flows from investing activities:                                               |                                                              |                    |

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|                                                        |          |   |          |   |
|--------------------------------------------------------|----------|---|----------|---|
| Capital expenditures                                   | (14,615  | ) | (18,432  | ) |
| Acquisition of<br>restaurants and real<br>estate       | (12,956  | ) | (2,330   | ) |
| Proceeds from<br>disposition of property               | 1,921    |   | —        |   |
| Collections on notes<br>receivable                     | 1,151    |   | 1,359    |   |
| Issuance of notes<br>receivable                        | (1,394   | ) | (1,151   | ) |
| Net cash flows used in<br>investing activities         | (25,893  | ) | (20,554  | ) |
| Cash flows from<br>financing activities:               |          |   |          |   |
| Revolver borrowings                                    | 38,000   |   | 167,500  |   |
| Revolver payments                                      | (30,000  | ) | (102,750 | ) |
| Long-term debt<br>payments                             | (2,378   | ) | (57,486  | ) |
| Proceeds from exercise<br>of stock options             | 492      |   | 471      |   |
| Tax withholding on<br>share-based payments             | —        |   | (982     | ) |
| Tax benefit from<br>share-based<br>compensation        | —        |   | 976      |   |
| Deferred financing costs                               | —        |   | (1,265   | ) |
| Purchase of treasury<br>stock                          | (19,137  | ) | (37,310  | ) |
| Net bank overdrafts                                    | (4,361   | ) | —        |   |
| Net cash flows used in<br>financing activities         | (17,384  | ) | (30,846  | ) |
| Increase (decrease) in<br>cash and cash<br>equivalents | (145     | ) | 5,527    |   |
| Cash and cash<br>equivalents at beginning<br>of period | 1,671    |   | 3,074    |   |
| Cash and cash<br>equivalents at end of<br>period       | \$ 1,526 |   | \$ 8,601 |   |

See accompanying notes

Denny's Corporation and Subsidiaries  
Notes to Condensed Consolidated Financial Statements  
(Unaudited)

Note 1. Introduction and Basis of Presentation

Denny's Corporation, or Denny's, is one of America's largest full-service restaurant chains based on number of restaurants. At September 28, 2016, the Denny's brand consisted of 1,728 restaurants, 1,560 of which were franchised/licensed restaurants and 168 of which were company operated.

Our unaudited condensed consolidated financial statements have been prepared pursuant to the rules and regulations of the Securities and Exchange Commission. Therefore, certain information and notes normally included in financial statements prepared in accordance with U.S. generally accepted accounting principles have been condensed or omitted. In our opinion, all adjustments considered necessary for a fair presentation of the interim periods presented have been included. Such adjustments are of a normal and recurring nature. The preparation of these financial statements requires us to make estimates and judgments that affect the reported amounts of assets, liabilities, revenues and expenses, and related disclosure of contingent assets and liabilities. Actual results may differ from these estimates under different assumptions or conditions; however, we believe that our estimates, including those for the above-described items, are reasonable.

These interim condensed consolidated financial statements should be read in conjunction with our consolidated financial statements and notes thereto for the year ended December 30, 2015 and the related Management's Discussion and Analysis of Financial Condition and Results of Operations, both of which are contained in our Annual Report on Form 10-K for the fiscal year ended December 30, 2015. The results of operations for the interim periods presented are not necessarily indicative of the results for the entire fiscal year ending December 28, 2016.

Note 2. Summary of Significant Accounting Policies

Newly Adopted Accounting Standards

Consolidation

ASU 2015-02,"Consolidation (Topic 810): Amendments to the Consolidation Analysis"

Effective December 31, 2015, we adopted ASU 2015-02, which improves targeted areas of the consolidation guidance and reduces the number of consolidation models. The adoption of this guidance did not have a material impact on our consolidated financial statements.

Debt Issuance

ASU 2015-03,"Interest—Imputation of Interest (Subtopic 835-30): Simplifying the Presentation of Debt Issuance Costs" and ASU 2015-15,"Interest—Imputation of Interest (Subtopic 835-30): Presentation and Subsequent Measurement of Debt Issuance Costs Associated with Line-of-Credit Arrangements—Amendments to SEC Paragraphs Pursuant to Staff Announcement at June 18, 2015 EITF Meeting (SEC Update)"

Effective December 31, 2015, we adopted ASU 2015-03, which simplifies the guidance on the presentation of debt issuance costs. The new guidance requires debt issuance costs to be presented in the balance sheet as a reduction of the related debt liability rather than as an asset. Also effective December 31, 2015, we adopted ASU 2015-15, which addresses the SEC's comments related to the absence of authoritative guidance within ASU 2015-03 related to

line-of-credit arrangements. According to this guidance, the SEC will not object to an entity deferring and presenting debt issuance costs as an asset and subsequently amortizing the deferred debt issuance costs ratably over the term of the line-of-credit arrangement, regardless of whether there are any outstanding borrowings on the line-of-credit arrangement. The adoption of this guidance did not have any impact on our consolidated financial statements and we will continue to classify debt issuance costs as an asset.

## Intangibles

ASU 2015-05, "Intangibles—Goodwill and Other—Internal-Use Software (Subtopic 350-40): Customer's Accounting for Fees Paid in a Cloud Computing Arrangement"

Effective December 31, 2015, we adopted, on a prospective basis, ASU 2015-05, which provides guidance about whether a cloud computing arrangement includes a software license. If a software license is included, the customer should account for the license consistent with the acquisition of other software licenses. If a software license is not included, the arrangement should be accounted for as a service contract. The adoption of this guidance did not have a material impact on our consolidated financial statements.

## Inventory

ASU 2015-11, "Inventory (Topic 330): Simplifying the Measurement of Inventory"

Effective December 31, 2015, we adopted ASU 2015-11, which requires inventory that is measured using the first-in, first-out method to be measured at the lower of cost and net realizable value. Net realizable value is defined as the estimated selling prices in the ordinary course of business, less reasonably predictable costs of completion, disposal, and transportation. The adoption of this guidance did not have a material impact on our consolidated financial statements.

## Derivatives

ASU 2016-05, "Derivatives and Hedging (Topic 815): Effect of Derivative Contract Novations on Existing Hedge Accounting Relationships (a consensus of the Emerging Issues Task Force)"

In March 2016, the FASB issued ASU 2016-05, which clarifies that a change in the counterparty to a derivative instrument that has been designated as the hedging instrument under Topic 815 does not, in and of itself, require dedesignation of that hedging relationship provided that all other hedge accounting criteria continue to be met. We early adopted this guidance as of March 30, 2016 on a prospective basis. The adoption of this guidance did not have any impact on our consolidated financial statements.

## Accounting Standards to be Adopted

### Revenue Recognition

ASU 2014-09, "Revenue from Contracts with Customers (Topic 606)",  
ASU 2015-14, "Revenue from Contracts with Customers (Topic 606): Deferral of the Effective Date",  
ASU 2016-08, "Revenue from Contracts with Customers (Topic 606): Principal versus Agent Considerations (Reporting Revenue Gross versus Net",  
ASU 2016-10, "Revenue from Contracts with Customers (Topic 606): Identifying Performance Obligations and Licensing" and  
ASU 2016-12, "Revenue from Contracts with Customers (Topic 606): Narrow-Scope Improvements and Practical Expedients"

In May 2014, the FASB issued ASU 2014-09, which clarifies the principles used to recognize revenue for all entities. The new guidance requires companies to recognize revenue when it transfers goods or service to a customer in an amount that reflects the consideration to which a company expects to be entitled. In August 2015, the FASB issued ASU 2015-14, which defers the effective date for ASU 2014-09. The guidance is now effective for annual and interim periods beginning after December 15, 2017 (our fiscal 2018). The guidance allows for either a retrospective or

cumulative effect transition method. Early application is permitted only as of annual reporting periods beginning after December 15, 2016, including interim reporting periods within that reporting period.

In March 2016, the FASB issued ASU 2016-08, which clarifies the implementation guidance provided in ASU 2014-09 on principal versus agent considerations. In April 2016, the FASB issued ASU 2016-10, which clarifies the implementation guidance in ASU 2014-09 on licensing and identifying performance obligations. In May 2016, the FASB issued ASU 2016-12, which provides clarifying guidance and adds some practical expedients in the areas of assessing collectability, presentation of sales taxes received from customers, noncash consideration, contract modification and clarification of using the full retrospective approach to adopt ASU 2014-09. These three new ASUs must be adopted concurrently with ASU 2014-09. The guidance is not expected to impact the recognition of company restaurant sales or royalties from franchised restaurants. We are currently evaluating the impact this guidance will have on the recognition of other transactions on our consolidated financial statements and related disclosures and have not yet selected a transition method.

#### Financial Instruments

ASU 2016-01, "Financial Instruments—Overall (Subtopic 825-10): Recognition and Measurement of Financial Assets and Financial Liabilities"

In January 2016, the FASB issued ASU 2016-01, which requires equity investments (except those accounted for under the equity method of accounting, or those that result in consolidation of the investee) to be measured at fair value with changes in fair value recognized in net income, requires public business entities to use the exit price notion when measuring the fair value of financial instruments for disclosure purposes, requires separate presentation of financial assets and financial liabilities by measurement category and form of financial asset, and eliminates the requirement for public business entities to disclose the method(s) and significant assumptions used to estimate the fair value that is required to be disclosed for financial instruments measured at amortized cost. ASU 2016-01 is effective for annual and interim periods beginning after December 15, 2017 (our fiscal 2018) with early adoption permitted. We are currently evaluating the impact the adoption of this guidance will have on our consolidated financial statements.

