

PAPA JOHNS INTERNATIONAL INC

Form 10-Q

May 03, 2016

Table of Contents

UNITED STATES

SECURITIES AND EXCHANGE COMMISSION

Washington, D.C. 20549

FORM 10-Q

(Mark One)

Quarterly report pursuant to Section 13 or 15(d) of the Securities Exchange Act of 1934

For the quarterly period ended March 27, 2016

OR

Transition report pursuant to Section 13 or 15(d) of the Securities Exchange Act of 1934

Commission File Number: 0-21660

PAPA JOHN'S INTERNATIONAL, INC.

Edgar Filing: PAPA JOHNS INTERNATIONAL INC - Form 10-Q

(Exact name of registrant as specified in its charter)

Delaware	61-1203323
(State or other jurisdiction of incorporation or organization)	(I.R.S. Employer Identification number)

2002 Papa Johns Boulevard

Louisville, Kentucky 40299-2367

(Address of principal executive offices)

(502) 261-7272

(Registrant's telephone number, including area code)

Indicate by check mark whether the registrant (1) has filed all reports required to be filed by Section 13 or 15(d) of the Securities Exchange Act of 1934 during the preceding 12 months (or for such shorter period that the registrant was required to file such reports), and (2) has been subject to such filing requirements for the past 90 days: Yes 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 (Section 232.405 of this chapter) during the preceding 12 months (or for such shorter period that the registrant was required to submit and post such files). Yes No

Indicate by check mark whether the registrant is a large accelerated filer, an accelerated filer, a non-accelerated filer or a smaller reporting company. See 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

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

Edgar Filing: PAPA JOHNS INTERNATIONAL INC - Form 10-Q

At April 26, 2016, there were outstanding 37,242,152 shares of the registrant's common stock, par value \$0.01 per share.

---

Table of Contents

INDEX

	Page No.
<b><u>PART I. FINANCIAL INFORMATION</u></b>	
<b><u>Item 1. Financial Statements</u></b>	
<u>Condensed Consolidated Balance Sheets — March 27, 2016 and December 27, 2015</u>	3
<u>Condensed Consolidated Statements of Income — Three Months Ended March 27, 2016 and March 29, 2015</u>	4
<u>Consolidated Statements of Comprehensive Income — Three Months Ended March 27, 2016 and March 29, 2015</u>	5
<u>Consolidated Statements of Cash Flows — Three Months Ended March 27, 2016 and March 29, 2015</u>	6
<u>Notes to Condensed Consolidated Financial Statements</u>	7
<b><u>Item 2. Management’s Discussion and Analysis of Financial Condition and Results of Operations</u></b>	15
<b><u>Item 3. Quantitative and Qualitative Disclosures About Market Risk</u></b>	21
<b><u>Item 4. Controls and Procedures</u></b>	23
<b><u>PART II. OTHER INFORMATION</u></b>	
<b><u>Item 1. Legal Proceedings</u></b>	23
<b><u>Item 1A. Risk Factors</u></b>	23
<b><u>Item 2. Unregistered Sales of Equity Securities and Use of Proceeds</u></b>	23
<b><u>Item 6. Exhibits</u></b>	24

Table of Contents

## PART I. FINANCIAL INFORMATION

## Item 1. Financial Statements

## Papa John's International, Inc. and Subsidiaries

## Condensed Consolidated Balance Sheets

(In thousands, except per share amounts)	March 27, 2016 (Unaudited)	December 27, 2015
Assets		
Current assets:		
Cash and cash equivalents	\$ 17,272	\$ 21,006
Accounts receivable, net	56,683	63,320
Notes receivable, net	7,049	7,816
Income taxes receivable	48	272
Inventories	22,267	21,564
Prepaid expenses	18,450	20,372
Other current assets	9,460	8,941
Assets held for sale	9,094	9,299
Total current assets	140,323	152,590
Property and equipment, net	213,296	214,044
Notes receivable, less current portion, net	11,126	11,105
Goodwill	87,740	79,657
Deferred income taxes	2,041	2,415
Other assets	36,453	34,247
Total assets	\$ 490,979	\$ 494,058
Liabilities and stockholders' (deficit) equity		
Current liabilities:		
Accounts payable	\$ 33,582	\$ 43,492
Income and other taxes payable	8,805	8,527
Accrued expenses and other current liabilities	62,579	80,918
Total current liabilities	104,966	132,937
Deferred revenue	3,847	3,190
Long-term debt	316,717	255,146
Deferred income taxes	9,394	4,610
Other long-term liabilities	52,862	47,606
Total liabilities	487,786	443,489

Edgar Filing: PAPA JOHNS INTERNATIONAL INC - Form 10-Q

Redeemable noncontrolling interests	8,887	8,363
Stockholders' (deficit) equity:		
Preferred stock (\$0.01 par value per share; no shares issued)	—	—
Common stock (\$0.01 par value per share; issued 43,876 at March 27, 2016 and 43,731 at December 27, 2015)	439	437
Additional paid-in capital	157,175	158,348
Accumulated other comprehensive loss	(5,213)	(1,836)
Retained earnings	163,564	143,789
Treasury stock (6,540 shares at March 27, 2016 and 5,308 shares at December 27, 2015, at cost)	(334,828)	(271,557)
Total stockholders' (deficit) equity, net of noncontrolling interests	(18,863)	29,181
Noncontrolling interests in subsidiaries	13,169	13,025
Total stockholders' (deficit) equity	(5,694)	42,206
Total liabilities, redeemable noncontrolling interests and stockholders' (deficit) equity	\$ 490,979	\$ 494,058

See accompanying notes.

Table of Contents

Papa John's International, Inc. and Subsidiaries

Condensed Consolidated Statements of Income

(Unaudited)

(In thousands, except per share amounts)	Three Months Ended	
	March 27, 2014	March 29, 2015
Revenues:		
Domestic Company-owned restaurant sales	\$ 205,679	\$ 197,287
Domestic franchise royalties and fees	26,476	25,624
Domestic commissary and other sales	168,985	183,947
International	27,455	25,426
Total revenues	428,595	432,284
Costs and expenses:		
Operating costs (excluding depreciation and amortization shown separately below):		
Domestic Company-owned restaurant expenses	161,310	155,032
Domestic commissary and other expenses	156,806	170,339
International expenses	17,590	15,478
General and administrative expenses	40,247	43,749
Depreciation and amortization	9,744	10,041
Total costs and expenses	385,697	394,639
Operating income	42,898	37,645
Net interest expense	(1,489)	(1,209)
Income before income taxes	41,409	36,436
Income tax expense	13,358	12,197
Net income before attribution to noncontrolling interests	28,051	24,239
Income attributable to noncontrolling interests	(1,869)	(2,003)
Net income attributable to the Company	\$ 26,182	\$ 22,236
Calculation of income for earnings per share:		
Net income attributable to the Company	\$ 26,182	\$ 22,236
Change in noncontrolling interest redemption value	220	70
Net income attributable to participating securities	(110)	(100)
Net income attributable to common shareholders	\$ 26,292	\$ 22,206
Basic earnings per common share	\$ 0.69	\$ 0.56
Diluted earnings per common share	\$ 0.69	\$ 0.55
Basic weighted average common shares outstanding	37,931	39,827
Diluted weighted average common shares outstanding	38,297	40,510
Dividends declared per common share	\$ 0.175	\$ 0.14

See accompanying notes.

