

CRACKER BARREL OLD COUNTRY STORE, INC  
Form 10-Q  
June 02, 2015

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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 May 1, 2015

OR

Transition report pursuant to Section 13 or 15(d) of the Securities Exchange Act of 1934  
For the transition period from \_\_\_\_\_ to \_\_\_\_\_

Commission file number: 001 25225

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Cracker Barrel Old Country Store, Inc.  
(Exact name of registrant as specified in its charter)

Tennessee 62 0812904  
(State or other jurisdiction of incorporation or organization) (I.R.S. Employer Identification Number)

305 Hartmann Drive  
Lebanon, Tennessee 37087-4779  
(Address of principal executive offices) (Zip code)

Registrant's telephone number, including area code: (615) 444-5533

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

Yes No

Indicate by check mark whether the registrant has submitted electronically and posted on its corporate Web site, if any, every Interactive Data File required to be submitted and posted pursuant to Rule 405 of Regulation S-T (§ 232.405 of this chapter) during the preceding 12 months (or for such shorter period that the registrant was required to submit and post such files). Yes No

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

Yes      No

Indicate the number of shares outstanding of each of the registrant's classes of common stock, as of the latest practicable date.

23,957,780 Shares of Common Stock

Outstanding as of May 26, 2015

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CRACKER BARREL OLD COUNTRY STORE, INC.

FORM 10-Q

For the Quarter Ended May 1, 2015

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## PART I – FINANCIAL INFORMATION

## ITEM 1. Financial Statements

CRACKER BARREL OLD COUNTRY STORE, INC.  
CONDENSED CONSOLIDATED BALANCE SHEETS

(In thousands, except share data)

(Unaudited)

|  | May 1,<br>2015 | August 1,<br>2014* |
|--|----------------|--------------------|
| <b>ASSETS</b>  |                |                    |
| Current Assets:  |                |                    |
| Cash and cash equivalents  | \$202,054      | \$119,361          |
| Accounts receivable  | 25,858         | 22,704             |
| Income taxes receivable  | 8,269          | 2,973              |
| Inventories  | 136,405        | 165,426            |
| Prepaid expenses and other current assets  | 13,826         | 11,997             |
| Deferred income taxes  | 4,964          | 7,188              |
| Total current assets   | 391,376        | 329,649            |
| Property and equipment   | 1,909,628      | 1,867,121          |
| Less: Accumulated depreciation and amortization of capital leases  | 866,730        | 823,837            |
| Property and equipment – net   | 1,042,898      | 1,043,284          |
| Other assets   | 66,793         | 59,315             |
| Total assets   | \$1,501,067    | \$1,432,248        |
| <b>LIABILITIES AND SHAREHOLDERS' EQUITY</b>  |                |                    |
| Current Liabilities:   |                |                    |
| Accounts payable   | \$89,327       | \$98,477           |
| Current maturities of long-term debt   | --             | 25,000             |
| Deferred revenue   | 63,457         | 49,825             |
| Current interest rate swap liability   | 68             | 4,704              |
| Other current liabilities  | 163,077        | 166,432            |
| Total current liabilities  | 315,929        | 344,438            |
| Long-term debt   | 400,000        | 375,000            |
| Long-term interest rate swap liability   | 9,633          | 3,239              |
| Other long-term obligations  | 130,083        | 123,221            |
| Deferred income taxes  | 61,350         | 57,709             |
| Commitments and Contingencies (Note 12)  |                |                    |
| Shareholders' Equity:  |                |                    |
| Preferred stock – 100,000,000 shares of \$.01 par value authorized; 300,000 shares designated as Series A Junior Participating Preferred Stock; no shares issued                         | --             | --                 |
| Common stock – 400,000,000 shares of \$.01 par value authorized; 23,949,084 shares issued and outstanding at May 1, 2015, and 23,821,227 shares issued and outstanding at August 1, 2014 | 239            | 238                |
| Additional paid-in capital   | 50,555         | 39,969             |
| Accumulated other comprehensive loss   | (4,027 )       | (4,733 )           |
| Retained earnings  | 537,305        | 493,167            |
| Total shareholders' equity   | 584,072        | 528,641            |
| Total liabilities and shareholders' equity   | \$1,501,067    | \$1,432,248        |

See Notes to unaudited Condensed Consolidated Financial Statements.

\* This Condensed Consolidated Balance Sheet has been derived from the audited Consolidated Balance Sheet as of August 1, 2014, as filed with the Securities and Exchange Commission in the Company's Annual Report on Form 10-K for the fiscal year ended August 1, 2014.

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CONDENSED CONSOLIDATED STATEMENTS OF INCOME(In thousands, except share data)  
(Unaudited)

|   | Quarter Ended  |                | Nine Months Ended |                |
|---|----------------|----------------|-------------------|----------------|
|   | May 1,<br>2015 | May 2,<br>2014 | May 1,<br>2015    | May 2,<br>2014 |
| Total revenue   | \$683,705      | \$643,298      | \$2,123,099       | \$1,990,930    |
| Cost of goods sold (exclusive of depreciation and rent) | 216,142        | 201,507        | 700,592           | 650,451        |
| Labor and other related expenses                        | 246,805        | 242,977        | 740,806           | 718,466        |
| Other store operating expenses                          | 126,711        | 121,060        | 390,609           | 374,501        |
| Store operating income                                  | 94,047         | 77,754         | 291,092           | 247,512        |
| General and administrative expenses                     | 38,570         | 32,541         | 108,952           | 99,356         |
| Operating income  | 55,477         | 45,213         | 182,140           | 148,156        |
| Interest expense  | 4,030          | 4,327          | 13,138            | 13,205         |
| Income before income taxes                              | 51,447         | 40,886         | 169,002           | 134,951        |
| Provision for income taxes                              | 16,130         | 12,158         | 52,498            | 42,008         |
| Net income  | \$35,317       | \$28,728       | \$116,504         | \$92,943       |
| Net income per share:                                   |                |                |                   |                |
| Basic   | \$1.48         | \$1.21         | \$4.87            | \$3.90         |
| Diluted   | \$1.47         | \$1.20         | \$4.85            | \$3.88         |
| Weighted average shares:                                |                |                |                   |                |
| Basic   | 23,937,844     | 23,820,309     | 23,904,945        | 23,816,841     |
| Diluted   | 24,066,061     | 23,978,474     | 24,033,296        | 23,958,058     |
| Dividends declared per share                            | \$1.00         | \$1.75         | \$3.00            | \$3.25         |
| Dividends paid per share                                | \$1.00         | \$0.75         | \$3.00            | \$2.25         |

See Notes to unaudited Condensed Consolidated Financial Statements.

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CRACKER BARREL OLD COUNTRY STORE, INC.