ASU 2016-13, "Financial Instruments—Credit Losses (Topic 326): Measurement of Credit Losses on Financial Instruments"

In June 2016, the FASB issued ASU 2016-13, which replaces the incurred loss impairment methodology in current GAAP with a methodology that reflects expected credit losses and requires consideration of a broader range of reasonable and supportable information to inform financial statement users of credit loss estimates. ASU 2016-13 is effective for annual and interim periods beginning after December 15, 2019 (our fiscal 2020) with early adoption permitted for annual and interim periods beginning after December 15, 2018 (our fiscal 2019). We do not expect the adoption of this guidance to have a material impact on our consolidated financial statements.

#### Leases

ASU 2016-02, "Leases (Topic 842)"

In February 2016, the FASB issued ASU 2016-02, which provides guidance for accounting for leases. The new guidance requires companies to recognize the assets and liabilities for the rights and obligations created by leased assets. The accounting guidance for lessors is largely unchanged. ASU 2016-02 is effective for annual and interim periods beginning after December 15, 2018 (our fiscal 2019) with early adoption permitted. The guidance will be adopted using a modified retrospective approach. We are currently evaluating the impact the adoption of this guidance will have on our consolidated financial statements, but expect the adoption will result in a significant increase in the assets and liabilities on our consolidated balance sheet.





## Stock Compensation

ASU 2016-09, "Compensation - Stock Compensation (Topic 718): Improvements to Employee Share-Based Payment Accounting"

In March 2016, the FASB issued ASU 2016-09, which simplifies several aspects of the accounting for share-based payment transactions, including the recognition of excess tax benefits and deficiencies, the classification of those excess tax benefits on the statement of cash flows, an accounting policy election for forfeitures, the amount an employer can withhold to cover income taxes and still qualify for equity classification and the classification of those taxes paid on the statement of cash flows. ASU 2016-09 is effective for annual and interim periods beginning after December 15, 2016 (our fiscal 2017) with early adoption permitted. The guidance will be applied either prospectively, retrospectively or using a modified retrospective transition method, depending on the area covered in this update. We are currently evaluating the impact the adoption of this guidance will have on our consolidated financial statements.

## Statement of Cash Flows

ASU 2016-15, "Statement of Cash Flows (Topic 230): Classification of Certain Cash Receipts and Cash Payments (a consensus of the Emerging Issues Task Force)"

In August 2016, the FASB issued ASU 2016-15, which addresses eight specific cash flow issues with the objective of reducing the existing diversity in practice. ASU 2016-15 is effective for annual and interim periods beginning after December 15, 2017 (our fiscal 2018) with early adoption permitted. The guidance is to be applied using a retrospective transition method to each period presented. We do not expect the adoption of this guidance to have a material impact on our consolidated financial statements.

We reviewed all other newly issued accounting pronouncements and concluded that they are either not applicable to our business or are not expected to have a material effect on our consolidated financial statements as a result of future adoption.

## Note 3. Receivables

Receivables were comprised of the following:

|                                                                         | September 28,<br>2016 | December 30,<br>2015 |
|-------------------------------------------------------------------------|-----------------------|----------------------|
|                                                                         | (In thousands)        |                      |
| Current assets:                                                         |                       |                      |
| Receivables:                                                            |                       |                      |
| Trade accounts receivable from franchisees                              | \$ 10,064             | \$ 10,591            |
| Notes receivable from franchisees                                       | 1,557                 | 1,352                |
| Vendor receivables                                                      | 1,454                 | 3,049                |
| Credit card receivables                                                 | 1,141                 | 1,606                |
| Other                                                                   | 239                   | 251                  |
| Allowance for doubtful accounts                                         | (280 )                | (297 )               |
| Total current receivables, net                                          | \$ 14,175             | \$ 16,552            |
| Noncurrent assets (included as a component of other noncurrent assets): |                       |                      |
| Notes receivable from franchisees                                       | \$ 579                | \$ 541               |



## Note 4. Goodwill and Other Intangible Assets

The following table reflects the changes in carrying amounts of goodwill.

|                                                                          | (In<br>thousands) |
|--------------------------------------------------------------------------|-------------------|
| Balance, December 30, 2015                                               | \$ 33,454         |
| Additions related to acquisition                                         | 1,827             |
| Write-offs and reclassifications associated with the sale of restaurants | (11 )             |
| Balance, September 28, 2016                                              | \$ 35,270         |

Other intangible assets were comprised of the following:

|                                          | September 28, 2016          |                             | December 30, 2015           |                             |
|------------------------------------------|-----------------------------|-----------------------------|-----------------------------|-----------------------------|
|                                          | Gross<br>Carrying<br>Amount | Accumulated<br>Amortization | Gross<br>Carrying<br>Amount | Accumulated<br>Amortization |
|                                          | (In thousands)              |                             |                             |                             |
| Intangible assets with indefinite lives: |                             |                             |                             |                             |
| Trade names                              | \$44,077                    | \$ —                        | \$44,068                    | \$ —                        |
| Liquor licenses                          | 166                         | —                           | 126                         | —                           |
| Intangible assets with definite lives:   |                             |                             |                             |                             |
| Franchise and license agreements         | 3,765                       | 3,712                       | 12,237                      | 12,026                      |
| Reacquired franchise rights              | 10,496                      | 895                         | 2,823                       | 1,154                       |
| Intangible assets                        | \$58,504                    | \$ 4,607                    | \$59,254                    | \$ 13,180                   |

During the three quarters ended September 28, 2016, we acquired nine franchised restaurants for \$12.4 million, of which \$8.5 million was allocated to reacquired franchise rights, \$2.0 million to property and \$1.8 million to goodwill. The \$8.5 million decrease in gross franchise and license agreements during the three quarters ended September 28, 2016 primarily resulted from the removal of fully amortized agreements.

## Note 5. Other Current Liabilities

Other current liabilities consisted of the following:

|                                                                                | September 28,<br>2016 | December 30,<br>2015 |
|--------------------------------------------------------------------------------|-----------------------|----------------------|
|                                                                                | (In thousands)        |                      |
| Accrued salaries and vacation                                                  | \$22,871              | \$ 30,549            |
| Accrued insurance, primarily current portion of liability for insurance claims | 6,545                 | 7,076                |
| Accrued taxes                                                                  | 8,958                 | 7,311                |
| Accrued advertising                                                            | 3,919                 | 7,737                |
| Accrued pension                                                                | 355                   | 9,648                |
| Gift cards                                                                     | 3,923                 | 4,611                |
| Other                                                                          | 9,174                 | 10,616               |
| Other current liabilities                                                      | \$55,745              | \$ 77,548            |



# Note 6. Operating (Gains), Losses and Other Charges, Net

Operating (gains), losses and other charges, net are comprised of the following:

|                                                  | Quarter Ended  |        | Three Quarters Ended |          |
|--------------------------------------------------|----------------|--------|----------------------|----------|
|                                                  | September 28,  |        | September 28,        |          |
|                                                  | 2016           | 2015   | 2016                 | 2015     |
|                                                  | (In thousands) |        |                      |          |
| Pension settlement loss                          | \$—            | \$ —   | \$24,297             | \$ —     |
| Gains on sales of assets and other, net          | (77 )          | (23 )  | (764 )               | (43 )    |
| Restructuring charges and exit costs             | 326            | 332    | 832                  | 1,094    |
| Impairment charges                               | —              | 577    | —                    | 671      |
| Operating (gains), losses and other charges, net | \$249          | \$ 886 | \$24,365             | \$ 1,722 |

The pre-tax pension settlement loss of \$24.3 million related to the completion of the Pension Plan liquidation during the three quarters ended September 28, 2016. See Note 9 for details on the Pension Plan liquidation. Gains on sales of assets and other, net of \$0.8 million for the three quarters ended September 28, 2016 primarily related to restaurants sold to franchisees.

Restructuring charges and exit costs were comprised of the following:

|                                            | Quarter Ended  |        | Three Quarters Ended |          |
|--------------------------------------------|----------------|--------|----------------------|----------|
|                                            | September 28,  |        | September 28,        |          |
|                                            | 2016           | 2015   | 2016                 | 2015     |
|                                            | (In thousands) |        |                      |          |
| Exit costs                                 | \$154          | \$ 43  | \$269                | \$ 583   |
| Severance and other restructuring charges  | 172            | 289    | 563                  | 511      |
| Total restructuring charges and exit costs | \$326          | \$ 332 | \$832                | \$ 1,094 |

The components of the change in accrued exit cost liabilities are as follows:

|                                                            | (In thousands) |
|------------------------------------------------------------|----------------|
| Balance, December 30, 2015                                 | \$ 2,043       |
| Exit costs <sup>(1)</sup>                                  | 269            |
| Payments, net of sublease receipts                         | (378 )         |
| Interest accretion                                         | 91             |
| Balance, September 28, 2016                                | 2,025          |
| Less current portion included in other current liabilities | 748            |
| Long-term portion included in other noncurrent liabilities | \$ 1,277       |

(1) Included as a component of operating (gains), losses and other charges, net.