4

---



Table of Contents

Papa John's International, Inc. and Subsidiaries

Consolidated Statements of Comprehensive Income

(Unaudited)

(In thousands)	Three Months Ended	
	March 27, 2016	March 29, 2015
Net income before attribution to noncontrolling interests	\$ 28,051	\$ 24,239
Other comprehensive loss, before tax:		
Foreign currency translation adjustments	(2,071)	(1,541)
Interest rate swaps (1)	(3,289)	(1,084)
Other comprehensive loss, before tax	(5,360)	(2,625)
Income tax effect:		
Foreign currency translation adjustments	766	570
Interest rate swaps (2)	1,217	401
Income tax effect	1,983	971
Other comprehensive loss, net of tax	(3,377)	(1,654)
Comprehensive income before attribution to noncontrolling interests	24,674	22,585
Comprehensive loss, redeemable noncontrolling interests	(1,244)	(1,313)
Comprehensive loss, nonredeemable noncontrolling interests	(625)	(690)
Comprehensive income attributable to the Company	\$ 22,805	\$ 20,582

(1) Amounts reclassified out of accumulated other comprehensive loss into net interest (expense) income included \$317 and \$394 for the three months ended March 27, 2016 and March 29, 2015, respectively.

(2) The income tax effects of amounts reclassified out of accumulated other comprehensive loss into net interest (expense) income were \$117 and \$146 for the three months ended March 27, 2016 and March 29, 2015, respectively.

See accompanying notes.

Table of Contents

Papa John's International, Inc. and Subsidiaries

Consolidated Statements of Cash Flows

(Unaudited)

(In thousands)	Three Months Ended March 27, 2016	March 29, 2015
Operating activities		
Net income before attribution to noncontrolling interests	\$ 28,051	\$ 24,239
Adjustments to reconcile net income to net cash provided by operating activities:		
Provision for uncollectible accounts and notes receivable	216	659
Depreciation and amortization	9,744	10,041
Deferred income taxes	7,141	(36)
Stock-based compensation expense	2,172	2,264
Other	1,101	1,180
Changes in operating assets and liabilities, net of acquisitions:		
Accounts receivable	6,457	(1,312)
Income taxes receivable	223	5,899
Inventories	(612)	1,043
Prepaid expenses	1,938	2,755
Other current assets	(314)	(303)
Other assets and liabilities	(614)	(154)
Accounts payable	(10,007)	(3,828)
Income and other taxes payable	277	167
Accrued expenses and other current liabilities	(16,738)	(2,291)
Deferred revenue	934	(74)
	29,969	40,249

Net cash provided by  
operating activities

Investing activities

Purchases of property and equipment	(10,249)	(7,558)
Loans issued	(917)	(506)
Repayments of loans issued	1,275	1,083
Acquisitions, net of cash acquired	(11,202)	(341)
Other	159	20
Net cash used in investing activities	(20,934)	(7,302)

Financing activities

Net proceeds from issuance of long-term debt	61,500	549
Cash dividends paid	(6,628)	(5,545)
Excess tax benefit on equity awards	3,884	5,091
Tax payments for equity award issuances	(5,670)	(5,557)
Proceeds from exercise of stock options	922	2,210
Acquisition of Company common stock	(66,033)	(24,765)
Distributions to noncontrolling interest holders	(980)	(1,705)
Other	294	253
Net cash used in financing activities	(12,711)	(29,469)
Effect of exchange rate changes on cash and cash equivalents	(58)	(76)
Change in cash and cash equivalents	(3,734)	3,402
Cash and cash equivalents at beginning of period	21,006	20,122
Cash and cash equivalents at end of period	\$ 17,272	\$ 23,524

See accompanying notes.



Table of Contents

Papa John's International, Inc. and Subsidiaries

Notes to Condensed Consolidated Financial Statements (Unaudited)

March 27, 2016

1. Basis of Presentation

The accompanying unaudited condensed consolidated financial statements have been prepared in accordance with accounting principles generally accepted in the United States ("GAAP") for interim financial information and with the instructions to Form 10-Q and Article 10 of Regulation S-X. Accordingly, they do not include all of the information and footnotes required by GAAP for complete financial statements. In the opinion of management, all adjustments, consisting of normal recurring accruals, considered necessary for a fair presentation have been included. Operating results for the three months ended March 27, 2016 are not necessarily indicative of the results that may be expected for the fiscal year ended December 25, 2016. For further information, refer to the consolidated financial statements and footnotes thereto included in the Annual Report on Form 10-K for Papa John's International, Inc. (referred to as the "Company", "Papa John's" or in the first person notations of "we", "us" and "our") for the year ended December 27, 2015.

2. Significant Accounting Policies

Noncontrolling Interests

Papa John's has four joint venture arrangements in which there are noncontrolling interests. These joint ventures include 213 restaurants at March 27, 2016 and 200 restaurants at March 29, 2015. We are required to report the consolidated net income at amounts attributable to the Company and the noncontrolling interests. Additionally, disclosures are required to clearly identify and distinguish between the interests of the Company and the interests of the noncontrolling owners, including a disclosure on the face of the condensed consolidated statements of income attributable to the noncontrolling interest holder.

The income before income taxes attributable to these joint ventures for the three months ended March 27, 2016 and March 29, 2015 was as follows (in thousands):

	March 27, 2016	March 29, 2015
Papa John's International, Inc.	\$ 2,760	\$ 3,010
Noncontrolling interests	1,869	2,003
Total income before income taxes	\$ 4,629	\$ 5,013

Table of Contents

The following summarizes the redemption feature location and related accounting within the condensed consolidated balance sheets:

Type of Joint Venture Arrangement	Location within the Condensed Consolidated Balance Sheets	Recorded Value
Joint Venture with no redemption feature	Permanent equity	Carrying value
Option to require the Company to purchase their interest - currently redeemable	Temporary equity	Redemption value*
Option to require the Company to purchase their interest - not currently redeemable	Temporary equity	Carrying value

---

\*The change in redemption value is recorded as an adjustment to “Redeemable noncontrolling interests” and “Retained earnings” in the condensed consolidated balance sheets.

#### Deferred Income Tax Accounts and Tax Reserves

We are subject to income taxes in the United States and several foreign jurisdictions. Significant judgment is required in determining our provision for income taxes and the related assets and liabilities. The provision for income taxes includes income taxes paid, currently payable or receivable and those deferred. We use an estimated annual effective rate based on expected annual income to determine our quarterly provision for income taxes. Discrete items are recorded in the quarter in which they occur.

Deferred tax assets and liabilities are determined based on differences between financial reporting and tax basis of assets and liabilities and are measured using enacted tax rates and laws that are expected to be in effect when the differences reverse. Deferred tax assets are also recognized for the estimated future effects of tax loss carryforwards. The effect on deferred taxes of changes in tax rates is recognized in the period in which the new tax rate is enacted. As a result, our effective tax rate may fluctuate. Valuation allowances are established when necessary on a jurisdictional basis to reduce deferred tax assets to the amounts we expect to realize. As of March 27, 2016, we had a net deferred tax liability of approximately \$7.4 million.