CONDENSED CONSOLIDATED STATEMENTS OF COMPREHENSIVE INCOME

(Unaudited and in thousands)

|   | Quarter Ended  |                | Nine Months Ended |                |
|---|----------------|----------------|-------------------|----------------|
|   | May 1,<br>2015 | May 2,<br>2014 | May 1,<br>2015    | May 2,<br>2014 |
| Net income  | \$35,317       | \$28,728       | \$116,504         | \$92,943       |
| Other comprehensive income before income tax expense: |                |                |                   |                |
| Change in fair value of interest rate swaps           | 8,035          | 1,984          | 1,148             | 3,361          |
| Income tax expense                                    | 3,098          | 766            | 442               | 1,296          |
| Other comprehensive income, net of tax                | 4,937          | 1,218          | 706               | 2,065          |
| Comprehensive income                                  | \$40,254       | \$29,946       | \$117,210         | \$95,008       |

See Notes to unaudited Condensed Consolidated Financial Statements.

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CONDENSED CONSOLIDATED STATEMENTS OF CASH FLOWS  
(Unaudited and in thousands)

|   | Nine Months Ended |                |
|---|-------------------|----------------|
|   | May 1,<br>2015    | May 2,<br>2014 |
| Cash flows from operating activities:   |                   |                |
| Net income  | \$ 116,504        | \$ 92,943      |
| Adjustments to reconcile net income to net cash provided by operating activities:   |                   |                |
| Depreciation and amortization   | 53,928            | 50,601         |
| Loss on disposition of property and equipment                                       | 5,413             | 3,159          |
| Share-based compensation  | 10,795            | 6,132          |
| Excess tax benefit from share-based compensation                                    | (3,224 )          | (612 )         |
| Changes in assets and liabilities:  |                   |                |
| Inventories   | 29,021            | (691 )         |
| Other current assets  | (7,055 )          | (3,918 )       |
| Accounts payable  | (9,150 )          | (38,666 )      |
| Deferred revenue  | 13,632            | 10,663         |
| Other current liabilities   | (3,971 )          | (18,871 )      |
| Other long-term assets and liabilities  | 10,787            | 457            |
| Net cash provided by operating activities   | 216,680           | 101,197        |
| Cash flows from investing activities:   |                   |                |
| Purchase of property and equipment  | (60,239 )         | (63,195 )      |
| Proceeds from insurance recoveries of property and equipment                        | 184               | 858            |
| Proceeds from sale of property and equipment  | 1,563             | 1,572          |
| Net cash used in investing activities   | (58,492 )         | (60,765 )      |
| Cash flows from financing activities:   |                   |                |
| Proceeds from issuance of long-term debt  | 406,250           | --             |
| (Taxes withheld) and proceeds from issuance of share-based compensation awards, net | (3,432 )          | (8,430 )       |
| Principal payments under long-term debt and other long-term obligations             | (406,250)         | (1 )           |
| Purchases and retirement of common stock  | --                | (12,473 )      |
| Deferred financing costs  | (3,537 )          | --             |
| Dividends on common stock   | (71,750 )         | (53,619 )      |
| Excess tax benefit from share-based compensation                                    | 3,224             | 612            |
| Net cash used in financing activities   | (75,495 )         | (73,911 )      |
| Net increase (decrease) in cash and cash equivalents                                | 82,693            | (33,479 )      |
| Cash and cash equivalents, beginning of period                                      | 119,361           | 121,718        |
| Cash and cash equivalents, end of period  | \$ 202,054        | \$ 88,239      |
| Supplemental disclosures of cash flow information:                                  |                   |                |
| Cash paid during the period for:  |                   |                |
| Interest, net of amounts capitalized  | \$ 11,682         | \$ 11,950      |
| Income taxes  | \$ 46,374         | \$ 48,675      |
| Supplemental schedule of non-cash investing and financing activities:               |                   |                |
| Capital expenditures accrued in accounts payable                                    | \$ 3,842          | \$ 4,985       |



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|  |          |           |
|--|----------|-----------|
| Change in fair value of interest rate swaps          | \$1,148  | \$3,361   |
| Change in deferred tax asset for interest rate swaps | \$(442)  | \$(1,296) |
| Dividends declared but not yet paid                  | \$24,610 | \$41,900  |

See Notes to unaudited Condensed Consolidated Financial Statements.

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CRACKER BARREL OLD COUNTRY STORE, INC.

NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS

(In thousands, except percentages, share and per share data)

(Unaudited)

1. Condensed Consolidated Financial Statements

Cracker Barrel Old Country Store, Inc. and its affiliates (collectively, in these Notes to Condensed Consolidated Financial Statements, the “Company”) are principally engaged in the operation and development in the United States of the Cracker Barrel Old Country Store® (“Cracker Barrel”) concept.

The condensed consolidated balance sheets at May 1, 2015 and August 1, 2014 and the related condensed consolidated statements of income, comprehensive income and cash flows for the quarters and nine months ended May 1, 2015 and May 2, 2014, respectively, have been prepared by the Company in accordance with accounting principles generally accepted in the United States of America (“GAAP”) and pursuant to the rules and regulations of the Securities and Exchange Commission (the “SEC”) without audit. In the opinion of management, all adjustments (consisting of normal and recurring items) necessary for a fair presentation of such condensed consolidated financial statements have been made. The results of operations for any interim period are not necessarily indicative of results for a full year.

These condensed consolidated financial statements should be read in conjunction with the audited consolidated financial statements and notes thereto contained in the Company’s Annual Report on Form 10-K for the year ended August 1, 2014 (the “2014 Form 10-K”). The accounting policies used in preparing these condensed consolidated financial statements are the same as described in the 2014 Form 10-K. References to a year in these Notes to Condensed Consolidated Financial Statements are to the Company’s fiscal year unless otherwise noted.

Recent Accounting Pronouncements Not Adopted

Reporting Discontinued Operations and Disclosures of Disposals of Components of an Entity

In April 2014, the Financial Accounting Standards Board (“FASB”) issued accounting guidance which changes the criteria for disposals to qualify as discontinued operations and requires new disclosures about disposals of both discontinued operations and certain other disposals that do not meet the new definition. This accounting guidance is effective for fiscal years beginning on or after December 15, 2014 and interim periods within those years on a prospective basis. The Company is currently evaluating the impact of adopting this accounting guidance, but it is not expected to have a significant impact on the Company’s consolidated financial position or results of operations upon adoption in the first quarter of 2016.

Revenue Recognition

In May 2014, the FASB issued accounting guidance which clarifies the principles for recognizing revenue and provides a comprehensive model for revenue recognition. Revenue recognition should depict the transfer of goods or services to a customer at an amount that reflects the consideration a company expects to receive in exchange for those goods or services. The guidance also requires additional disclosures about the nature, amount, timing and uncertainty of revenue and cash flows arising from customer contracts. This accounting guidance is effective for fiscal years beginning after December 15, 2016 and interim periods within those years. Early application is not permitted. A company may apply this accounting guidance either retrospectively or using the cumulative effect transition method. The Company is currently evaluating the impact of adopting this accounting guidance in the first quarter of 2018.