As of September 28, 2016 and December 30, 2015, we had accrued severance and other restructuring charges of \$0.3 million and \$0.4 million, respectively. The balance as of September 28, 2016 is expected to be paid during the next 12 months.

Impairment charges of \$0.7 million for the three quarters ended September 30, 2015 resulted primarily from the impairment of a restaurant identified as assets held for sale.

## Note 7. Fair Value of Financial Instruments

## Fair Value of Assets and Liabilities Measured on a Recurring and Nonrecurring Basis

Financial assets and liabilities measured at fair value on a recurring basis are summarized below:

|                                                       | Total      | Quoted Prices<br>in Active<br>Markets for<br>Identical<br>Assets/Liabilities<br>(Level 1) | Significant<br>Other<br>Observable<br>Inputs<br>(Level 2) | Significant<br>Unobservable<br>Inputs<br>(Level 3) | Valuation<br>Technique |
|-------------------------------------------------------|------------|-------------------------------------------------------------------------------------------|-----------------------------------------------------------|----------------------------------------------------|------------------------|
| (In thousands)                                        |            |                                                                                           |                                                           |                                                    |                        |
| Fair value measurements as of September 28, 2016:     |            |                                                                                           |                                                           |                                                    |                        |
| Deferred compensation plan investments <sup>(1)</sup> | \$ 10,925  | \$ 10,925                                                                                 | \$ —                                                      | \$ —                                               | —market approach       |
| Interest rate swaps <sup>(2)</sup>                    | (14,577 )  | —                                                                                         | (14,577 )                                                 | —                                                  | income approach        |
| Total                                                 | \$(3,652 ) | \$ 10,925                                                                                 | \$(14,577 )                                               | \$ —                                               | —                      |
| Fair value measurements as of December 30, 2015:      |            |                                                                                           |                                                           |                                                    |                        |
| Deferred compensation plan investments <sup>(1)</sup> | \$ 10,159  | \$ 10,159                                                                                 | \$ —                                                      | \$ —                                               | —market approach       |
| Interest rate swaps <sup>(2)</sup>                    | (1,660 )   | —                                                                                         | (1,660 )                                                  | —                                                  | income approach        |
| Total                                                 | \$8,499    | \$ 10,159                                                                                 | \$(1,660 )                                                | \$ —                                               | —                      |

(1) The fair values of our deferred compensation plan investments are based on the closing market prices of the elected investments.

(2) The fair values of our interest rate swaps are based upon Level 2 inputs, which include valuation models as reported by our counterparties. The key inputs for the valuation models are quoted market prices, interest rates and forward yield curves. See Note 8 for details on the interest rate swaps.

Those assets and liabilities measured at fair value on a nonrecurring basis are summarized below:

|                                                  | Significant<br>Other<br>Observable<br>Inputs<br>(Level<br>2) | Significant<br>Unobservable<br>Inputs<br>(Level 3) | Valuation Technique |
|--------------------------------------------------|--------------------------------------------------------------|----------------------------------------------------|---------------------|
| (In thousands)                                   |                                                              |                                                    |                     |
| Fair value measurements as of December 30, 2015: |                                                              |                                                    |                     |
| Assets held for sale <sup>(1)</sup>              | \$931                                                        | \$ 264                                             | market approach     |

(1) As of December 30, 2015, assets held for sale were written down to their fair value. The fair value of assets held for sale is based upon Level 2 inputs, which include sales agreements.

## Note 8. Long-Term Debt

Denny's Corporation and certain of its subsidiaries have a credit facility consisting of a five-year \$325 million senior secured revolver (with a \$30 million letter of credit sublimit). As of September 28, 2016, we had outstanding revolver loans of \$203.0 million and outstanding letters of credit under the senior secured revolver of \$22.4 million. These balances resulted in availability of \$99.6 million under the revolving facility. Prior to considering the impact of our interest rate swaps, described below, the weighted-average interest rate on outstanding revolver loans was 2.28% and 1.76% as of September 28, 2016 and December 30, 2015, respectively. Taking into consideration our interest rate swaps, the weighted-average interest rate of outstanding revolver loans was 2.63% and 2.31% as of September 28, 2016 and December 30, 2015, respectively.

A commitment fee of 0.25% is paid on the unused portion of the revolving credit facility. Borrowings under the credit facility bear a tiered interest rate, which is based on the Company's consolidated leverage ratio and was set at LIBOR plus 175 basis points as of September 28, 2016. The maturity date for the credit facility is March 30, 2020.



The credit facility is available for working capital, capital expenditures and other general corporate purposes. The credit facility is guaranteed by the Company and its material subsidiaries and is secured by assets of the Company and its subsidiaries, including the stock of the Company's subsidiaries. It includes negative covenants that are usual for facilities and transactions of this type. The credit facility also includes certain financial covenants with respect to a maximum consolidated leverage ratio and a minimum consolidated fixed charge coverage ratio.

#### Interest Rate Hedges

We have interest rate swaps to hedge a portion of the cash flows of our floating rate debt. We designated the interest rate swaps as cash flow hedges of our exposure to variability in future cash flows attributable to payments of LIBOR due on specific notional debt obligations.

Based on the interest rate as determined by our consolidated leverage ratio in effect as of September 28, 2016, under the terms of the swaps, we will pay the following fixed rates on the notional amounts noted:

| Period Covered                  | Notional<br>Amount<br>(In<br>thousands) | Fixed<br>Rate |
|---------------------------------|-----------------------------------------|---------------|
| March 31, 2015 - March 29, 2018 | \$ 120,000                              | 2.88 %        |
| March 29, 2018 - March 31, 2025 | 170,000                                 | 4.19 %        |
| April 1, 2025 - March 31, 2026  | 50,000                                  | 4.21 %        |

As of September 28, 2016, the fair value of the interest rate swaps was a liability of \$14.6 million, which is recorded as a component of other noncurrent liabilities in our Condensed Consolidated Balance Sheets. See Note 14 for the amounts recorded in accumulated other comprehensive loss related to the interest rate swaps.

We believe that our estimated cash flows from operations for 2016, combined with our capacity for additional borrowings under our credit facility, will enable us to meet our anticipated cash requirements and fund capital expenditures over the next twelve months.

#### Note 9. Defined Benefit Plans

The components of net periodic benefit cost were as follows:

|                                | Quarter Ended<br>September 30,<br>2016 | September 30,<br>2015 | Three Quarters<br>Ended<br>September 30,<br>2016 | September 30,<br>2015 |
|--------------------------------|----------------------------------------|-----------------------|--------------------------------------------------|-----------------------|
|                                | (In thousands)                         |                       |                                                  |                       |
| Pension Plan:                  |                                        |                       |                                                  |                       |
| Service cost                   | \$—                                    | \$ 95                 | \$105                                            | \$ 285                |
| Interest cost                  | —                                      | 745                   | —                                                | 2,237                 |
| Expected return on plan assets | —                                      | (877)                 | —                                                | (2,631)               |
| Amortization of net loss       | —                                      | 434                   | —                                                | 1,300                 |
| Net periodic benefit cost      | \$—                                    | \$ 397                | \$105                                            | \$ 1,191              |
| Other Defined Benefit Plans:   |                                        |                       |                                                  |                       |
| Interest cost                  | \$23                                   | \$ 26                 | \$69                                             | \$ 80                 |

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|                           |      |       |       |        |
|---------------------------|------|-------|-------|--------|
| Amortization of net loss  | 21   | 20    | 64    | 59     |
| Net periodic benefit cost | \$44 | \$ 46 | \$133 | \$ 139 |

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During 2014, our Board of Directors approved the termination and liquidation of the Advantica Pension Plan (the "Pension Plan") as of December 31, 2014. During the three quarters ended September 28, 2016, we completed the liquidation of the Pension Plan. Accordingly, we made a final contribution of \$9.5 million to the Pension Plan. The resulting \$67.7 million in Pension Plan assets were used to make lump sum payments and purchase annuity contracts, which are administered by a third-party provider. In addition, during the three quarters ended September 28, 2016, we recognized a pre-tax settlement loss of \$24.3 million related to the liquidation, reflecting the recognition of unamortized actuarial losses that were recorded in accumulated other comprehensive income. See Note 14. We made no contributions to the Pension Plan during the three quarters ended September 30, 2015.

We made contributions of \$0.1 million to our other defined benefit plans during both the three quarters ended September 28, 2016 and the three quarters ended September 30, 2015. We expect to contribute less than \$0.1 million to our other defined benefit plans over the remainder of fiscal 2016.

Additional minimum pension liability, net of tax, of \$0.9 million and \$22.8 million is reported as a component of accumulated other comprehensive loss in our Condensed Consolidated Statement of Shareholders' Equity as of September 28, 2016 and December 30, 2015, respectively.