Tax authorities periodically audit the Company. We record reserves and related interest and penalties for identified exposures as income tax expense. We evaluate these issues on a quarterly basis to adjust for events, such as statute of limitations expirations, court rulings or audit settlements, which may impact our ultimate payment for such exposures.

## Fair Value Measurements and Disclosures

The Company is required to determine the fair value of financial assets and liabilities based on the price that would be received to sell the asset or paid to transfer the liability to a market participant. Fair value is a market-based measurement, not an entity specific measurement. The fair value of certain assets and liabilities approximates carrying value because of the short-term nature of the accounts, including cash, accounts receivable and accounts payable. The carrying value of our notes receivable net of allowances also approximates fair value. The fair value of the amount outstanding under our revolving credit facility approximates its carrying value due to its variable market-based interest rate. These assets and liabilities are categorized as Level 1 as defined below.

Certain assets and liabilities are measured at fair value on a recurring basis and are required to be classified and disclosed in one of the following categories:

- Level 1: Quoted market prices in active markets for identical assets or liabilities.
  - Level 2: Observable market-based inputs or unobservable inputs that are corroborated by market data.
- Level 3: Unobservable inputs that are not corroborated by market data.



Table of Contents

Our financial assets and liabilities that were measured at fair value on a recurring basis as of March 27, 2016 and December 27, 2015 are as follows (in thousands):

	Carrying Value	Fair Value Measurements		
		Level 1	Level 2	Level 3
March 27, 2016				
Financial assets:				
Cash surrender value of life insurance policies (a)	\$ 19,099	\$ 19,099	\$ —	\$ —
Financial liabilities:				
Interest rate swaps (b)	5,561	—	5,561	—
December 27, 2015				
Financial assets:				
Cash surrender value of life insurance policies (a)	\$ 17,916	\$ 17,916	\$ —	\$ —
Financial liabilities:				
Interest rate swaps (b)	2,262	—	2,262	—

(a) Represents life insurance policies held in our non-qualified deferred compensation plan.

(b) The fair value of our interest rate swaps are based on the sum of all future net present value cash flows. The future cash flows are derived based on the terms of our interest rate swaps, as well as considering published discount factors, and projected London Interbank Offered Rates (“LIBOR”).

There were no transfers among levels within the fair value hierarchy during the three months ended March 27, 2016.

## Variable Interest Entity

Papa John’s domestic restaurants, both Company-owned and franchised, participate in Papa John’s Marketing Fund, Inc. (“PJMF”), a nonstock corporation designed to operate at break-even for the purpose of designing and administering advertising and promotional programs for all participating domestic restaurants. PJMF is a variable interest entity as it does not have sufficient equity to fund its operations without ongoing financial support and contributions from its members. Based on the ownership and governance structure and operating procedures of PJMF, we have determined that we do not have the power to direct the most significant activities of PJMF and therefore are not the primary beneficiary. Accordingly, consolidation of PJMF is not appropriate.

## Accounting Standards Adopted

## Income Taxes

In November 2015, the Financial Accounting Standards Board (“FASB”) issued Accounting Standards Update (“ASU”) 2015-17 “Income Taxes (Topic 740): Balance Sheet Classification of Deferred Taxes”. ASU 2015-17 requires the Company to classify deferred tax assets and liabilities as noncurrent amounts in the consolidated balance sheets. Such amounts were previously required to be classified as current and noncurrent assets and liabilities. The Company is required to adopt the provisions of ASU 2015-17 for fiscal 2017; however, the Company elected to retrospectively adopt the provisions in fiscal 2015, as allowed, and reclassified all previously reported current amounts as long-term.

## Deferred Debt Issuance Costs

In April 2015, the FASB issued “Interest – Imputation of Interest: Simplifying the Presentation of Debt Issuance Costs” (ASU 2015-03). The update requires that deferred debt issuance costs be reported as a reduction to long-term debt (previously reported in other noncurrent assets). We adopted ASU 2015-03 in the first quarter of 2016 and for all

## Table of Contents

retrospective periods, as required. The impact of the adoption was not material to our condensed consolidated financial statements. See Debt Footnote for more details.

### Accounting Standards to be Adopted in Future Periods

#### Employee Share-Based Payments

In March 2016, the FASB issued ASU 2016-09, “Compensation – Stock Compensation: Improvements to Employee Share-Based Payment Accounting” (ASU 2016-09). The guidance changes how companies account for certain aspects of share-based payment awards to employees, including the accounting for income taxes, forfeitures, and statutory tax withholding requirements, as well as classification in the statement of cash flows. ASU 2016-09 is effective for the Company beginning in fiscal 2017, with early application permitted. Based on the significance of our employee stock compensation program, we expect the adoption could have a material impact to our condensed consolidated statements of income.

#### Leases

In February 2016, the FASB issued ASU 2016-02, “Leases,” which amends leasing guidance by requiring companies to recognize a right-of-use asset and a lease liability for all operating and capital leases (financing) with lease terms greater than twelve months. The lease liability will be equal to the present value of lease payments. The lease asset will be based on the lease liability, subject to adjustment, such as for initial direct costs. For income statement purposes, leases will continue to be classified as operating or capital (financing) with lease expense in both cases calculated substantially the same as under the prior leasing guidance. ASU 2016-02 is effective for interim and annual periods beginning after December 15, 2018 (fiscal 2019 for the Company), and early adoption is permitted. The Company has not yet determined the effect of the adoption on its condensed consolidated financial statements.

#### Revenue from Contract with Customers

In May 2014, the FASB issued “Revenue from Contracts with Customers” (ASU 2014-09), a comprehensive new revenue recognition standard that will supersede nearly all existing revenue recognition guidance under GAAP. This update requires companies to recognize revenue at amounts that reflect the consideration to which the company expects to be entitled in exchange for those goods or services at the time of transfer. In doing so, companies will need to use more judgment and make more estimates than under today’s guidance. Such estimates may include identifying performance obligations in the contract, estimating the amount of variable consideration to include in the transaction price and allocating the transaction price to each separate performance obligation. Companies can either apply a full

retrospective adoption or a modified retrospective adoption.

We are required to adopt the new requirements in the first quarter of 2018. We are currently evaluating the method of adoption and impact of the new requirements on our consolidated financial statements. We currently do not believe the impact will be significant.

#### Reclassifications

Certain prior year captions have been combined in the condensed consolidated statement of income and certain amounts within the consolidated statement of cash flows have been reclassified to conform to the current year presentation.

#### 3. Calculation of Earnings Per Share

We compute earnings per share using the two-class method. The two-class method requires an earnings allocation formula that determines earnings per share for common shareholders and participating security holders according to dividends declared and participating rights in undistributed earnings. We consider time-based restricted stock awards to be participating securities because holders of such shares have non-forfeitable dividend rights. Under the two-class method, undistributed earnings allocated to participating securities are subtracted from net income attributable to the Company in determining net income attributable to common shareholders.

Table of Contents

Additionally, in accordance with Accounting Standards Codification (“ASC”) 480, “Distinguishing Liabilities from Equity”, the change in the redemption value for the noncontrolling interest of PJ Denver, LLC increases or decreases income attributable to common shareholders.