Index2. Fair Value Measurements

The Company's assets and liabilities measured at fair value on a recurring basis at May 1, 2015 were as follows:

|   | Quoted<br>Prices<br>in Active<br>Markets<br>for<br>Identical<br>Assets<br>(Level 1) | Significant<br>Other<br>Observable<br>Inputs<br>(Level 2) | Significant<br>Unobservable<br>Inputs<br>(Level 3) | Fair<br>Value |
|---|---|---|--|---------------|
| Cash equivalents*                         | \$ 128,072  | \$ --   | \$ --  | \$ 128,072    |
| Interest rate swap asset (see Note 5)     | --  | 3,146   | --   | 3,146         |
| Deferred compensation plan assets**       | 26,847  | --  | --   | 26,847        |
| Total assets at fair value                | \$ 154,919  | \$ 3,146  | \$ --  | \$ 158,065    |
| Interest rate swap liability (see Note 5) | \$--  | \$ 9,701  | \$ --  | \$ 9,701      |
| Total liabilities at fair value           | \$--  | \$ 9,701  | \$ --  | \$ 9,701      |

The Company's assets and liabilities measured at fair value on a recurring basis at August 1, 2014 were as follows:

|   | Quoted<br>Prices<br>in<br>Active<br>Markets<br>for<br>Identical<br>Assets<br>(Level<br>1) | Significant<br>Other<br>Observable<br>Inputs<br>(Level 2) | Significant<br>Unobservable<br>Inputs<br>(Level 3) | Fair<br>Value |
|---|---|---|--|---------------|
| Cash equivalents*                         | \$ 63,068   | \$ --   | \$ --  | \$ 63,068     |
| Interest rate swap asset (see Note 5)     | --  | 240   | --   | 240           |
| Deferred compensation plan assets**       | 25,322  | --  | --   | 25,322        |
| Total assets at fair value                | \$ 88,390   | \$ 240  | \$ --  | \$ 88,630     |
| Interest rate swap liability (see Note 5) | \$--  | \$ 7,943  | \$ --  | \$ 7,943      |
| Total liabilities at fair value           | \$--  | \$ 7,943  | \$ --  | \$ 7,943      |

\*Consists of money market fund investments.

\*\*Represents plan assets invested in mutual funds established under a rabbi trust for the Company's non-qualified savings plan and is included in the Consolidated Balance Sheets as other assets.

The Company's money market fund investments and deferred compensation plan assets are measured at fair value using quoted market prices. The fair values of the Company's interest rate swap assets and liabilities are determined based on the present value of expected future cash flows. Since the values of the Company's interest rate swaps are based on the LIBOR forward curve, which is observable at commonly quoted intervals for the full terms of the swaps, it is considered a Level 2 input. Non-performance risk is reflected in determining the fair value of the interest rate swaps by using the Company's credit spread less the risk-free interest rate, both of which are observable at commonly

quoted intervals for the terms of the swaps. Thus, the adjustment for non-performance risk is also considered a Level 2 input.

The fair values of the Company's accounts receivable and accounts payable approximate their carrying amounts because of their short duration. The fair value of the Company's variable rate debt, based on quoted market prices, which are considered Level 1 inputs, approximates its carrying amount at May 1, 2015 and August 1, 2014.

### 3. Inventories

Inventories were comprised of the following at:

|            | May 1,<br>2015 | August 1,<br>2014 |
|------------|----------------|-------------------|
| Retail     | \$98,907       | \$128,386         |
| Restaurant | 21,928         | 22,371            |
| Supplies   | 15,570         | 14,669            |
| Total      | \$136,405      | \$165,426         |

Index4. Debt

Long-term debt consisted of the following at:

|   | May 1,<br>2015 | August 1,<br>2014 |
|---|----------------|-------------------|
| Revolving credit facility expiring on January 8, 2020 | \$400,000      | \$--              |
| Revolving credit facility expiring on July 8, 2016    | --             | 212,500           |
| Term loan payable on or before July 8, 2016           | --             | 187,500           |
|   | 400,000        | 400,000           |
| Current maturities                                    | --             | 25,000            |
| Long-term debt  | \$400,000      | \$375,000         |

On January 8, 2015, the Company entered into a five-year \$750,000 revolving credit facility (the "2015 Revolving Credit Facility"). The 2015 Revolving Credit Facility replaced a term loan totaling \$181,250 and a \$218,750 revolving credit facility ("Prior Credit Facility"). In the second quarter of 2015, loan acquisition costs associated with the 2015 Revolving Credit Facility were capitalized in the amount of \$3,537 and will be amortized over the five-year term of the 2015 Revolving Credit Facility. Loan acquisition costs of \$412 associated with the Prior Credit Facility were written off in the second quarter of 2015 and are recorded in interest expense in the Condensed Consolidated Statement of Income.

At May 1, 2015, the Company had \$400,000 of outstanding borrowings under the 2015 Revolving Credit Facility and \$11,530 of standby letters of credit, which reduce the Company's borrowing availability under the 2015 Revolving Credit Facility (see Note 12 for more information on the Company's standby letters of credit). At May 1, 2015, the Company had \$338,470 in borrowing availability under the 2015 Revolving Credit Facility.

In accordance with the 2015 Revolving Credit Facility, outstanding borrowings bear interest, at the Company's election, either at LIBOR or prime plus a percentage point spread based on certain specified financial ratios under the 2015 Revolving Credit Facility. As of May 1, 2015, the Company's outstanding borrowings were swapped at a weighted average interest rate of 3.48% (see Note 5 for information on the Company's interest rate swaps).

The 2015 Revolving Credit Facility contains customary financial covenants, which include maintenance of a maximum consolidated total leverage ratio and a minimum consolidated interest coverage ratio. At May 1, 2015, the Company was in compliance with all debt covenants.

The 2015 Revolving Credit Facility also imposes restrictions on the amount of dividends the Company is permitted to pay and the amount of shares the Company is permitted to repurchase. Under the 2015 Revolving Credit Facility, provided there is no default existing and the total of the Company's availability under the 2015 Revolving Credit Facility plus the Company's cash and cash equivalents on hand is at least \$100,000 (the "cash availability"), the Company may declare and pay cash dividends on shares of its common stock and repurchase shares of its common stock (1) in an unlimited amount if at the time such dividend or repurchase is made the Company's consolidated total leverage ratio is 3.00 to 1.00 or less and (2) in an aggregate amount not to exceed \$100,000 in any fiscal year if the Company's consolidated total leverage ratio is greater than 3.00 to 1.00 at the time the dividend or repurchase is made; notwithstanding (1) and (2), so long as immediately after giving effect to the payment of any such dividends, cash availability is at least \$100,000, the Company may declare and pay cash dividends on shares of its common stock in an aggregate amount not to exceed in any fiscal year the product of the aggregate amount of dividends declared in the fourth quarter of the immediately preceding fiscal year multiplied by four.