#### Note 10. Share-Based Compensation

Total share-based compensation cost included as a component of net income was as follows:

|  | Quarter Ended<br>September 28,<br>2016 |  | Quarter Ended<br>September 30,<br>2015 | Three Quarters Ended<br>September 28,<br>2016 |  | Three Quarters Ended<br>September 30,<br>2015 |
|--|----------------------------------------|--|----------------------------------------|-----------------------------------------------|--|-----------------------------------------------|
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## Restricted Stock Units for Board Members

During the quarter ended June 29, 2016, we granted approximately 0.1 million deferred stock units (DSUs) (which are equity classified) with a weighted average grant date fair value of \$10.77 per unit to non-employee members of our Board of Directors. A director may elect to convert these awards into shares of common stock either on a specific date in the future (while still serving as a member of our Board of Directors) or upon termination as a member of our Board of Directors. During the quarter ended September 28, 2016 these awards were subsequently canceled and rescinded and replacement awards were issued. Directors who had previously elected a one-year conversion of the 2016 award received a replacement cash award. The total replacement cash award was \$0.5 million and is liability classified. Directors who had previously elected conversion of the 2016 award at a later date received a replacement DSU award, which is equity classified and has a three year vesting term. The total replacement DSU award was less than 0.1 million DSUs with a weighted average grant date fair value of \$10.77 per unit. During the three quarters ended September 28, 2016, less than 0.1 million DSUs were converted into shares of common stock. As of September 28, 2016, we had approximately \$0.3 million of unrecognized compensation cost related to all unvested restricted stock unit awards outstanding, which is expected to be recognized over a weighted average of 2.6 years.

## Note 11. Income Taxes

The effective tax rate was 35.2% for the quarter and 64.2% year-to-date compared to 30.1% and 34.0%, respectively, for the prior year periods. For the 2016 periods, the difference in the overall effective rate from the U.S. statutory rate was primarily due to the Pension Plan liquidation, foreign tax credits and certain discrete items. During the three quarters ended September 28, 2016, we amended prior years' U.S. tax returns in order to maximize a foreign tax credit in lieu of a foreign tax deduction. This created a benefit to the effective tax rate of 4.8% for the quarter and 4.6% year-to-date. In addition, during the three quarters ended September 28, 2016, certain discrete items created an increase to the effective tax rate of 4.3% for the quarter and 4.7% year-to-date.

In addition to the items noted above, the 2016 year-to-date rate was also impacted by the recognition of a \$2.1 million tax benefit related to the \$24.3 million pre-tax settlement loss on the Pension Plan liquidation. This benefit was at a rate lower than the effective tax rate due to the previous recognition of an approximate \$7.2 million tax benefit in connection with the reversal of our valuation allowance in 2011. Excluding the impact of the Pension Plan liquidation, our effective income tax rate would have been 35.6% for the three quarters ended September 28, 2016.

## Note 12. Net Income Per Share

The amounts used for the basic and diluted net income per share calculations are summarized below:

|                                                    | Quarter Ended                                |          | Three Quarters Ended |           |
|----------------------------------------------------|----------------------------------------------|----------|----------------------|-----------|
|                                                    | September 28, 2016                           |          | September 28, 2015   |           |
|                                                    | 2016                                         | 2015     | 2016                 | 2015      |
|                                                    | (In thousands, except for per share amounts) |          |                      |           |
| Net income                                         | \$9,726                                      | \$ 8,950 | \$8,128              | \$ 27,217 |
| Weighted average shares outstanding - basic        | 74,851                                       | 82,923   | 76,214               | 83,952    |
| Effect of dilutive share-based compensation awards | 1,940                                        | 2,133    | 1,838                | 2,115     |
| Weighted average shares outstanding - diluted      | 76,791                                       | 85,056   | 78,052               | 86,067    |
| Basic net income per share                         | \$0.13                                       | \$ 0.11  | \$0.11               | \$ 0.32   |
| Diluted net income per share                       | \$0.13                                       | \$ 0.11  | \$0.10               | \$ 0.32   |
| Anti-dilutive share-based compensation awards      | —                                            | —        | —                    | —         |



## Note 13. Supplemental Cash Flow Information

|                                                                      | Three Quarters Ended |          |
|----------------------------------------------------------------------|----------------------|----------|
|                                                                      | September 28, 2016   |          |
|                                                                      | September 28, 2015   |          |
|                                                                      | (In thousands)       |          |
| Income taxes paid, net                                               | \$1,140              | \$ 4,916 |
| Interest paid                                                        | \$8,197              | \$ 6,102 |
| Noncash investing and financing activities:                          |                      |          |
| Property acquisition payable                                         | \$—                  | \$ 615   |
| Issuance of common stock, pursuant to share-based compensation plans | \$3,597              | \$ 4,551 |
| Execution of capital leases                                          | \$7,180              | \$ 3,635 |
| Treasury stock payable                                               | \$695                | \$ 1,785 |

## Note 14. Shareholders' Equity

## Share Repurchase

Our credit facility permits the purchase of Denny's stock and the payment of cash dividends subject to certain limitations. In March 2015, our Board of Directors approved a share repurchase program authorizing us to repurchase up to \$100 million of our common stock (in addition to prior authorizations). Under this program, we may, from time to time, purchase shares in the open market (including pre-arranged stock trading plans in accordance with the guidelines specified in Rule 10b5-1 under the Securities Exchange Act of 1934, as amended) or in privately negotiated transactions, subject to market and business conditions.

In May 2016, our Board of Directors approved a new share repurchase program authorizing us to repurchase an additional \$100 million of our common stock, in addition to repurchases previously authorized. Such repurchases are to be made in a manner similar to, and will be in addition to, authorizations under the March 2015 repurchase program.

In November 2015, as part of our previously authorized share repurchase programs, we entered into a variable term, capped accelerated share repurchase (the "ASR") agreement with Wells Fargo Bank, National Association ("Wells Fargo") to repurchase an aggregate of \$50 million of our common stock. During 2015, pursuant to the terms of the ASR agreement, we paid \$50 million in cash and received approximately 3.5 million shares of our common stock, which represents the minimum number of shares to be delivered based on the cap price. We recorded \$36.9 million of treasury stock related to these shares. During the quarter ended September 28, 2016, we settled the ASR agreement with Wells Fargo. As a result, we received final delivery of an additional 1.5 million shares of our common stock, bringing the total number of shares repurchased pursuant to the ASR agreement to 5.0 million. The total number of shares repurchased was based on a combined discounted volume-weighted average price (VWAP) of \$9.90 per share, which was determined based on the average of the daily VWAP of our common stock, less a fixed discount, over the term of the ASR agreement. During July 2016, we recorded \$13.1 million of treasury stock related to the settlement of the equity forward contract related to the ASR agreement.

In addition to the settlement of the ASR agreement, during the three quarters ended September 28, 2016, we repurchased 1.9 million shares of our common stock for approximately \$19.6 million. This brings the total amount repurchased under the March 2015 repurchase program to 8.0 million shares of our common stock for approximately \$81.8 million, leaving approximately \$18.2 million of our common stock that can be repurchased under this program as of September 28, 2016. Additionally, under the May 2016 repurchase program, we are also authorized to

repurchase up to \$100 million of our common stock as of September 28, 2016.

Repurchased shares are included as treasury stock in our Condensed Consolidated Balance Sheets and our Condensed Consolidated Statement of Shareholders' Equity.



## Accumulated Other Comprehensive Loss

The components of the change in accumulated other comprehensive loss were as follows:

|                                                                           | Pensions       | Derivatives | Accumulated<br>Other<br>Comprehensive<br>Loss |
|---------------------------------------------------------------------------|----------------|-------------|-----------------------------------------------|
|                                                                           | (In thousands) |             |                                               |
| Balance as of December 30, 2015                                           | \$(22,764)     | \$ (1,013 ) | \$ (23,777 )                                  |
| Net loss                                                                  | (342 )         | —           | (342 )                                        |
| Amortization of net loss <sup>(1)</sup>                                   | 64             | —           | 64                                            |
| Settlement loss recognized <sup>(2)</sup>                                 | 24,297         | —           | 24,297                                        |
| Net change in fair value of derivatives                                   | —              | (12,302 )   | (12,302 )                                     |
| Reclassification of derivatives to interest expense <sup>(3)</sup>        | —              | (614 )      | (614 )                                        |
| Income tax (expense) benefit related to items of other comprehensive loss | (2,168 )       | 5,034       | 2,866                                         |
| Balance as of September 28, 2016                                          | \$(913 )       | \$ (8,895 ) | \$ (9,808 )                                   |

Before-tax amount related to our Other Defined Benefit Plans that was reclassified from accumulated other comprehensive loss and included as a component of pension expense within general and administrative expenses in our Condensed Consolidated Statements of Income during the three quarters ended September 28, 2016. See Note 9 for additional details.

Before-tax amount related to the liquidation of our Pension Plan that was reclassified from accumulated other comprehensive loss and included as a component of operating (gains), losses and other charges, net in our Condensed Consolidated Statements of Income during the three quarters ended September 28, 2016. See Note 9 for additional details.

Amounts reclassified from accumulated other comprehensive loss into income, represent payments made to the counterparty for the effective portions of the interest rate swaps. These amounts are included as a component of interest expense in our Condensed Consolidated Statements of Income. We expect to reclassify approximately \$0.7 million from accumulated other comprehensive loss related to our interest rate swaps during the next twelve months. See Note 8 for additional details.