The calculations of basic and diluted earnings per common share are as follows (in thousands, except per-share data):

	Three Months Ended	
	March 27, 2016	March 29, 2015
Basic earnings per common share:		
Net income attributable to the Company	\$ 26,182	\$ 22,236
Change in noncontrolling interest redemption value	220	70
Net income attributable to participating securities	(110)	(100)
Net income attributable to common shareholders	\$ 26,292	\$ 22,206
Weighted average common shares outstanding	37,931	39,827
Basic earnings per common share	\$ 0.69	\$ 0.56
Diluted earnings per common share:		
Net income attributable to common shareholders	\$ 26,292	\$ 22,206
Weighted average common shares outstanding	37,931	39,827
Dilutive effect of outstanding equity awards (a)	366	683
Diluted weighted average common shares outstanding	38,297	40,510
Diluted earnings per common share	\$ 0.69	\$ 0.55

(a) Excludes 476 awards for the three months ended March 27, 2016 and 112 awards for the three months ended March 29, 2015, as the effect of including such awards would have been antidilutive.

#### 4. Acquisition of Restaurants

For the three months ended March 27, 2016, we completed the acquisition of 20 franchised Papa John’s restaurants located in Alabama, Florida and Kentucky in two separate transactions with an aggregate purchase price of \$11.2 million. These acquisitions were accounted for by the purchase method of accounting, whereby operating results subsequent to the acquisition date are included in our consolidated financial results.

The aggregate purchase price of the acquisitions has been allocated based on initial fair value estimates as follows (in thousands):

Property and equipment	\$ 1,028
Franchise rights	1,230
Goodwill	8,837
Other	107
Total purchase price	\$ 11,202

The excess of the purchase price over the aggregate fair value of net assets acquired was allocated to goodwill for the domestic Company-owned restaurants segment and is eligible for deduction over 15 years under U.S. tax regulations.

Table of Contents

## 5. Debt

Long-term debt consists of the following (in thousands):

	March 27, 2016	December 27, 2015
Outstanding debt	\$ 317,500	\$ 256,000
Debt issuance costs	(783)	(854)
Total long-term debt	\$ 316,717	\$ 255,146

Our outstanding debt is comprised entirely of a \$400 million unsecured revolving line of credit (“Credit Facility”) with an expiration date of October 31, 2019. Including outstanding letters of credit, the remaining availability under the Credit Facility was approximately \$58.8 million as of March 27, 2016. We have the option to increase the Credit Facility by an additional \$100 million.

The interest rate charged on outstanding balances is LIBOR plus 75 to 175 basis points. The commitment fee on the unused balance ranges from 15 to 25 basis points.

The Credit Facility contains customary affirmative and negative covenants, including financial covenants requiring the maintenance of specified fixed charges and leverage ratios. At March 27, 2016, we were in compliance with these covenants.

We attempt to minimize interest risk exposure by fixing our rate through the utilization of interest rate swaps, which are derivative financial instruments. Our swaps are entered into with financial institutions and have reset dates and critical terms that match those of our existing debt and the anticipated critical terms of future debt. By using a derivative instrument to hedge exposures to changes in interest rates, we expose ourselves to credit risk. Credit risk is the failure of the counterparty to perform under the terms of the derivative contract.

As of March 27, 2016, we have the following interest rate swap agreements, including three forward starting swaps executed in 2015 that become effective in 2018 upon expiration of the two existing swaps for \$125 million:

Effective Dates

Fixed Rates

	Floating Rate Debt		
July 30, 2013 through April 30, 2018	\$ 75 million	1.42	%
December 30, 2014 through April 30, 2018	\$ 50 million	1.36	%
April 30, 2018 through April 30, 2023	\$ 55 million	2.33	%
April 30, 2018 through April 30, 2023	\$ 35 million	2.36	%
April 30, 2018 through April 30, 2023	\$ 35 million	2.34	%

The weighted average interest rate on the revolving line of credit, including the impact of the interest rate swap agreements, was 2.1% for the three months ended March 27, 2016 and March 29, 2015. Interest paid, including payments made or received under the swaps, was \$1.6 million and \$1.3 million for the three months ended March 27, 2016 and March 29, 2015, respectively. As of March 27, 2016, the portion of the \$5.6 million interest rate swap liability that would be reclassified into earnings during the next twelve months as interest expense approximates \$723,000.

## 6. Segment Information

We have five reportable segments: domestic Company-owned restaurants, domestic commissaries, North America franchising, international operations and “all other” units. The domestic Company-owned restaurant segment consists of the operations of all domestic (“domestic” is defined as contiguous United States) Company-owned restaurants and derives its revenues principally from retail sales of pizza and side items, including breadsticks, cheesesticks, chicken poppers and wings, dessert items and canned or bottled beverages. The domestic commissary segment consists of the operations of our regional dough production and product distribution centers and derives its revenues principally from the sale and distribution of food and paper products to domestic Company-owned and franchised restaurants. The North America franchising segment consists of our franchise sales and support activities and derives its revenues from sales of



Table of Contents

franchise and development rights and collection of royalties from our franchisees located in the United States and Canada. The international operations segment principally consists of Company-owned restaurants in China and distribution sales to franchised Papa John's restaurants located in the United Kingdom, Mexico and China and our franchise sales and support activities, which derive revenues from sales of franchise and development rights and the collection of royalties from our international franchisees. International franchisees are defined as all franchise operations outside of the United States and Canada. All other business units that do not meet the quantitative thresholds for determining reportable segments, which are not operating segments, we refer to as our "all other" segment, which consists of operations that derive revenues from the sale, principally to Company-owned and franchised restaurants, of printing and promotional items, risk management services, and information systems and related services used in restaurant operations, including our point-of-sale system, online and other technology-based ordering platforms.

Generally, we evaluate performance and allocate resources based on profit or loss from operations before income taxes and intercompany eliminations. Certain administrative and capital costs are allocated to segments based upon predetermined rates or actual estimated resource usage. We account for intercompany sales and transfers as if the sales or transfers were to third parties and eliminate the activity in consolidation.

Our reportable segments are business units that provide different products or services. Separate management of each segment is required because each business unit is subject to different operational issues and strategies. No single external customer accounted for 10% or more of our consolidated revenues.

Table of Contents

Our segment information is as follows (in thousands):

	Three Months Ended	
	March 27, 2016	March 29, 2015
Revenues from external customers:		
Domestic Company-owned restaurants	\$ 205,679	\$ 197,287
Domestic commissaries	155,954	162,333
North America franchising	26,476	25,624
International	27,455	25,426
All others	13,031	21,614
Total revenues from external customers	\$ 428,595	\$ 432,284
Intersegment revenues:		
Domestic commissaries	\$ 58,326	\$ 57,887
North America franchising	713	671
International	65	75
All others	4,097	3,932
Total intersegment revenues	\$ 63,201	\$ 62,565
Income (loss) before income taxes:		
Domestic Company-owned restaurants	\$ 20,187	\$ 18,480
Domestic commissaries	11,546	11,800
North America franchising	23,580	22,319
International	3,038	1,344
All others	51	443
Unallocated corporate expenses	(16,332)	(17,205)
Elimination of intersegment profit	(661)	(745)
Total income before income taxes	\$ 41,409	\$ 36,436
Property and equipment:		
Domestic Company-owned restaurants	\$ 223,026	
Domestic commissaries	111,069	
International	16,213	
All others	48,823	
Unallocated corporate assets	182,882	
Accumulated depreciation and amortization	(368,717)	
Net property and equipment	\$ 213,296	

Table of Contents

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

## Overview

Papa John's International, Inc. (referred to as the "Company," "Papa John's" or in the first person notations of "we," "us" and "our") began operations in 1984. At March 27, 2016, there were 4,903 Papa John's restaurants (773 Company-owned and 4,130 franchised) operating in all 50 states and 40 international countries and territories. Our revenues are principally derived from retail sales of pizza and other food and beverage products to the general public by Company-owned restaurants, franchise royalties, sales of franchise and development rights, sales to franchisees of food and paper products, printing and promotional items, risk management services, and information systems and related services used in their operations.