5. Derivative Instruments and Hedging Activities

The Company has interest rate risk relative to its outstanding borrowings (see Note 4 for information on the Company's outstanding borrowings). The Company's policy has been to manage interest cost using a mix of fixed and variable rate debt. To manage this risk in a cost efficient manner, the Company uses derivative instruments, specifically interest rate swaps.

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For each of the Company's interest rate swaps, the Company has agreed to exchange with a counterparty the difference between fixed and variable interest amounts calculated by reference to an agreed-upon notional principal amount. The interest rates on the portion of the Company's outstanding debt covered by its interest rate swaps are fixed at the rates in the table below plus the Company's credit spread. The Company's credit spread at May 1, 2015 was 1.25%. All of the Company's interest rate swaps are accounted for as cash flow hedges.

A summary of the Company's interest rate swaps at May 1, 2015 is as follows:

| Trade Date         | Effective Date | Term<br>(in<br>Years) | Notional<br>Amount | Fixed<br>Rate |
|--------------------|----------------|-----------------------|--------------------|---------------|
| August 10, 2010    | May 3, 2013    | 2                     | \$200,000          | 2.73 %        |
| July 25, 2011      | May 3, 2013    | 2                     | 50,000             | 2.00 %        |
| July 25, 2011      | May 3, 2013    | 3                     | 50,000             | 2.45 %        |
| September 19, 2011 | May 3, 2013    | 2                     | 25,000             | 1.05 %        |
| September 19, 2011 | May 3, 2013    | 2                     | 25,000             | 1.05 %        |
| December 7, 2011   | May 3, 2013    | 3                     | 50,000             | 1.40 %        |
| March 18, 2013     | May 3, 2015    | 3                     | 50,000             | 1.51 %        |
| April 8, 2013      | May 3, 2015    | 2                     | 50,000             | 1.05 %        |
| April 15, 2013     | May 3, 2015    | 2                     | 50,000             | 1.03 %        |
| April 22, 2013     | May 3, 2015    | 3                     | 25,000             | 1.30 %        |
| April 25, 2013     | May 3, 2015    | 3                     | 25,000             | 1.29 %        |
| June 18, 2014      | May 3, 2015    | 4                     | 40,000             | 2.51 %        |
| June 24, 2014      | May 3, 2015    | 4                     | 30,000             | 2.51 %        |
| July 1, 2014       | May 5, 2015    | 4                     | 30,000             | 2.43 %        |
| January 30, 2015   | May 3, 2019    | 2                     | 80,000             | 2.15 %        |
| January 30, 2015   | May 3, 2019    | 2                     | 60,000             | 2.16 %        |
| January 30, 2015   | May 4, 2021    | 3                     | 120,000            | 2.41 %        |
| January 30, 2015   | May 3, 2019    | 2                     | 60,000             | 2.15 %        |
| January 30, 2015   | May 4, 2021    | 3                     | 80,000             | 2.40 %        |

The notional amount for the interest rate swap entered into on June 18, 2014 increases by \$40,000 each May over the four-year term of the interest rate swap beginning in May 2016 until the notional amount reaches \$160,000 in May 2018. The notional amounts for the interest rate swaps entered into on June 24, 2014 and July 1, 2014 increase by \$30,000 each May over the four-year terms of the interest rate swaps beginning in May 2016 until the notional amounts each reach \$120,000 in May 2018.

The Company does not hold or use derivative instruments for trading purposes. The Company also does not have any derivatives not designated as hedging instruments and has not designated any non-derivatives as hedging instruments.

Companies may elect to offset related assets and liabilities and report the net amount on their financial statements if the right of setoff exists. Under a master netting agreement, the Company has the legal right to offset the amounts owed to the Company against amounts owed by the Company under a derivative instrument that exists between the Company and a counterparty. When the Company is engaged in more than one outstanding derivative transaction with the same counterparty and also has a legally enforceable master netting agreement with that counterparty, its credit risk exposure is based on the net exposure under the master netting agreement. If, on a net basis, the Company owes the counterparty, the Company regards its credit exposure to the counterparty as being zero.

The estimated fair values of the Company's derivative instruments as of May 1, 2015 and August 1, 2014 were as follows:



|                     |  | August      |         |
|---------------------|--|-------------|---------|
|                     |  | May 1, 2015 | 1, 2014 |
| (See Note 2)        | Balance Sheet Location                 |             |         |
| Interest rate swaps | Other assets                           | \$3,146     | \$240   |
| Interest rate swaps | Current interest rate swap liability   | \$68        | \$4,704 |
| Interest rate swaps | Long-term interest rate swap liability | 9,633       | 3,239   |
|                     | Total                                  | \$9,701     | \$7,943 |

The following table summarizes the offsetting of the Company's derivative assets in the Condensed Consolidated Balance Sheets at May 1, 2015 and August 1, 2014:

| (See Note 2) | Gross Asset Amounts |                | Liability Amount Offset |                | Net Asset Amount Presented in the Balance Sheets |                |
|--------------|---------------------|----------------|-------------------------|----------------|--|----------------|
|              | May 1, 2015         | August 1, 2014 | May 1, 2015             | August 1, 2014 | May 1, 2015                                      | August 1, 2014 |
|              | Interest rate swaps | \$3,245        | \$240                   | \$(99)         | \$--   | \$3,146        |

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The following table summarizes the offsetting of the Company's derivative liabilities in the Condensed Consolidated Balance Sheets at May 1, 2015 and August 1, 2014:

|                     | Gross Liability<br>Amounts |              | Asset<br>Amount<br>Offset |              | Net Liability<br>Amount<br>Presented in the<br>Balance Sheets |              |
|---------------------|----------------------------|--------------|---------------------------|--------------|---|--------------|
|                     | August<br>May 1,           | August<br>1, | May<br>1,                 | August<br>1, | August<br>May 1,  | August<br>1, |
| (See Note 2)        | 2015                       | 2014         | 2015                      | 2014         | 2015  | 2014         |
| Interest rate swaps | \$9,701                    | \$8,441      | \$--                      | \$(498)      | \$9,701   | \$7,943      |

The estimated fair value of the Company's interest rate swap assets and liabilities incorporates the Company's non-performance risk (see Note 2). The adjustment related to the Company's non-performance risk at May 1, 2015 and August 1, 2014 resulted in reductions of \$209 and \$62, respectively, in the fair value of the interest rate swap assets and liabilities. The offset to the interest rate swap assets and liabilities is recorded in accumulated other comprehensive loss ("AOCL"), net of the deferred tax asset, and will be reclassified into earnings over the term of the underlying debt. As of May 1, 2015, the estimated pre-tax portion of AOCL that is expected to be reclassified into earnings over the next twelve months is \$4,089. Cash flows related to the interest rate swap are included in interest expense and in operating activities.