## Note 15. Commitments and Contingencies

We have guarantees related to certain franchisee leases and loans. Payments under these guarantees would result from the inability of a franchisee to fund required payments when due. Through September 28, 2016, no events had occurred that caused us to make payments under these guarantees. There were \$8.3 million and \$8.7 million of loans outstanding under these programs as of September 28, 2016 and December 30, 2015, respectively. As of September 28, 2016, the maximum amounts payable under the lease and loan guarantees were \$2.0 million and \$1.2 million, respectively. As a result of these guarantees, we have recorded liabilities of less than \$0.1 million as of both September 28, 2016 and December 30, 2015, which are included as a component of other noncurrent liabilities in our Condensed Consolidated Balance Sheets and other nonoperating expense in our Condensed Consolidated Statements of Income.

There are various claims and pending legal actions against or indirectly involving us, incidental to and arising out of the ordinary course of the business. In the opinion of management, based upon information currently available, the ultimate liability with respect to these proceedings and claims will not materially affect the Company's consolidated results of operations or financial position.

## Note 16. Subsequent Events

We performed an evaluation of subsequent events and determined that no events required disclosure.

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

Forward-Looking Statements

The following discussion is intended to highlight significant changes in our financial position as of September 28, 2016 and results of operations for the quarter and three quarters ended September 28, 2016 as compared to the quarter and three quarters ended September 30, 2015. This report contains forward-looking statements within the meaning of the Private Securities Litigation Reform Act of 1995. The forward-looking statements included in Management's Discussion and Analysis of Financial Condition and Results of Operations, which reflect our best judgment based on factors currently known and are intended to speak only as of the date such statements are made, involve risks, uncertainties, and other factors which may cause our actual performance to be materially different from the performance indicated or implied by such statements. Such factors include, among others: competitive pressures from within the restaurant industry; the level of success of our operating initiatives and advertising and promotional efforts; adverse publicity; health concerns arising from food-related pandemics, outbreaks of flu viruses, such as avian flu, or other diseases; changes in business strategy or development plans; terms and availability of capital; regional weather conditions; overall changes in the general economy (including with regard to energy costs), particularly at the retail level; political environment (including acts of war and terrorism); and other factors included in the discussion below, or in Part II. Item 7. Management's Discussion and Analysis of Financial Condition and Results of Operations and Part I. Item 1A. Risk Factors, contained in our Annual Report on Form 10-K for the year ended December 30, 2015. While we may elect to update forward-looking statements at some point in the future, we expressly disclaim any obligation to update any forward-looking statements, whether as a result of new information, future events, or otherwise, except as required by law.

## Statements of Income

The following table contains information derived from our Condensed Consolidated Statements of Income expressed as a percentage of total operating revenues, except as noted below. Percentages may not add due to rounding.

|                                                     | Quarter Ended          |       |    |                    |       | Three Quarters Ended |           |       |                    |           |       |   |
|-----------------------------------------------------|------------------------|-------|----|--------------------|-------|----------------------|-----------|-------|--------------------|-----------|-------|---|
|                                                     | September 28, 2016     |       |    | September 30, 2015 |       | September 28, 2016   |           |       | September 30, 2015 |           |       |   |
|                                                     | (Dollars in thousands) |       |    |                    |       |                      |           |       |                    |           |       |   |
| Revenue:                                            |                        |       |    |                    |       |                      |           |       |                    |           |       |   |
| Company restaurant sales                            | \$93,122               | 72.5  | %  | \$89,279           | 72.1  | %                    | \$272,718 | 72.3  | %                  | \$263,890 | 71.9  | % |
| Franchise and license revenue                       | 35,264                 | 27.5  | %  | 34,499             | 27.9  | %                    | 104,625   | 27.7  | %                  | 103,378   | 28.1  | % |
| Total operating revenue                             | 128,386                | 100.0 | %  | 123,778            | 100.0 | %                    | 377,343   | 100.0 | %                  | 367,268   | 100.0 | % |
| Costs of company restaurant sales (a):              |                        |       |    |                    |       |                      |           |       |                    |           |       |   |
| Product costs                                       | 22,819                 | 24.5  | %  | 23,289             | 26.1  | %                    | 67,253    | 24.7  | %                  | 66,609    | 25.2  | % |
| Payroll and benefits                                | 35,999                 | 38.7  | %  | 34,249             | 38.4  | %                    | 104,548   | 38.3  | %                  | 101,118   | 38.3  | % |
| Occupancy                                           | 4,928                  | 5.3   | %  | 5,164              | 5.8   | %                    | 14,721    | 5.4   | %                  | 14,972    | 5.7   | % |
| Other operating expenses                            | 13,372                 | 14.4  | %  | 12,388             | 13.9  | %                    | 37,544    | 13.8  | %                  | 36,019    | 13.6  | % |
| Total costs of company restaurant sales             | 77,118                 | 82.8  | %  | 75,090             | 84.1  | %                    | 224,066   | 82.2  | %                  | 218,718   | 82.9  | % |
| Costs of franchise and license revenue (a)          | 10,275                 | 29.1  | %  | 10,649             | 30.9  | %                    | 31,037    | 29.7  | %                  | 32,843    | 31.8  | % |
| General and administrative expenses                 | 17,558                 | 13.7  | %  | 16,008             | 12.9  | %                    | 50,691    | 13.4  | %                  | 49,771    | 13.6  | % |
| Depreciation and amortization                       | 5,609                  | 4.4   | %  | 5,422              | 4.4   | %                    | 16,207    | 4.3   | %                  | 15,760    | 4.3   | % |
| Operating (gains), losses and other charges, net    | 249                    | 0.2   | %  | 886                | 0.7   | %                    | 24,365    | 6.5   | %                  | 1,722     | 0.5   | % |
| Total operating costs and expenses, net             | 110,809                | 86.3  | %  | 108,055            | 87.3  | %                    | 346,366   | 91.8  | %                  | 318,814   | 86.8  | % |
| Operating income                                    | 17,577                 | 13.7  | %  | 15,723             | 12.7  | %                    | 30,977    | 8.2   | %                  | 48,454    | 13.2  | % |
| Interest expense, net                               | 3,117                  | 2.4   | %  | 2,327              | 1.9   | %                    | 8,905     | 2.4   | %                  | 6,678     | 1.8   | % |
| Other nonoperating (income) expense, net            | (543)                  | (0.4) | %) | 592                | 0.5   | %                    | (635)     | (0.2) | %)                 | 538       | 0.1   | % |
| Net income before income taxes                      | 15,003                 | 11.7  | %  | 12,804             | 10.3  | %                    | 22,707    | 6.0   | %                  | 41,238    | 11.2  | % |
| Provision for income taxes                          | 5,277                  | 4.1   | %  | 3,854              | 3.1   | %                    | 14,579    | 3.9   | %                  | 14,021    | 3.8   | % |
| Net income                                          | \$9,726                | 7.6   | %  | \$8,950            | 7.2   | %                    | \$8,128   | 2.2   | %                  | \$27,217  | 7.4   | % |
| Other Data:                                         |                        |       |    |                    |       |                      |           |       |                    |           |       |   |
| Company average unit sales                          | \$573                  |       |    | \$563              |       |                      | \$1,689   |       |                    | \$1,660   |       |   |
| Franchise average unit sales                        | \$396                  |       |    | \$393              |       |                      | \$1,174   |       |                    | \$1,167   |       |   |
| Company equivalent units (b)                        | 163                    |       |    | 159                |       |                      | 161       |       |                    | 159       |       |   |
| Franchise equivalent units (b)                      | 1,560                  |       |    | 1,536              |       |                      | 1,554     |       |                    | 1,536     |       |   |
| Company same-store sales increase (c)(d)            | 1.0                    | %     |    | 7.0                | %     |                      | 1.5       | %     |                    | 7.5       | %     |   |
| Domestic franchise same-store sales increase (c)(d) | 1.0                    | %     |    | 5.9                | %     |                      | 0.9       | %     |                    | 6.7       | %     |   |

(a)

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Costs of company restaurant sales percentages are as a percentage of company restaurant sales. Costs of franchise and license revenue percentages are as a percentage of franchise and license revenue. All other percentages are as a percentage of total operating revenue.

- (b) Equivalent units are calculated as the weighted average number of units outstanding during a defined time period.
- (c) Same-store sales include sales from restaurants that were open the same period in the prior year.
- (d) Prior year amounts have not been restated for 2016 comparable units.