The results of operations are based on the preparation of consolidated financial statements in conformity with accounting principles generally accepted in the United States ("GAAP"). The preparation of consolidated financial statements requires management to select accounting policies for critical accounting areas and make estimates and assumptions that affect the amounts reported in the consolidated financial statements. Significant changes in assumptions and/or conditions in our critical accounting policies could materially impact our operating results. See "Notes 1 and 2" of "Notes to Condensed Consolidated Financial Statements" for a discussion of the basis of presentation and the significant accounting policies.

## Restaurant Progression

	Three Months Ended	
	March 27, 2016	March 29, 2015
Papa John's Restaurant Progression:		
North America Company-owned:		
Beginning of period	707	686
Opened	2	3
Acquired	20	2
End of period	729	691
International Company-owned:		
Beginning of period	45	49
Closed	(1)	(1)
End of period	44	48
North America franchised:		

Edgar Filing: PAPA JOHNS INTERNATIONAL INC - Form 10-Q

Beginning of period	2,681	2,654
Opened	18	18
Closed	(18)	(20)
Divested	(20)	(2)
End of period	2,661	2,650
International franchised:		
Beginning of period	1,460	1,274
Opened	24	50
Closed	(15)	(14)
End of period	1,469	1,310
Total restaurants - end of period	4,903	4,699

Table of Contents

Results of Operations

Income Statement Presentation

We have streamlined our income statement presentation by combining certain income statement captions in the condensed consolidated statements of income and have conformed prior year amounts to this new presentation.

Review of Consolidated Operating Results

Revenues. Domestic Company-owned restaurant sales were \$205.7 million for the first quarter of 2016, an increase of \$8.4 million, or 4.3%, compared to the first quarter of 2015, primarily due to an increase in equivalent units, including 20 restaurants acquired from franchisees during the first quarter, and a 1.0% increase in comparable sales. “Equivalent units” represents the number of restaurants open at the beginning of a given period, adjusted for restaurants opened, closed, acquired or sold during the period on a weighted average basis. “Comparable sales” represents the change in year-over-year sales for the same base of restaurants for the same fiscal periods.

Domestic franchise royalties and fees were \$26.5 million for the first quarter of 2016, an increase of approximately \$850,000, or 3.3%, compared to the first quarter of 2015. The increase was primarily due to reduced levels of royalty incentives in the first quarter of 2016. Domestic franchise restaurant sales increased 0.3% to \$564.4 million in the first quarter of 2016, primarily due to a 0.6% increase in equivalent units, partially offset by a 0.2% decrease in comparable sales. Franchise restaurant sales are not included in Company revenues; however, our domestic royalty revenue is derived from these sales.

Domestic commissary and other sales decreased \$15.0 million, or 8.1%. The decrease was due to the prior year inclusion of approximately \$8.5 million of point-of-sale system (“FOCUS”) equipment sales to franchisees. The higher levels of 2015 FOCUS sales had no impact on 2015 operating results. Additionally, domestic commissary sales decreased by approximately \$6.4 million as revenues associated with lower pricing for certain commodities, including meats and dough, were somewhat offset by an increase in sales volumes.

International revenues increased approximately \$2.0 million, or 8.0%, primarily due to the following:

- The first quarter of 2016 includes sublease rental revenue in the United Kingdom of approximately \$1.6 million, which was shown net of the rental expenses in the prior year.
- Higher royalties and commissary revenues resulted from an increase in the number of restaurants and an increase in comparable sales of 5.7%, calculated on a constant dollar basis. International franchise restaurant sales increased

8.3% to \$154.3 million in the first quarter of 2016. International franchise restaurant sales are not included in Company revenues; however, our international royalty revenue is derived from these sales.

- These increases were somewhat offset by lower China Company-owned restaurant revenues.

The negative impact of foreign currency exchange rates was approximately \$1.9 million on international revenues.

Costs and expenses. The operating margin for domestic Company-owned restaurants was 21.6% in the first quarter of 2016 compared to 21.4% in the first quarter of 2015 and consisted of the following (dollars in thousands):

	Three Months Ended			
	March 27, 2016		March 29, 2015	
Restaurant sales	\$ 205,679		\$ 197,287	
Cost of sales	47,201	22.9%	47,504	24.1%
Other operating expenses	114,109	55.5%	107,528	54.5%
Total expenses	\$ 161,310 78.4%		\$ 155,032 78.6%	
Margin	\$ 44,369	21.6%	\$ 42,255	21.4%

Table of Contents

Domestic Company-owned restaurants cost of sales was approximately 1.2% lower primarily due to lower commodity costs, including meats and dough. Domestic restaurants other operating expenses were approximately 1.0% higher as a percentage of sales primarily due to higher labor costs, including minimum wage increases, and insurance costs.

The domestic commissary and other operating margin was 7.2% in the first quarter of 2016, compared to 7.4% in the first quarter of 2015 and consisted of the following (dollars in thousands):

	Three Months Ended March 27, 2016				March 29, 2015			
	Revenues \$	Expenses \$	Margin \$	Margin %	Revenues \$	Expenses \$	Margin \$	Margin %
Commissary	155,954	144,573	11,381	7.3%	162,333	149,736	12,597	7.8%
Other	13,031	12,233	798	6.1%	21,614	20,603	1,011	4.7%
Domestic commissary and other	\$ 168,985	\$ 156,806	\$ 12,179	7.2%	\$ 183,947	\$ 170,339	\$ 13,608	7.4%

The 0.5% lower margin for domestic commissary was primarily due to the reclassification of certain expenses from general and administrative to operating expenses beginning in the first quarter of 2016, which had no impact on commissary income before income taxes. The higher margin of 1.4% for “Other” was primarily due to the prior year including FOCUS equipment sales to franchisees which had no significant margin.

The international operating margin was 35.9% in the first quarter of 2016 compared to 39.1% in the first quarter of 2015. The 3.2% lower margin was primarily due to the following:

- Margin was 2.2% lower due to the gross presentation of certain sublease rental income and expenses. These amounts were shown net in the prior year and had no impact on income before income taxes.
- Company-owned China restaurants margins were lower as a percentage of revenues. The lower results for Company-owned China restaurants were substantially offset by lower depreciation expense on assets held for sale.