The following table summarizes the pre-tax effects of the Company's derivative instruments on AOCL for the nine months ended May 1, 2015 and the year ended August 1, 2014:

|                     | Amount of<br>Income<br>Recognized in<br>AOCL on<br>Derivatives<br>(Effective<br>Portion) |                                       |
|---------------------|--|---------------------------------------|
|                     | Nine<br>Months<br>Ended<br>May 1,<br>2015  | Year<br>Ended<br>August<br>1,<br>2014 |
| Cash flow hedges:   |  |                                       |
| Interest rate swaps | \$1,148  | \$3,058                               |

The following table summarizes the pre-tax effects of the Company's derivative instruments on income for the quarters and nine-month periods ended May 1, 2015 and May 2, 2014:

| Location of Loss<br>Reclassified from<br>AOCL into Income<br>(Effective Portion) | Amount of Loss Reclassified<br>from AOCL into Income<br>(Effective Portion) |                |                      |                |
|--|---|----------------|----------------------|----------------|
|  | Quarter Ended   |                | Nine Months<br>Ended |                |
|  | May 1,<br>2015  | May 2,<br>2014 | May 1,<br>2015       | May 2,<br>2014 |
|  |   |                |                      |                |

Cash flow hedges:

|                                      |         |         |         |         |
|--------------------------------------|---------|---------|---------|---------|
| Interest rate swaps Interest expense | \$2,040 | \$2,007 | \$6,055 | \$6,033 |
|--------------------------------------|---------|---------|---------|---------|

Any portion of the fair value of the swaps determined to be ineffective will be recognized currently in earnings. No ineffectiveness has been recorded in the nine-month periods ended May 1, 2015 and May 2, 2014.

6. Shareholders' Equity

During the nine months ended May 1, 2015, the Company issued 127,857 shares of its common stock resulting from the vesting of share-based compensation awards and stock option exercises. Related tax withholding payments on certain share-based compensation awards exceeded proceeds received from the exercise of stock options, which resulted in a net reduction to shareholders' equity of \$3,432.

During the nine months ended May 1, 2015, total share-based compensation expense was \$10,795. The excess tax benefit realized upon exercise of share-based compensation awards was \$3,224.

During the nine months ended May 1, 2015, the Company paid dividends of \$3.00 per share of its common stock and declared a regular dividend of \$1.00 per share of its common stock that was paid on May 5, 2015 to shareholders of record on April 17, 2015. On June 2, 2015, the Company declared a regular dividend of \$1.10 per share and a special dividend of \$3.00 per share, both payable on August 5, 2015 to shareholders of record on July 17, 2015.

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The following table summarizes the changes in AOCL, net of tax, related to the Company's interest rate swaps for the nine-month period ended May 1, 2015 (see Notes 2 and 5):

|   | Changes<br>in<br>AOCL |
|---|-----------------------|
| AOCL balance at August 1, 2014                      | \$(4,733 )            |
| Other comprehensive income before reclassifications | 4,426                 |
| Amounts reclassified from AOCL                      | (3,720 )              |
| Other comprehensive income, net of tax              | 706                   |
| AOCL balance at May 1, 2015                         | \$(4,027 )            |

The following table summarizes the amounts reclassified out of AOCL related to the Company's interest rate swaps for the quarter and nine-month period ended May 1, 2015:

|                           | Amount<br>Reclassified from<br>AOCL |   | Affected Line Item in the<br>Condensed Consolidated<br>Statements of Income |
|---------------------------|-------------------------------------|---|---|
|                           | Quarter<br>Ended<br>May 1,<br>2015  | Nine<br>Months<br>Ended<br>May 1,<br>2015 |   |
| Loss on cash flow hedges: |                                     |   |   |
| Interest rate swaps       | \$(2,040)                           | \$(6,055)                                 | Interest expense  |
| Tax benefit               | 787                                 | 2,335                                     | Provision for income taxes  |
|                           | \$(1,253)                           | \$(3,720)                                 | Net of tax  |

7. Seasonality

Historically, the net income of the Company has been lower in the first and third quarters and higher in the second and fourth quarters. Management attributes these variations to the Christmas holiday shopping season and the summer vacation and travel season. The Company's retail sales, which are made substantially to the Company's restaurant customers, historically have been highest in the Company's second quarter, which includes the Christmas holiday shopping season. Historically, interstate tourist traffic and the propensity to dine out have been higher during the summer months, thereby contributing to higher profits in the Company's fourth quarter. The Company generally opens additional new locations throughout the year. Therefore, the results of operations for any interim period cannot be considered indicative of the operating results for an entire year.

8. Segment Information

Cracker Barrel stores represent a single, integrated operation with two related and substantially integrated product lines. The operating expenses of the restaurant and retail product lines of a Cracker Barrel store are shared and are indistinguishable in many respects. Accordingly, the Company currently manages its business on the basis of one reportable operating segment. All of the Company's operations are located within the United States. Total revenue was comprised of the following for the specified periods:

| Quarter Ended  |                | Nine Months Ended |                |
|----------------|----------------|-------------------|----------------|
| May 1,<br>2015 | May 2,<br>2014 | May 1,<br>2015    | May 2,<br>2014 |
|                |                |                   |                |

Revenue:

|               |           |           |             |             |
|---------------|-----------|-----------|-------------|-------------|
| Restaurant    | \$557,098 | \$523,557 | \$1,681,363 | \$1,573,895 |
| Retail        | 126,607   | 119,741   | 441,736     | 417,035     |
| Total revenue | \$683,705 | \$643,298 | \$2,123,099 | \$1,990,930 |

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Index9. Share-Based Compensation

Share-based compensation is recorded in general and administrative expenses in the accompanying Condensed Consolidated Statements of Income. Total share-based compensation was comprised of the following for the specified periods:

|   | Quarter Ended |             | Nine Months Ended |             |
|---|---------------|-------------|-------------------|-------------|
|   | May 1, 2015   | May 2, 2014 | May 1, 2015       | May 2, 2014 |
| Nonvested stock awards                              | \$3,670       | \$1,269     | \$8,652           | \$4,611     |
| Performance-based market stock units ("MSU Grants") | 795           | 617         | 2,143             | 1,521       |
|   | \$4,465       | \$1,886     | \$10,795          | \$6,132     |

10. Shareholder Rights Plans

On April 9, 2015, the Company's Board of Directors declared a dividend of one preferred share purchase right (a "Right") for each outstanding share of common stock, par value \$0.01 per share, and adopted a shareholder rights plan, as set forth in the Rights Agreement dated as of April 9, 2015 (the "Rights Agreement"), by and between the Company and American Stock Transfer & Trust Company, LLC, as rights agent. The dividend was payable on April 20, 2015 to the shareholders of record on April 20, 2015. The Rights Agreement replaced the Company's previous shareholder rights plan adopted in 2012 (the "2012 Plan"), and it became effective immediately following the expiration of the 2012 Plan at the close of business on April 9, 2015. The 2012 Plan and the preferred share purchase rights issued thereunder expired by their own terms and shareholders of the Company were not entitled to any payment as a result of the expiration of the 2012 Plan.