## Unit Activity

|                                                          | Quarter Ended<br>September 28,<br>2016 |                       | Three Quarters Ended<br>September 28,<br>2016 |                       |
|----------------------------------------------------------|----------------------------------------|-----------------------|-----------------------------------------------|-----------------------|
|                                                          | September 30,<br>2015                  | September 30,<br>2015 | September 30,<br>2015                         | September 30,<br>2015 |
| Company restaurants, beginning of period                 | 162                                    | 160                   | 164                                           | 161                   |
| Units opened                                             | —                                      | —                     | 1                                             | —                     |
| Units acquired from franchisees                          | 6                                      | 1                     | 9                                             | 2                     |
| Units sold to franchisees                                | —                                      | —                     | (6                                            | ) —                   |
| Units closed                                             | —                                      | —                     | —                                             | (2                    |
| End of period                                            | 168                                    | 161                   | 168                                           | 161                   |
| Franchised and licensed restaurants, beginning of period | 1,558                                  | 1,536                 | 1,546                                         | 1,541                 |
| Units opened                                             | 13                                     | 9                     | 37                                            | 31                    |
| Units purchased from Company                             | —                                      | —                     | 6                                             | —                     |
| Units acquired by Company                                | (6                                     | ) (1                  | ) (9                                          | ) (2                  |
| Units closed                                             | (5                                     | ) (5                  | ) (20                                         | ) (31                 |
| End of period                                            | 1,560                                  | 1,539                 | 1,560                                         | 1,539                 |
| Total restaurants, end of period                         | 1,728                                  | 1,700                 | 1,728                                         | 1,700                 |

## Company Restaurant Operations

During the quarter ended September 28, 2016, company restaurant sales increased \$3.8 million, or 4.3%, primarily resulting from a 1.0% increase in company same-store sales and a four equivalent unit increase in company restaurants as compared to the prior year period. During the three quarters ended September 28, 2016, company restaurant sales increased \$8.8 million, or 3.3%, primarily resulting from a 1.5% increase in company same-store sales and a two equivalent unit increase in company restaurants as compared to the prior year period.

Total costs of company restaurant sales as a percentage of company restaurant sales decreased to 82.8% for the quarter and 82.2% year-to-date from 84.1% and 82.9%, respectively, in the prior year periods.

Product costs were 24.5% for the quarter and 24.7% year-to-date compared to 26.1% and 25.2%, respectively, in the prior year periods. These decreases were primarily due to the reduced cost of eggs and the leverage gained from pricing increases.

Payroll and benefits were 38.7% for the quarter and 38.3% year-to-date compared to 38.4% and 38.3%, respectively, in the prior year period. The increase for the quarter was primarily due to a 0.5 percentage point increase in labor costs and a 0.3 percentage point increase in workers' compensation costs, partially offset by a 0.6 percentage point decrease in incentive compensation. The year-to-date period was flat as compared to the prior year period, as a 0.7 percentage point increase in labor costs and a 0.3 percentage point increase in group insurance was offset by a 0.8 percentage point decrease in incentive compensation and a 0.3 percentage point decrease in workers' compensation costs. Contributing to the increase in labor costs in the year-to-date period was the impact of the California Paid Sick Leave law, which became effective in July 2015.

Occupancy costs decreased to 5.3% for the quarter and 5.4% year-to-date from 5.8% and 5.7%, respectively, in the prior year periods. These decreases were primarily due to decreases in general liability insurance costs.



Other operating expenses were comprised of the following amounts and percentages of company restaurant sales:

|                          | Quarter Ended          |      |   |                       |      |   | Three Quarters Ended  |      |   |                       |      |   |
|--------------------------|------------------------|------|---|-----------------------|------|---|-----------------------|------|---|-----------------------|------|---|
|                          | September 28,<br>2016  |      |   | September 30,<br>2015 |      |   | September 28,<br>2016 |      |   | September 30,<br>2015 |      |   |
|                          | (Dollars in thousands) |      |   |                       |      |   |                       |      |   |                       |      |   |
| Utilities                | \$3,429                | 3.7  | % | \$3,517               | 3.9  | % | \$9,232               | 3.4  | % | \$9,825               | 3.7  | % |
| Repairs and maintenance  | 1,559                  | 1.7  | % | 1,549                 | 1.7  | % | 4,893                 | 1.8  | % | 4,496                 | 1.7  | % |
| Marketing                | 3,500                  | 3.8  | % | 3,383                 | 3.8  | % | 10,123                | 3.7  | % | 9,848                 | 3.7  | % |
| Other direct costs       | 4,884                  | 5.2  | % | 3,939                 | 4.4  | % | 13,296                | 4.9  | % | 11,850                | 4.5  | % |
| Other operating expenses | \$13,372               | 14.4 | % | \$12,388              | 13.9 | % | \$37,544              | 13.8 | % | \$36,019              | 13.6 | % |

#### Franchise Operations

Franchise and license revenue and costs of franchise and license revenue were comprised of the following amounts and percentages of franchise and license revenue for the periods indicated:

|                                        | Quarter Ended          |       |   |                       |       |   | Three Quarters Ended  |       |   |                       |       |   |
|----------------------------------------|------------------------|-------|---|-----------------------|-------|---|-----------------------|-------|---|-----------------------|-------|---|
|                                        | September 28,<br>2016  |       |   | September 30,<br>2015 |       |   | September 28,<br>2016 |       |   | September 30,<br>2015 |       |   |
|                                        | (Dollars in thousands) |       |   |                       |       |   |                       |       |   |                       |       |   |
| Royalties                              | \$25,039               | 71.0  | % | \$23,922              | 69.3  | % | \$73,694              | 70.4  | % | \$70,859              | 68.5  | % |
| Initial fees                           | 757                    | 2.1   | % | 558                   | 1.6   | % | 2,081                 | 2.0   | % | 1,659                 | 1.6   | % |
| Occupancy revenue                      | 9,468                  | 26.8  | % | 10,019                | 29.1  | % | 28,850                | 27.6  | % | 30,860                | 29.9  | % |
| Franchise and license revenue          | \$35,264               | 100.0 | % | \$34,499              | 100.0 | % | \$104,625             | 100.0 | % | \$103,378             | 100.0 | % |
| Occupancy costs                        | \$7,023                | 19.9  | % | \$7,620               | 22.1  | % | \$21,373              | 20.4  | % | \$23,244              | 22.5  | % |
| Other direct costs                     | 3,252                  | 9.2   | % | 3,029                 | 8.8   | % | 9,664                 | 9.2   | % | 9,599                 | 9.3   | % |
| Costs of franchise and license revenue | \$10,275               | 29.1  | % | \$10,649              | 30.9  | % | \$31,037              | 29.7  | % | \$32,843              | 31.8  | % |

During the quarter ended September 28, 2016, royalties increased \$1.1 million, or 4.7%, primarily resulting from a 24 equivalent unit increase in franchised and licensed restaurants, a 1.0% increase in domestic same-store sales and a higher average royalty rate as compared to the prior year period. During the three quarters ended September 28, 2016, royalties increased \$2.8 million, or 4.0%, primarily resulting from a 18 equivalent unit increase in franchised and licensed restaurants, a 0.9% increase in domestic same-store sales and a higher average royalty rate as compared to the prior year period. Initial fees increased \$0.2 million for the quarter and \$0.4 million year-to-date as a higher number of restaurants were opened by franchisees and sold to franchisees during the current year periods. The decrease in occupancy revenue of \$0.6 million, or 5.5%, for the quarter and \$2.0 million, or 6.5%, year-to-date was primarily the result of lease expirations.

Costs of franchise and license revenue decreased \$0.4 million, or 3.5%, for the quarter and decreased \$1.8 million, or 5.5%, year-to-date. Occupancy costs decreased \$0.6 million, or 7.8%, for the quarter and \$1.9 million, or 8.0%, year-to-date, primarily resulting from lease expirations. Other direct costs increased \$0.2 million, or 7.4%, for the quarter and were essentially flat year-to-date. As a result, costs of franchise and license revenue as a percentage of franchise and license revenue decreased to 29.1% for the quarter from 30.9% for the prior year quarter and decreased to 29.7% year-to-date from 31.8% for the prior year period.

#### Other Operating Costs and Expenses



Other operating costs and expenses such as general and administrative expenses and depreciation and amortization expense relate to both company and franchise operations.

General and administrative expenses were comprised of the following:

|                                           | Quarter Ended<br>September 28,<br>2016 |           | Three Quarters Ended<br>September 28,<br>2016 |           |
|-------------------------------------------|----------------------------------------|-----------|-----------------------------------------------|-----------|
|                                           | September 30,<br>2015                  |           | September 30,<br>2015                         |           |
|                                           | (In thousands)                         |           |                                               |           |
| Share-based compensation                  | \$1,775                                | \$ 1,941  | \$5,625                                       | \$ 5,505  |
| Other general and administrative expenses | 15,783                                 | 14,067    | 45,066                                        | 44,266    |
| Total general and administrative expenses | \$17,558                               | \$ 16,008 | \$50,691                                      | \$ 49,771 |

Other general and administrative expenses increased by \$1.7 million for the quarter and \$0.8 million year-to-date primarily resulting from increases of \$1.2 million and \$1.0 million, respectively, related to market valuation changes in our non-qualified deferred compensation plan liabilities. Offsetting gains on the underlying plan investments are included as a component of other non-operating income, net. The \$0.2 million decrease in share-based compensation, as compared to the prior year quarter, primarily resulted from the cancellation of equity awards and subsequent issuance of cash awards to non-employee members of our Board of Directors. See Note 10 for details.