The international operating margins consisted of the following (dollars in thousands):

	Three Months Ended				March 29, 2015			
	March 27, 2016		Margin \$	Margin %	Revenues	Expenses	Margin \$	Margin %
Royalties and franchise development fees	\$ 6,868	\$ -	\$ 6,868		\$ 6,498	\$ -	\$ 6,498	
Restaurant, commissary and other	20,587	17,590	2,997	14.6%	18,928	15,478	3,450	18.2%
Total international	\$ 27,455	\$ 17,590	\$ 9,865	35.9%	\$ 25,426	\$ 15,478	\$ 9,948	39.1%

(a) The negative impact of foreign currency exchange rates was approximately \$700,000 in the first quarter of 2016.

General and administrative (G&A) expenses were \$40.3 million, or 9.4% of revenues in the first quarter of 2016, as compared to \$43.7 million, or 10.1% of revenues, in the same period of 2015. The decrease of \$3.5 million was primarily due to the following:

- Corporate G&A costs decreased primarily due to lower legal costs and lower expenses for our annual operators' conference due to the later timing of the event in the second quarter of 2016.



Table of Contents

- Domestic Company-owned restaurant supervisor bonuses decreased due to lower comparable sales bonus payouts.
- International G&A costs decreased primarily due to lower advertising spending; in the prior year, advertising levels were higher with the launch of the United Kingdom Quality Guarantee in 2015.

Depreciation and amortization. Depreciation and amortization was \$9.7 million (2.3% of revenues) for the first quarter of 2016 and \$10.0 million (2.3% of revenues) for the first quarter of 2015.

Net interest (expense) income. Net interest expense increased approximately \$300,000 primarily due to a higher average outstanding debt balance.

Income tax expense. The effective income tax rate was 32.3% for the first quarter of 2016 and 33.5% for the same period in 2015. Our effective income tax rate may fluctuate from quarter to quarter for various reasons, including the timing of various deductions and credits.

Diluted earnings per share. Diluted earnings per share were \$0.69 in the first quarter of 2016, compared to \$0.55 in the first quarter of 2015, an increase of \$0.14, or 25.5%.

## Discussion of Operating Results by Segment

See “Review of Consolidated Operating Results” above for revenue highlights.

First quarter 2016 income before income taxes was \$41.4 million, compared to \$36.4 million in the prior year comparable period, or a 13.6% increase as summarized in the following table on a reporting segment basis (in thousands):

(In thousands)	Three Months Ended		Increase (Decrease)
	March 27, 2016	March 29, 2015	
Domestic Company-owned restaurants	\$ 20,187	\$ 18,480	\$ 1,707
Domestic commissaries	11,546	11,800	(254)
North America franchising	23,580	22,319	1,261
International	3,038	1,344	1,694

Edgar Filing: PAPA JOHNS INTERNATIONAL INC - Form 10-Q

All others	51	443	(392)
Unallocated corporate expenses	(16,332)	(17,205)	873
Elimination of intersegment profits	(661)	(745)	84
Total income before income taxes	\$ 41,409	\$ 36,436	\$ 4,973

Changes in income before income taxes are summarized on a segment basis as follows:

- Domestic Company-owned Restaurant Segment. Domestic Company-owned restaurants' income before income taxes increased \$1.7 million in the first quarter of 2016. The increase was primarily due to lower commodity costs, including meats and dough.
- Domestic Commissary Segment. Domestic commissaries' income before income taxes decreased approximately \$250,000 primarily due to a lower margin, which was partially offset by higher sales volumes. We expect the 2016 margin will not be significantly different from the 2015 margin.
- North America Franchising Segment. North America Franchising income before income taxes increased approximately \$1.3 million primarily due to reduced royalty and development incentives.
- International Segment. International income before income taxes increased approximately \$1.7 million primarily due to the previously mentioned increase in units and comparable sales of 5.7%, which resulted in higher royalties and contributed to an increase in United Kingdom profits. The United Kingdom profits also increased from lower advertising costs; in the prior year, advertising costs were higher with the launch of the

Table of Contents

Quality Guarantee in 2015. These increases were somewhat offset by the negative impact of foreign currency exchange rates of approximately \$700,000.

- All Others Segment. The “All others” segment, which primarily includes our online and mobile ordering business and our wholly-owned print and promotions subsidiary, Preferred Marketing Solutions, decreased approximately \$400,000. The decrease was primarily due to higher support and infrastructure costs to support our digital ordering business, somewhat offset by higher revenues from a higher digital sales mix.
- Unallocated Corporate Segment. Unallocated corporate expenses were approximately \$900,000 lower primarily due to lower legal costs and lower expenses for our annual operators’ conference due to the later timing of the event in the second quarter of 2016.

## Liquidity and Capital Resources

## Debt

Our debt is comprised entirely of a \$400 million unsecured revolving credit facility with outstanding balances of \$317.5 million as of March 27, 2016 and \$256.0 million as of December 27, 2015. The increase in the outstanding balance was primarily due to borrowings to fund share repurchases, pay dividends, acquire restaurants and pay a legal settlement.

The interest rate charged on outstanding balances is LIBOR plus 75 to 175 basis points. The commitment fee on the unused balance ranges from 15 to 25 basis points. The increment over LIBOR and the commitment fee are determined quarterly based upon the ratio of total indebtedness to earnings before interest, taxes, depreciation and amortization (“EBITDA”), as defined by the Credit Facility. The remaining availability under the Credit Facility, reduced for outstanding letters of credit, was approximately \$58.8 million as of March 27, 2016.

As of March 27, 2016, we have the following interest rate swap agreements, including three forward starting swaps executed in 2015 that become effective in 2018 upon expiration of the two existing swaps for \$125 million:

Effective Dates	Floating Rate Debt	Fixed Rates	
July 30, 2013 through April 30, 2018	\$ 75 million	1.42	%
December 30, 2014 through April 30, 2018	\$ 50 million	1.36	%
April 30, 2018 through April 30, 2023	\$ 55 million	2.33	%
April 30, 2018 through April 30, 2023	\$ 35 million	2.36	%

Edgar Filing: PAPA JOHNS INTERNATIONAL INC - Form 10-Q

April 30, 2018 through April 30, 2023      \$ 35 million      2.34      %

Our Credit Facility contains affirmative and negative covenants, including the following financial covenants, as defined by the revolving credit facility:

	Permitted Ratio	Actual Ratio for the Quarter Ended March 27, 2016
Leverage Ratio	Not to exceed 3.0 to 1.0	1.95 to 1.0
Interest Coverage Ratio	Not less than 3.5 to 1.0	4.7 to 1.0

Our leverage ratio is defined as outstanding debt divided by consolidated EBITDA for the most recent four fiscal quarters. Our interest coverage ratio is defined as the sum of consolidated EBITDA and consolidated rental expense for the most recent four fiscal quarters divided by the sum of consolidated interest expense and consolidated rental expense for the most recent four fiscal quarters. We were in compliance with all covenants as of March 27, 2016.

Table of Contents

## Cash Flows

Cash flow provided by operating activities was \$30.0 million for the three months ended March 27, 2016, compared to \$40.2 million for the same period in 2015. The decrease of approximately \$10.3 million was primarily due to the payment of approximately \$12.5 million in the first quarter of 2016 for the previously disclosed legal settlement, partially offset by higher net income.