The Rights

The Rights initially trade with, and are inseparable from, the Company's common stock. The Rights are evidenced only by the balances indicated in the book-entry account system of the transfer agent for the Company's common stock or, in the case of certified shares, the certificates that represent shares of the Company's common stock. New Rights will accompany any new shares of common stock the Company issues after April 20, 2015 until the earlier of the Distribution Date, redemption of the Rights by the Board of Directors or the final expiration date of the Rights Agreement, each as described below.

Exercise Price

Each Right will allow its holder to purchase from the Company one one-hundredth of a share of Series A Junior Participating Preferred Stock ("Preferred Share") for \$600.00 (the "Exercise Price"), once the Rights become exercisable. This portion of a Preferred Share will give the shareholder approximately the same dividend and liquidation rights as would one share of common stock. Prior to exercise, the Right does not give its holder any dividend, voting, or liquidation rights.

Exercisability

The Rights will not be exercisable until 10 days after the public announcement that a person or group has become an "Acquiring Person" by obtaining beneficial ownership of 20% or more of the outstanding common stock.

Shares held by affiliates and associates of an Acquiring Person, and Notional Common Shares (as defined in the Rights Agreement) held by counterparties to a Derivatives Contract (as defined in the Rights Agreement) with an

Acquiring Person, will be deemed to be beneficially owned by the Acquiring Person. Certain synthetic interests in securities created by derivative positions – whether or not such interests are considered to be ownership of the underlying common stock or are reportable for purposes of Regulation 13D of the Securities Exchange Act – are treated as beneficial ownership of the number of shares of the Company’s common stock equivalent to the economic exposure created by the derivative.

The date when the Rights become exercisable is the “Distribution Date.” Until the Distribution Date, the common stock certificates will evidence the Rights, and any transfer of shares of common stock will constitute a transfer of Rights. After that date, the Rights will separate from the common stock and will be evidenced by book-entry credits or by Rights certificates that the Company will mail to all eligible holders of common stock. Any Rights held by an Acquiring Person will be void and may not be exercised.

At May 1, 2015, none of the Rights were exercisable.

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### Consequences of a Person or Group Becoming an Acquiring Person

If a person or group becomes an Acquiring Person, after the Distribution Date, each Right will generally entitle the holder, except the Acquiring Person or any associate or affiliate thereof, to acquire, for the exercise price of \$600.00 per Right (subject to adjustment as provided in the Rights Agreement), shares of the Company's common stock (or, in certain circumstances, Preferred Shares) having a market value equal to twice the Right's then-current exercise price. In addition, if, the Company is later acquired in a merger or similar transaction after the Distribution Date, each Right will generally entitle the holder, except the Acquiring Person or any associate or affiliate thereof, to acquire, for the exercise price of \$600.00 per Right (subject to adjustment as provided in the Rights Agreement), shares of the acquiring corporation having a market value equal to twice the Right's then-current exercise price.

### Preferred Share Provisions

Each one one-hundredth of a Preferred Share, if issued:

- will not be redeemable;
- will entitle holders to quarterly dividend payments of \$0.01 per share, or an amount equal to the dividend paid on one share of common stock, whichever is greater;
- will entitle holders upon liquidation either to receive \$1.00 per share or an amount equal to the payment made on one share of common stock, whichever is greater;
- will have the same voting power as one share of common stock; and
  - if shares of the Company's common stock are exchanged via merger, consolidation, or a similar transaction, will entitle holders to a per share payment equal to the payment made on one share of common stock.

The value of one one-hundredth of a Preferred Share will generally approximate the value of one share of common stock.

### Redemption

The Board of Directors may redeem the Rights for \$0.01 per Right at any time before any person or group becomes an Acquiring Person. If the Board of Directors redeems any Rights, it must redeem all of the Rights. Once the Rights are redeemed, the only right of the holders of Rights will be to receive the redemption price of \$0.01 per Right. The redemption price will be adjusted if the Company has a stock split or stock dividends of its common stock.

### Qualifying Offer Provision

The Rights would also not interfere with all-cash, fully financed tender offers for all shares of common stock that remain open for a minimum of 60 business days, are subject to a minimum condition of a majority of the outstanding shares and provide for a 20-business day "subsequent offering period" after consummation (such offers are referred to as "qualifying offers"). In the event the Company receives a qualifying offer and the Board of Directors has not redeemed the Rights prior to the consummation of such offer, the consummation of the qualifying offer shall not cause the offeror or its affiliates to become an Acquiring Person, and the Rights will immediately expire upon consummation of the qualifying offer.

### Exchange

After a person or group becomes an Acquiring Person, but before an Acquiring Person owns 50% or more of the Company's outstanding common stock, the Board of Directors may extinguish the Rights by exchanging one share of common stock or an equivalent security for each Right, other than Rights held by the Acquiring Person.





IndexAnti-Dilution Provisions

The Board of Directors may adjust the purchase price of the Preferred Shares, the number of Preferred Shares issuable and the number of outstanding Rights to prevent dilution that may occur from a stock dividend, a stock split, a reclassification of the Preferred Shares or common stock. No adjustments to the Exercise Price of less than 1% will be made.

Amendments

The terms of the Rights Agreement may be amended by the Board of Directors without the consent of the holders of the Rights. After a person or group becomes an Acquiring Person, the Board of Directors may not amend the agreement in a way that adversely affects holders of the Rights.

Expiration

If the Rights Agreement is approved by the Company's shareholders at the 2015 annual shareholders' meeting, the Rights will expire on April 9, 2018. If shareholders do not approve the Rights Agreement, the Rights will expire immediately following certification of the vote at the 2015 annual shareholders' meeting.

11. Net Income Per Share and Weighted Average Shares

Basic consolidated net income per share is computed by dividing consolidated net income available to common shareholders by the weighted average number of shares of common stock outstanding for the reporting period. Diluted consolidated net income per share reflects the potential dilution that could occur if securities, options or other contracts to issue shares of common stock were exercised or converted into shares of common stock and is based upon the weighted average number of shares of common stock and common equivalent shares outstanding during the reporting period. Common equivalent shares related to stock options, nonvested stock awards and MSU Grants issued by the Company are calculated using the treasury stock method. The outstanding stock options, nonvested stock awards and MSU Grants issued by the Company represent the only dilutive effects on diluted consolidated net income per share.