Depreciation and amortization was comprised of the following:

|                                             | Quarter Ended<br>September 28,<br>2016 |          | Three Quarters Ended<br>September 28,<br>2016 |           |
|---------------------------------------------|----------------------------------------|----------|-----------------------------------------------|-----------|
|                                             | September 30,<br>2015                  |          | September 30,<br>2015                         |           |
|                                             | (In thousands)                         |          |                                               |           |
| Depreciation of property and equipment      | \$4,289                                | \$ 4,217 | \$12,568                                      | \$ 12,141 |
| Amortization of capital lease assets        | 941                                    | 853      | 2,629                                         | 2,560     |
| Amortization of intangible and other assets | 379                                    | 352      | 1,010                                         | 1,059     |
| Total depreciation and amortization expense | \$5,609                                | \$ 5,422 | \$16,207                                      | \$ 15,760 |

Operating (gains), losses and other charges, net were comprised of the following:

|                                                  | Quarter Ended<br>September 28,<br>2016 |        | Three Quarters Ended<br>September 28,<br>2016 |          |
|--------------------------------------------------|----------------------------------------|--------|-----------------------------------------------|----------|
|                                                  | September 30,<br>2015                  |        | September 30,<br>2015                         |          |
|                                                  | (In thousands)                         |        |                                               |          |
| Pension settlement loss                          | \$—                                    | \$ —   | \$24,297                                      | \$ —     |
| Gains on sales of assets and other, net          | (77 )                                  | (23 )  | (764 )                                        | (43 )    |
| Restructuring charges and exit costs             | 326                                    | 332    | 832                                           | 1,094    |
| Impairment charges                               | —                                      | 577    | —                                             | 671      |
| Operating (gains), losses and other charges, net | \$249                                  | \$ 886 | \$24,365                                      | \$ 1,722 |

The pre-tax pension settlement loss of \$24.3 million related to the completion of the Pension Plan liquidation during the three quarters ended September 28, 2016. See Note 9 for details on the Pension Plan liquidation. Gains on sales of assets and other, net of \$0.8 million for the three quarters ended September 28, 2016 primarily related to restaurants sold to franchisees.

Restructuring charges and exit costs were comprised of the following:

|                                           | Quarter Ended      |                    | Three Quarters Ended |                    |
|-------------------------------------------|--------------------|--------------------|----------------------|--------------------|
|                                           | September 28, 2016 | September 30, 2015 | September 28, 2016   | September 30, 2015 |
|                                           | (In thousands)     |                    |                      |                    |
| Exit costs                                | \$154              | \$ 43              | \$269                | \$ 583             |
| Severance and other restructuring charges | 172                | 289                | 563                  | 511                |
| Total restructuring and exit costs        | \$326              | \$ 332             | \$832                | \$ 1,094           |

Operating income was \$17.6 million for the quarter and \$31.0 million year-to-date compared with \$15.7 million and \$48.5 million, respectively, for the prior year periods. The current year-to-date period was significantly impacted by the \$24.3 million pre-tax settlement loss related to the Pension Plan liquidation.

Interest expense, net was comprised of the following:

|                                          | Quarter Ended      |                    | Three Quarters Ended |                    |
|------------------------------------------|--------------------|--------------------|----------------------|--------------------|
|                                          | September 28, 2016 | September 30, 2015 | September 28, 2016   | September 30, 2015 |
|                                          | (In thousands)     |                    |                      |                    |
| Interest on credit facilities            | \$1,158            | \$ 607             | \$3,352              | \$ 1,995           |
| Interest on interest rate swaps          | 193                | 284                | 614                  | 578                |
| Interest on capital lease liabilities    | 1,287              | 928                | 3,389                | 2,531              |
| Letters of credit and other fees         | 304                | 285                | 895                  | 899                |
| Interest income                          | (73 )              | (18 )              | (100 )               | (52 )              |
| Total cash interest                      | 2,869              | 2,086              | 8,150                | 5,951              |
| Amortization of deferred financing costs | 149                | 123                | 445                  | 366                |
| Interest accretion on other liabilities  | 99                 | 118                | 310                  | 361                |
| Total interest expense, net              | \$3,117            | \$ 2,327           | \$8,905              | \$ 6,678           |

Interest expense, net increased by \$0.8 million for the quarter and \$2.2 million year-to-date primarily due to the increased balance of our credit facility and an increase in capital leases.

Other nonoperating income, net was \$0.5 million for the quarter and \$0.6 million year-to-date compared to other nonoperating expense, net of \$0.6 million and \$0.5 million, respectively, for the prior year periods. The current year income was primarily the result of gains on deferred compensation plan investments. The prior year expense was primarily the result of losses on deferred compensation plan investments and the year-to-date period included \$0.3 million of write-offs of deferred financing costs related to our amended credit facility.

The provision for income taxes was \$5.3 million for the quarter and \$14.6 million year-to-date compared to \$3.9 million and \$14.0 million, respectively, for the prior year periods. The effective tax rate was 35.2% for the quarter and 64.2% year-to-date compared to 30.1% and 34.0%, respectively, for the prior year periods. For the 2016 periods, the difference in the overall effective rate from the U.S. statutory rate was primarily due to the Pension Plan liquidation, foreign tax credits and certain discrete items. During the three quarters ended September 28, 2016, we amended prior years' U.S. tax returns in order to maximize a foreign tax credit in lieu of a foreign tax deduction. This created a benefit to the effective tax rate of 4.8% for the quarter and 4.6% year-to-date. In addition, during the three quarters ended September 28, 2016, certain discrete items created an increase to the effective tax rate of 4.3% for the quarter and 4.7% year-to-date.



In addition to the items noted above, the 2016 rates were also impacted by the recognition of a \$2.1 million tax benefit related to the \$24.3 million pre-tax settlement loss on the Pension Plan liquidation. This benefit was at a rate lower than the effective tax rate due to the previous recognition of an approximate \$7.2 million tax benefit in connection with the reversal of our valuation allowance in 2011. Excluding the impact of the Pension Plan liquidation, our effective income tax rate would have been 35.6% for the three quarters ended September 28, 2016. We expect the 2016 fiscal year effective tax rate to be between 33% and 37% excluding the impact of the Pension Plan liquidation. The annual effective tax rate cannot be determined until the end of the fiscal year; therefore, the actual rate could differ from our current estimates.

Net income was \$9.7 million for the quarter and \$8.1 million year-to-date compared with \$9.0 million and \$27.2 million, respectively, for the prior year periods. The current year-to-date period was significantly impacted by the \$24.3 million pre-tax settlement loss related to the Pension Plan liquidation.

### Liquidity and Capital Resources

Our primary sources of liquidity and capital resources are cash generated from operations and borrowings under our credit facility (as described below). Principal uses of cash are operating expenses, capital expenditures and the repurchase of shares of our common stock.

The following table presents a summary of our sources and uses of cash and cash equivalents for the periods indicated:

|                                                  | Three Quarters Ended |                    |
|--------------------------------------------------|----------------------|--------------------|
|                                                  | September 28, 2016   | September 30, 2015 |
|                                                  | (In thousands)       |                    |
| Net cash provided by operating activities        | \$43,132             | \$ 56,927          |
| Net cash used in investing activities            | (25,893 )            | (20,554 )          |
| Net cash used in financing activities            | (17,384 )            | (30,846 )          |
| Increase (decrease) in cash and cash equivalents | \$(145 )             | \$ 5,527           |

Net cash flows provided by operating activities were \$43.1 million for the three quarters ended September 28, 2016 compared to \$56.9 million for the three quarters ended September 30, 2015. The decrease in cash flows provided by operating activities is primarily due to the payout of accrued incentive compensation and the funding of our pension liability during the three quarters ended September 28, 2016. We believe that our estimated cash flows from operations for 2016, combined with our capacity for additional borrowings under our credit facility, will enable us to meet our anticipated cash requirements and fund capital expenditures over the next twelve months.

Net cash flows used in investing activities were \$25.9 million for the three quarters ended September 28, 2016. These cash flows include capital expenditures of \$14.6 million and restaurant acquisition costs of \$13.0 million. The restaurant acquisition costs include \$12.4 million for nine franchised restaurants reacquired during the three quarters ended September 28, 2016 and the payment of \$0.6 million for a franchised restaurant that was reacquired during 2015. These costs were partially offset by proceeds from asset sales of \$1.9 million related to restaurants sold to franchisees.

Our principal capital requirements have been largely associated with the following:

Three Quarters Ended

|                        | September 30,<br>2016 | September 30,<br>2015 |
|------------------------|-----------------------|-----------------------|
|                        | (In thousands)        |                       |
| Facilities             | \$5,615               | \$ 6,989              |
| New construction       | 2,958                 | 761                   |
| Remodeling             | 4,714                 | 9,358                 |
| Information technology | 803                   | 587                   |
| Other                  | 525                   | 737                   |
| Capital expenditures   | \$14,615              | \$ 18,432             |

Capital expenditures for fiscal 2016 are expected to be approximately \$33 to \$35 million, including the acquisition of nine franchised restaurants, the completion of approximately 25 remodels at company restaurants, the opening of one new company restaurant, and the scrape and rebuild of a company restaurant. During the three quarters ended September 28, 2016, we acquired nine franchised restaurants and remodeled 17 company restaurants.