Our free cash flow, a non-GAAP financial measure, for the three months ended March 27, 2016 and March 29, 2015 was as follows (in thousands):

	Three Months Ended	
	March 27, 2016	March 29, 2015
Net cash provided by operating activities	\$ 29,969	\$ 40,249
Purchases of property and equipment	(10,249)	(7,558)
Free cash flow (a)	\$ 19,720	\$ 32,691

- (a) Free cash flow, a non-GAAP measure, is defined as net cash provided by operating activities (from the consolidated statements of cash flows) less the purchases of property and equipment. We view free cash flow as an important measure because it is one factor that management uses in determining the amount of cash available for discretionary investment. Free cash flow is not a term defined by GAAP and as a result our measure of free cash flow might not be comparable to similarly titled measures used by other companies. Free cash flow should not be construed as a substitute for or a better indicator of our performance than the Company's GAAP measures.

Cash flow used in investing activities was \$20.9 million for the three months ended March 27, 2016, compared to \$7.3 million for the same period in 2015, or an increase of \$13.6 million. The increase in cash flow used in investing activities was primarily due to the acquisition of 20 restaurants from franchisees for approximately \$11.2 million for the three months ended March 27, 2016.

We also require capital for share repurchases and the payment of cash dividends, which are funded by cash flow from operations and borrowings on our revolving credit facility. We repurchased \$66.0 million and \$24.8 million of common stock for the three months ended March 27, 2016 and March 29, 2015, respectively. Subsequent to March 27, 2016, through April 26, 2016, we repurchased an additional \$14.6 million of common stock. As of April 26, 2016, \$129.0 million remained available for repurchase under our Board of Directors' authorization.

We paid cash dividends of \$6.6 million (\$0.175 per common share) and \$5.6 million (\$0.14 per common share) in the first quarter of 2016 and 2015, respectively. Subsequent to the first quarter, on April 28, 2016, our Board of Directors declared a second quarter dividend of \$0.175 per common share (approximately \$6.6 million based on current shareholders of record). The dividend will be paid on May 20, 2016 to shareholders of record as of the close of business on May 9, 2016. The declaration and payment of any future dividends will be at the discretion of our Board of Directors, subject to the Company's financial results, cash requirements, and other factors deemed relevant by our Board of Directors.

#### Forward-Looking Statements

Certain matters discussed in this report, including information within Management's Discussion and Analysis of Financial Condition and Results of Operations, constitute forward-looking statements within the meaning of the federal securities laws. Generally, the use of words such as "expect," "intend," "estimate," "believe," "anticipate," "will," "foresee," "plan," "project," or similar words identify forward-looking statements that we intend to be included within the safe harbor protections provided by the federal securities laws. Such forward-looking statements may relate to projections or guidance concerning business performance, revenue, earnings, contingent liabilities, resolution of litigation, commodity costs, profit margins, unit growth, unit level performance, capital expenditures, and other financial and operational measures. Such statements are not guarantees of future performance and involve certain risks,

## Table of Contents

uncertainties and assumptions, which are difficult to predict and many of which are beyond our control. Therefore, actual outcomes and results may differ materially from those matters expressed or implied in such forward-looking statements. The risks, uncertainties and assumptions that are involved in our forward-looking statements include, but are not limited to:

- aggressive changes in pricing or other marketing or promotional strategies by competitors, which may adversely affect sales and profitability; and new product and concept developments by food industry competitors;
- changes in consumer preferences or consumer buying habits, including changes in general economic conditions or other factors that may affect consumer confidence and discretionary spending;
- the adverse impact on the Company or our results caused by product recalls, food quality or safety issues, incidences of foodborne illness, food contamination and other general public health concerns about our Company-owned or franchised restaurants or others in the restaurant industry;
- failure to maintain our brand strength, quality reputation and consumer enthusiasm for our better ingredients marketing and advertising strategy;
- the ability of the Company and its franchisees to meet planned growth targets and operate new and existing restaurants profitably, including difficulties finding qualified franchisees, store level employees or suitable sites;
- increases in food costs or sustained higher other operating costs. This could include increased employee compensation, benefits, insurance, tax rates, new regulatory requirements or increasing compliance costs;
- increases in insurance claims and related costs for programs funded by the Company up to certain retention limits, including medical, owned and non-owned automobiles, workers' compensation, general liability and property;
- disruption of our supply chain or commissary operations which could be caused by our sole source of supply of cheese or limited source of suppliers for other key ingredients or more generally due to weather, natural disasters including drought, disease, geopolitical or other disruptions beyond our control;
- increased risks associated with our international operations, including economic and political conditions, instability in our international markets, especially emerging markets, fluctuations in currency exchange rates, and difficulty in meeting planned sales targets and new store growth;
- the impact of current or future claims and litigation, including labor and employment-related claims;
- current or proposed legislation impacting our business;
- failure to effectively execute succession planning, and our reliance on the multiple roles of our founder, chairman and chief executive officer, who also serves as our brand spokesperson; and
- disruption of critical business or information technology systems, or those of our suppliers, and risks associated with systems failures and data privacy and security breaches, including theft of confidential Company, employee and customer information, including payment cards.

For a discussion of these and other risks that may cause actual results to differ from expectations, refer to "Part I. Item 1A. – Risk Factors" in our Annual Report on Form 10-K for the year ended December 27, 2015, as well as subsequent filings. We undertake no obligation to update publicly any forward-looking statements, whether as a result of future events, new information or otherwise, except as required by law.

### Item 3. Quantitative and Qualitative Disclosures About Market Risk

#### Interest Rate Risk

Our debt is comprised entirely of a \$400 million unsecured revolving credit facility with outstanding balances of \$317.5 million as of March 27, 2016 and \$256.0 million as of December 27, 2015 and a maturity date of October 31, 2019. Additionally, we have the option to increase the amount available by an additional \$100 million. The interest rate charged on outstanding balances is LIBOR plus 75 to 175 basis points. The commitment fee on the unused balance ranges from 15 to 25 basis points.

We attempt to minimize interest risk exposure by fixing our rate through the utilization of interest rate swaps, which are derivative financial instruments. Our swaps are entered into with financial institutions and have reset dates and critical terms that match those of our existing debt and the anticipated critical terms of future debt. By using a derivative



Table of Contents

instrument to hedge exposures to changes in interest rates, we expose ourselves to credit risk. Credit risk is the failure of the counterparty to perform under the terms of the derivative contract.

As of March 27, 2016, we have the following interest rate swap agreements, including three forward starting swaps executed in 2015 that become effective in 2018 upon expiration of the two existing swaps for \$125 million:

Effective Dates	Floating Rate Debt	Fixed Rates	
July 30, 2013 through April 30, 2018	\$ 75 million	1.42	%
December 30, 2014 through April 30, 2018	\$ 50 million	1.36	%
April 30, 2018 through April 30, 2023	\$ 55 million	2.33	%
April 30, 2018 through April 30, 2023	\$ 35 million	2.36	%
April 30, 2018 through April 30, 2023	\$ 35 million	2.34	%

The weighted average interest rate on the revolving line of credit, including the impact of the interest rate swap agreements, was 2.1% as of March 27, 2016. An increase in the present interest rate of 100 basis points on the line of credit balance outstanding as of March 27, 2016, including the impact of the interest rate swaps, would increase interest expense by \$1.9 million.