The following table reconciles the components of diluted earnings per share computations:

|  | Quarter Ended  |                | Nine Months Ended |                |
|--|----------------|----------------|-------------------|----------------|
|  | May 1,<br>2015 | May 2,<br>2014 | May 1,<br>2015    | May 2,<br>2014 |
| Net income per share numerator                       | \$35,317       | \$28,728       | \$116,504         | \$92,943       |
| Net income per share denominator:                    |                |                |                   |                |
| Weighted average shares                              | 23,937,844     | 23,820,309     | 23,904,945        | 23,816,841     |
| Add potential dilution:                              |                |                |                   |                |
| Stock options, nonvested stock awards and MSU Grants | 128,217        | 158,165        | 128,351           | 141,217        |
| Diluted weighted average shares                      | 24,066,061     | 23,978,474     | 24,033,296        | 23,958,058     |

12. Commitments and Contingencies

During 2014 and through September 25, 2014, the Company was served with several claims filed as a putative collective action alleging violations of the Fair Labor Standards Act ("FLSA"). The Company has recorded a total provision of approximately \$3,500 at May 1, 2015 to reflect potential liability related to these lawsuits. Although we continue to believe that the Company's associate managers are and have been properly classified as exempt employees

under FLSA and have therefore aggressively challenged the plaintiffs' claims in these lawsuits, in light of the potential cost and uncertainty involved in these lawsuits, in March 2015, we entered into a memorandum of understanding (the "MOU") with respect to a settlement with plaintiffs' counsel to resolve the series of lawsuits. In May 2015, the parties executed the settlement agreement based on the MOU, and the final resolution of these matters through settlement is subject to final court approval. No other provision for any potential liability has been made in the condensed consolidated financial statements of the Company related to these proceedings though an adverse outcome could be material to the Company's results of operations or financial position. See "Item 1. Legal Proceedings" of Part II of this Quarterly Report on Form 10-Q for further information related to these claims.

In addition to the matters described above, the Company and its subsidiaries are party to various legal and regulatory proceedings and claims incidental to their business in the ordinary course. 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.

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Related to its workers' compensation insurance coverage, the Company is contingently liable pursuant to standby letters of credit as credit guarantees to certain insurers. As of May 1, 2015, the Company had \$11,530 of standby letters of credit related to securing reserved claims under workers' compensation insurance. All standby letters of credit are renewable annually and reduce the Company's borrowing availability under its 2015 Revolving Credit Facility (see Note 4).

At May 1, 2015, the Company is secondarily liable for lease payments associated with one property. The Company is not aware of any non-performance under this lease arrangement that would result in the Company having to perform in accordance with the terms of this guarantee; and therefore, no provision has been recorded in the Condensed Consolidated Balance Sheets for amounts to be paid in case of non-performance by the primary obligor under such lease arrangement.

The Company enters into certain indemnification agreements in favor of third parties in the ordinary course of business. At May 1, 2015 and May 2, 2014, the Company recorded a liability in the Condensed Consolidated Balance Sheets related to legal costs. The Company believes that the amount recorded is immaterial to the Company's consolidated results of operations and financial position and that the probability of incurring an actual liability under other indemnification agreements is sufficiently remote so that no additional liability has been recorded in the Condensed Consolidated Balance Sheets.

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

Cracker Barrel Old Country Store, Inc. and its subsidiaries (collectively, the “Company,” “our” or “we”) are principally engaged in the operation and development in the United States of the Cracker Barrel Old Country Store (“Cracker Barrel”) concept. At May 1, 2015, we operated 634 Cracker Barrel stores in 42 states. All dollar amounts reported or discussed in this Management’s Discussion and Analysis of Financial Condition and Results of Operations (“MD&A”) are shown in thousands, except per share amounts and certain statistical information (e.g., number of stores). References to years in MD&A are to our fiscal year unless otherwise noted.

MD&A provides information which management believes is relevant to an assessment and understanding of our consolidated results of operations and financial condition. MD&A should be read in conjunction with the (i) condensed consolidated financial statements and notes thereto included in this Quarterly Report on Form 10-Q and (ii) financial statements and the notes thereto included in the Company’s Annual Report on Form 10-K for the fiscal year ended August 1, 2014 (the “2014 Form 10-K”). Except for specific historical information, many of the matters discussed in this report may express or imply projections of items such as revenues or expenditures, estimated capital expenditures, compliance with debt covenants, plans and objectives for future operations, inventory shrinkage, growth or initiatives, expected future economic performance or the expected outcome or impact of pending or threatened litigation. These and similar statements regarding events or results which we expect will or may occur in the future are forward-looking statements that, by their nature, involve risks, uncertainties and other factors which may cause our actual results and performance to differ materially from those expressed or implied by such statements. All forward-looking information is provided pursuant to the safe harbor established under the Private Securities Litigation Reform Act of 1995 and should be evaluated in the context of these risks, uncertainties and other factors.

Forward-looking statements generally can be identified by the use of forward-looking terminology such as “trends,” “assumptions,” “target,” “guidance,” “outlook,” “opportunity,” “future,” “plans,” “goals,” “objectives,” “expectations,” “near-term,” “long-term,” “projection,” “may,” “will,” “would,” “could,” “expect,” “intend,” “estimate,” “anticipate,” “believe,” “potential,” “forecasts” or “continue” (or the negative or other derivatives of each of these terms) or similar terminology. We believe the assumptions underlying any forward-looking statements are reasonable; however, any of the assumptions could be inaccurate, and therefore, actual results may differ materially from those projected in or implied by the forward-looking statements. In addition to the risks of ordinary business operations, and those discussed or described in this report or in information incorporated by reference into this report, factors and risks that may result in actual results differing from this forward-looking information include, but are not limited to, those contained in Part I, Item 1A of the 2014 Form 10-K, which is incorporated herein by this reference, as well as the factors described under “Critical Accounting Estimates” on pages 25-28 of this report or, from time to time, in our filings with the Securities and Exchange Commission (“SEC”), press releases and other communications.

Readers are cautioned not to place undue reliance on forward-looking statements made in this report because the statements speak only as of the report’s date. Except as may be required by law, we have no obligation or intention to update or revise any of these forward-looking statements to reflect events or circumstances occurring after the date of this report or to reflect the occurrence of unanticipated events. Readers are advised, however, to consult any future public disclosures that we may make on related subjects in reports that we file with or furnish to the SEC or in our other public disclosures.

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## Overview

Management believes that the Cracker Barrel brand remains one of the strongest and most differentiated brands in the restaurant industry, and we plan to continue to leverage that strength in 2015 to grow guest sales and profits. Our long-term strategy includes the following:

Enhancing the core business by increasing our brand's relevance to customers in order to drive guest traffic and sales in both restaurant and retail, implementing geographic pricing tiers to optimize average check and re-engineering store processes to increase operating margin;

Expanding the footprint through continued use of our proven site selection tools, introducing a new and more efficient building and equipment prototype and the selective entry into new markets; and

Extending the brand by building on the initial success of our licensing business, leveraging our brand strengths into a new fast casual concept and growing our retail business into an omni-channel business.