Cash flows used in financing activities were \$17.4 million for the three quarters ended September 28, 2016, which included cash payments for stock repurchases of \$19.1 million and accounts payable funding of \$4.4 million, partially offset by net long-term debt borrowings of \$5.6 million.

Our working capital deficit was \$48.1 million at September 28, 2016 compared to \$65.1 million at December 30, 2015. The decrease in working capital deficit was primarily related to the payout of accrued incentive compensation and the funding of our pension liability during the three quarters ended September 28, 2016. We are able to operate with a substantial working capital deficit because (1) restaurant operations and most food service operations are conducted primarily on a cash (and cash equivalent) basis with a low level of accounts receivable, (2) rapid turnover allows a limited investment in inventories, and (3) accounts payable for food, beverages and supplies usually become due after the receipt of cash from the related sales.

#### Credit Facility

As of September 28, 2016, we had outstanding revolver loans of \$203.0 million and outstanding letters of credit under the senior secured revolver of \$22.4 million. These balances resulted in availability of \$99.6 million under the revolving facility. Prior to considering the impact of our interest rate swaps, described below, the weighted-average interest rate on outstanding revolver loans was 2.28% as of September 28, 2016. Taking into consideration our interest rate swaps, the weighted-average interest rate of outstanding revolver loans was 2.63% as of September 28, 2016.

A commitment fee of 0.25% is paid on the unused portion of the revolving credit facility. Borrowings under the credit facility bear a tiered interest rate, which is based on the Company's consolidated leverage ratio and was set at LIBOR plus 175 basis points as of September 28, 2016. The maturity date for the credit facility is March 30, 2020.

The credit facility is available for working capital, capital expenditures and other general corporate purposes. The credit facility is guaranteed by the Company and its material subsidiaries and is secured by assets of the Company and its subsidiaries, including the stock of the Company's subsidiaries. It includes negative covenants that are usual for facilities and transactions of this type. The credit facility also includes certain financial covenants with respect to a maximum consolidated leverage ratio and a minimum consolidated fixed charge coverage ratio.

#### Interest Rate Hedges

We have interest rate swaps to hedge a portion of the cash flows of our floating rate debt. We designated the interest rate swaps as cash flow hedges of our exposure to variability in future cash flows attributable to payments of LIBOR due on specific notional debt obligations.

Based on the interest rate as determined by our consolidated leverage ratio in effect as of September 28, 2016, under the terms of the swaps, we will pay the following fixed rates on the notional amounts noted:

| Period Covered                  | Notional<br>Amount<br>(In<br>thousands) | Fixed<br>Rate |
|---------------------------------|-----------------------------------------|---------------|
| March 31, 2015 - March 29, 2018 | \$ 120,000                              | 2.88%         |

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|                                 |         |        |
|---------------------------------|---------|--------|
| March 29, 2018 - March 31, 2025 | 170,000 | 4.19 % |
| April 1, 2025 - March 31, 2026  | 50,000  | 4.21 % |

As of September 28, 2016, the fair value of the interest rate swaps was a liability of \$14.6 million, which is recorded as a component of other noncurrent liabilities in our Condensed Consolidated Balance Sheets.

### Implementation of New Accounting Standards

Information regarding the implementation of new accounting standards is incorporated by reference from Note 2 to our condensed consolidated financial statements set forth in Part I of this report.



Item 3. Quantitative and Qualitative Disclosures About Market Risk

There have been no material changes in our quantitative and qualitative market risks since the prior reporting period.

Item 4. Controls and Procedures

As required by Rule 13a-15(b) under the Securities Exchange Act of 1934, as amended (the “Exchange Act”), our management conducted an evaluation (under the supervision and with the participation of our President and Chief Executive Officer, John C. Miller, and our Executive Vice President, Chief Administrative Officer and Chief Financial Officer, F. Mark Wolfinger) as of the end of the period covered by this Quarterly Report on Form 10-Q, of the effectiveness of our disclosure controls and procedures as defined in Rule 13a-15(e) under the Exchange Act. Based on that evaluation, Messrs. Miller and Wolfinger each concluded that our disclosure controls and procedures are effective to provide reasonable assurance that information required to be disclosed in the reports that we file or submit under the Exchange Act (i) is recorded, processed, summarized and reported within the time periods specified in the Securities and Exchange Commission's rules and forms and (ii) is accumulated and communicated to our management, including Messrs. Miller and Wolfinger, as appropriate to allow timely decisions regarding required disclosure.

There have been no changes in our internal control over financial reporting identified in connection with the evaluation required by Rule 13a-15(d) 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.

PART II - OTHER INFORMATION

Item 1. Legal Proceedings

Information regarding legal proceedings is incorporated by reference from Note 15 to our condensed consolidated financial statements set forth in Part I of this report.

Item 1A. Risk Factors

There have been no material changes in the risk factors set forth in Part I, Item 1A, “Risk Factors” in our Annual Report on Form 10-K for the fiscal year ended December 30, 2015.

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

## Purchases of Equity Securities by the Issuer

The table below provides information concerning repurchases of shares of our common stock during the quarter ended September 28, 2016.

| Period                                   | Total<br>Number<br>of<br>Shares<br>Purchased | Average<br>Price<br>Paid Per<br>Share <sup>(1)</sup> | Total<br>Number of<br>Shares<br>Purchased<br>as Part of<br>Publicly<br>Announced<br>Programs <sup>(2)</sup> | Approximate<br>Dollar Value<br>of Shares<br>that May<br>Yet be<br>Purchased<br>Under the<br>Programs<br><sup>(2)(3)</sup> |
|------------------------------------------|----------------------------------------------|------------------------------------------------------|-------------------------------------------------------------------------------------------------------------|---------------------------------------------------------------------------------------------------------------------------|
| (In thousands, except per share amounts) |                                              |                                                      |                                                                                                             |                                                                                                                           |
| June 30, 2016 - July 27, 2016            | 1,706 <sup>(4)</sup>                         | \$ 10.05                                             | <sup>(4)</sup> 1,706                                                                                        | <sup>(4)</sup> \$ 127,987                                                                                                 |
| July 28, 2016 - August 24, 2016          | 317                                          | 10.99                                                | 317                                                                                                         | \$ 124,494                                                                                                                |
| August 25, 2016 - September 28, 2016     | 599                                          | 10.53                                                | 599                                                                                                         | \$ 118,178                                                                                                                |
| Total                                    | 2,622                                        | \$ 10.27                                             | <sup>(4)</sup> 2,622                                                                                        |                                                                                                                           |

(1) Average price paid per share excludes commissions.

On March 31, 2015, we announced that our Board of Directors approved a new share repurchase program, authorizing us to repurchase up to an additional \$100 million of our common stock (in addition to prior authorizations). Such repurchases may take place from time to time on the open market (including pre-arranged stock trading plans in accordance with the guidelines specified in Rule 10b5-1 under the Exchange Act) or in privately negotiated transactions, subject to market and business conditions. During the quarter ended September 28, 2016, taking into consideration the settlement of the ASR agreement (described below), we purchased 2,622,002 shares of our common stock for an aggregate consideration of approximately \$25.0 million, pursuant to the share repurchase program.

On May 26, 2016, we announced that our Board of Directors approved a new share repurchase program, authorizing us to repurchase up to an additional \$100 million of our common stock (in addition to prior authorizations). Such repurchases are to be made in a manner similar to, and will be in addition to, authorizations under the March 31, 2015 repurchase program.

Includes the settlement of the \$13.1 million equity forward contract and the final delivery of 1.5 million shares of our common stock received under the ASR agreement we entered in November 2015 to repurchase an aggregate \$50 million of our common stock. In total 5.0 million shares of our common stock were repurchased pursuant to the ASR agreement at an average purchase price of \$9.90 per share.

## Item 6. Exhibits

The following are included as exhibits to this report:

| Exhibit<br>No. | Description |
|----------------|-------------|
|----------------|-------------|

|      |                                                                                                                                                                                                  |
|------|--------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------|
| 31.1 | Certification of John C. Miller, President and Chief Executive Officer of Denny's Corporation, pursuant to Rule 13a-14(a), as adopted pursuant to Section 302 of the Sarbanes-Oxley Act of 2002. |
|------|--------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------------|

31.2 Certification of F. Mark Wolfinger, Executive Vice President, Chief Administrative Officer and Chief Financial Officer of Denny's Corporation, pursuant to Rule 13a-14(a), as adopted pursuant to Section 302 of the Sarbanes-Oxley Act of 2002.

32.1 Certification of John C. Miller, President and Chief Executive Officer of Denny's Corporation, and F. Mark Wolfinger, Executive Vice President, Chief Administrative Officer and Chief Financial Officer of Denny's Corporation, 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.LAB XBRL Taxonomy Extension Label Linkbase Document

101.PRE XBRL Taxonomy Extension Presentation Linkbase Document

101.DEF XBRL Taxonomy Extension Definition Linkbase Document

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.

DENNY'S CORPORATION

Date: November 1, 2016 By: /s/ F. Mark Wolfinger  
F. Mark Wolfinger  
Executive Vice President,  
Chief Administrative Officer and  
Chief Financial Officer

Date: November 1, 2016 By: /s/ Jay C. Gilmore  
Jay C. Gilmore  
Vice President,  
Chief Accounting Officer and  
Corporate Controller