## Foreign Currency Exchange Rate Risk

We are exposed to foreign currency exchange rate fluctuations from our operations outside of the United States, which can adversely impact our revenues, net income and cash flows. Our international operations principally consist of Company-owned restaurants in China and distribution sales to franchised Papa John's restaurants located in the United Kingdom, Mexico and China and our franchise sales and support activities, which derive revenues from sales of franchise and development rights and the collection of royalties from our international franchisees. Approximately 6% of our revenues for both of the three months ended March 27, 2016 and March 29, 2015 were derived from these operations.

We have not historically hedged our exposure to foreign currency fluctuations. Foreign currency exchange rate fluctuations had a negative impact on our revenues of approximately \$1.9 million and \$1.8 million for the three months ended March 27, 2016 and March 29, 2015, respectively, and a negative impact on our income before income taxes of \$700,000 and \$500,000 for the three months ended March 27, 2016 and March 29, 2015, respectively.

## Commodity Price Risk

In the ordinary course of business, the food and paper products we purchase, including cheese (our largest individual food cost item), are subject to seasonal fluctuations, weather, availability, demand and other factors that are beyond our control. We have pricing agreements with some of our vendors, including forward pricing agreements for a portion of our cheese purchases for our domestic Company-owned restaurants, which are accounted for as normal purchases; however, we still remain exposed to on-going commodity volatility.

Table of Contents

The following table presents the actual average block price for cheese by quarter through the first quarter of 2016 and the projected average block price for cheese by quarter through 2016 (based on the April 26, 2016 Chicago Mercantile Exchange cheese futures market prices):

	2016 Projected Block Price	2015 Actual Block Price
Quarter 1	\$ 1.473	\$ 1.538
Quarter 2	1.476	1.630
Quarter 3	1.560	1.684
Quarter 4	1.620	1.602
Full Year	\$ 1.532	* \$ 1.614

\*The full year estimate is based on futures prices and does not include the impact of forward pricing agreements for a portion of our cheese purchases for our domestic Company-owned restaurants. Additionally, the price charged to restaurants can vary somewhat by quarter from the actual block price based upon our monthly pricing mechanism.

## Item 4. Controls and Procedures

Under the supervision and with the participation of the Company's management, including its chief executive officer and chief financial officer, the Company has evaluated the effectiveness of the design and operation of its disclosure controls and procedures (as defined in Rules 13a-15(e) and 15d-15(e) under the Securities Exchange Act of 1934, as amended (the "Exchange Act")). Based upon this evaluation, the chief executive officer and chief financial officer have concluded that, as of the end of the period covered by this report, the Company's disclosure controls and procedures were effective.

During the most recently completed fiscal quarter, there was no change made in the Company's internal control over financial reporting (as defined in Rules 13a-15(f) and 15d-15(f) under the Exchange Act) that has materially affected, or is reasonably likely to materially affect, the Company's internal control over financial reporting.

## PART II. OTHER INFORMATION

## Item 1. Legal Proceedings

The Company is involved in a number of lawsuits, claims, investigations and proceedings consisting of intellectual property, employment, consumer, commercial and other matters arising in the ordinary course of business. In accordance with Accounting Standards Codification 450, "Contingencies", the Company has made accruals with respect to these matters, where appropriate, which are reflected in the Company's consolidated financial statements. We review these provisions at least quarterly and adjust these provisions to reflect the impact of negotiations, settlements, rulings, advice of legal counsel and other information and events pertaining to a particular case.

#### Item 1A. Risk Factors

There have been no material changes in the risk factors previously disclosed in the Company's Annual Report on Form 10-K for the fiscal year ended December 27, 2015.

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

Our Board of Directors has authorized the repurchase of up to \$1.525 billion of common stock under a share repurchase program that began on December 9, 1999 and expires on February 28, 2017. Through March 27, 2016, a total of 108.7 million shares with an aggregate cost of \$1.4 billion and an average price of \$12.70 per share have been repurchased under this program. Subsequent to March 27, 2016, through April 26, 2016, we acquired an additional 262,000 shares at an aggregate cost of \$14.6 million. As of April 26, 2016, approximately \$129.0 million remained available for repurchase of common stock under this authorization.

Table of Contents

The following table summarizes our repurchases by fiscal period during the three months ended March 27, 2016 (in thousands, except per-share amounts):

Fiscal Period	Total Number of Shares Purchased	Average Price Paid per Share	Total Number of Shares Purchased as Part of Publicly Announced Plans or Programs	Maximum Dollar Value of Shares that May Yet Be Purchased Under the Plans or Programs
12/28/2015 - 01/24/2016	399	\$ 52.06	107,854	\$ 188,900
01/25/2016 - 02/21/2016	537	\$ 47.67	108,391	\$ 163,304
02/22/2016 - 03/27/2016	350	\$ 56.14	108,741	\$ 143,648

The Company utilizes a written trading plan under Rule 10b5-1 under the Exchange Act from time to time to facilitate the repurchase of shares of our common stock under this share repurchase program. There can be no assurance that we will repurchase shares of our common stock either through a Rule 10b5-1 trading plan or otherwise.

During fiscal quarter ended March 27, 2016, the Company acquired approximately 27,000 shares of its common stock from employees to satisfy minimum tax withholding obligations that arose upon (i) vesting of restricted stock granted pursuant to approved plans and (ii) distribution of shares of common stock issued pursuant to deferred compensation obligations.

## Item 6. Exhibits

Exhibit Number	Description
31.1	Certification of Chief Executive Officer Pursuant to Exchange Act Rule 13a-15(e), As Adopted Pursuant to Section 302 of the Sarbanes-Oxley Act of 2002.
31.2	Certification of Chief Financial Officer Pursuant to Exchange Act Rule 13a-15(e), As Adopted Pursuant to Section 302 of the Sarbanes-Oxley Act of 2002.
32.1	Certification of Chief Executive Officer Pursuant to 18 U.S.C. Section 1350, As Adopted Pursuant to Section 906 of the Sarbanes-Oxley Act of 2002.

Edgar Filing: PAPA JOHNS INTERNATIONAL INC - Form 10-Q

- 32.2 Certification of Chief Financial Officer Pursuant to 18 U.S.C. Section 1350, As Adopted Pursuant to Section 906 of the Sarbanes-Oxley Act of 2002.
- 101 Financial statements from the quarterly report on Form 10-Q of Papa John's International, Inc. for the quarter ended March 27, 2016, filed on May 3, 2016, formatted in XBRL: (i) the Condensed Consolidated Balance Sheets, (ii) the Condensed Consolidated Statements of Income, (iii) the Consolidated Statements of Comprehensive Income, (iv) the Consolidated Statements of Cash Flows and (v) the Notes to Condensed Consolidated Financial Statements.

Table of Contents

SIGNATURE

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.

PAPA JOHN'S INTERNATIONAL, INC.  
(Registrant)

Date: May 3, 2016      /s/ Lance F. Tucker  
Lance F. Tucker  
Senior Vice President,  
Chief Financial Officer,  
Chief Administrative Officer and Treasurer