Our four priorities for 2015 are to:

- Extend the reach of the brand to drive traffic and sales in both our restaurant and retail businesses;
- Optimize average guest check through the implementation of geographic pricing tiers;
- Apply technology and process enhancements to drive store operating margins; and
- Further grow our store base with the opening of six new stores.

We have maintained our focus on the execution of these priorities. In the third quarter of 2015, we outperformed traffic and restaurant sales of our peers in the Knapp-Track™ Casual Dining Index for the fourteenth consecutive quarter and our comparable store retail sales increased over 4%. During the quarter, we introduced several new promotional menu items and have continued to focus on strengthening our relationships with our guests through alternative channels, such as digital and social media and our music program. During the quarter, we began implementation of our dining room management system in our stores and expect to substantially complete this initiative in the fourth quarter of 2015. This initiative's purpose is to optimize our wait list and seating process while reducing our overall cost. We also implemented our second market-level pricing increase during the quarter and continued to improve operating margins.

## Results of Operations

The following table highlights our operating results by percentage relationships to total revenue for the quarter and nine-month period ended May 1, 2015 as compared to the same periods in the prior year:

|   | Quarter Ended |             | Nine Months Ended |             |
|---|---------------|-------------|-------------------|-------------|
|   | May 1, 2015   | May 2, 2014 | May 1, 2015       | May 2, 2014 |
| Total revenue   | 100.0%        | 100.0%      | 100.0%            | 100.0%      |
| Cost of goods sold (exclusive of depreciation and rent) | 31.6          | 31.3        | 33.0              | 32.7        |
| Labor and other related expenses                        | 36.1          | 37.8        | 34.9              | 36.1        |
| Other store operating expenses                          | 18.5          | 18.8        | 18.4              | 18.8        |

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|                                     |      |       |       |       |
|-------------------------------------|------|-------|-------|-------|
| Store operating income              | 13.8 | 12.1  | 13.7  | 12.4  |
| General and administrative expenses | 5.7  | 5.1   | 5.1   | 5.0   |
| Operating income                    | 8.1  | 7.0   | 8.6   | 7.4   |
| Interest expense                    | 0.6  | 0.6   | 0.6   | 0.6   |
| Income before income taxes          | 7.5  | 6.4   | 8.0   | 6.8   |
| Provision for income taxes          | 2.3  | 1.9   | 2.5   | 2.1   |
| Net income                          | 5.2  | % 4.5 | % 5.5 | % 4.7 |

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The following table sets forth the number of stores in operation at the beginning and end of the quarters and nine-month periods ended May 1, 2015 and May 2, 2014, respectively:

|                             | Quarter Ended |             | Nine Months Ended |             |
|-----------------------------|---------------|-------------|-------------------|-------------|
|                             | May 1, 2015   | May 2, 2014 | May 1, 2015       | May 2, 2014 |
| Open at beginning of period | 634           | 625         | 631               | 624         |
| Opened during period        | --            | 2           | 3                 | 3           |
| Open at the end of period   | 634           | 627         | 634               | 627         |

## Total Revenue

Total revenue for the third quarter and first nine months of 2015 increased 6.3% and 6.6%, respectively, compared to the same periods in the prior year.

The following table highlights the key components of revenue for the quarter and nine-month period ended May 1, 2015 as compared to the quarter and nine-month period ended May 2, 2014:

|   | Quarter Ended |             | Nine Months Ended |             |
|---|---------------|-------------|-------------------|-------------|
|   | May 1, 2015   | May 2, 2014 | May 1, 2015       | May 2, 2014 |
| Revenue in dollars:                         |               |             |                   |             |
| Restaurant                                  | \$557,098     | \$523,557   | \$1,681,363       | \$1,573,895 |
| Retail                                      | 126,607       | 119,741     | 441,736           | 417,035     |
| Total revenue                               | \$683,705     | \$643,298   | \$2,123,099       | \$1,990,930 |
| Total revenue by percentage relationships:  |               |             |                   |             |
| Restaurant                                  | 81.5 %        | 81.4 %      | 79.2 %            | 79.1 %      |
| Retail                                      | 18.5 %        | 18.6 %      | 20.8 %            | 20.9 %      |
| Average unit volumes <sup>(1)</sup> :       |               |             |                   |             |
| Restaurant                                  | \$878.7       | \$836.5     | \$2,654.1         | \$2,517.9   |
| Retail                                      | 199.7         | 191.3       | 697.3             | 667.2       |
| Total revenue                               | \$1,078.4     | \$1,027.8   | \$3,351.4         | \$3,185.1   |
| Comparable store sales increase (decrease): |               |             |                   |             |
| Restaurant                                  | 5.2 %         | (0.6 %)     | 5.5 %             | 0.5 %       |
| Retail                                      | 4.5 %         | 0.9 %       | 4.5 %             | (0.2 %)     |
| Restaurant and retail                       | 5.1 %         | (0.3 %)     | 5.3 %             | 0.3 %       |

(1) Average unit volumes include sales of all stores.

For the third quarter of 2015, our comparable store restaurant sales increase consisted of a 3.4% average check increase for the quarter (including a 2.5% average menu price increase) and a 1.8% guest traffic increase. We believe the positive impact of lower gasoline prices on consumer spending and travel contributed to our guest traffic increase. For the third quarter of 2015, our comparable store retail sales increase resulted primarily from strong performance in apparel and accessories and bed and bath merchandise categories and the increase in guest traffic.

For the first nine months of 2015, our comparable store restaurant sales increase consisted of a 3.0% average check increase for the nine months (including a 2.4% average menu price increase) and a 2.5% guest traffic increase. We



believe the increase in guest traffic resulted from seasonal menu promotions, the milder winter weather as compared to the prior year, the positive impact of lower gasoline prices on consumer spending and travel and the success of our national advertising. For the first nine months of 2015, our comparable store retail sales increase resulted primarily from strong performance in apparel and accessories, décor, and bed and bath merchandise categories and the increase in guest traffic.

Restaurant and retail sales from newly opened stores accounted for the balance of the total revenue increases in the third quarter and first nine months of 2015 as compared to the same periods in the prior year.

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## Cost of Goods Sold (Exclusive of Depreciation and Rent)

The following table highlights the components of cost of goods sold (exclusive of depreciation and rent) in dollar amounts and as percentages of revenues for the third quarter and first nine months of 2015 as compared to the same periods in the prior year:

|  | Quarter Ended  |                | Nine Months Ended |                |
|--|----------------|----------------|-------------------|----------------|
|  | May 1,<br>2015 | May 2,<br>2014 | May 1,<br>2015    | May 2,<br>2014 |
| Cost of Goods Sold in dollars:               |                |                |                   |                |
| Restaurant                                   | \$153,351      | \$141,757      | \$470,511         | \$432,735      |
| Retail                                       | 62,791         | 59,750         | 230,081           | 217,716        |
| Total Cost of Goods Sold                     | \$216,142      | \$201,507      | \$700,592         | \$650,451      |
| Cost of Goods Sold by percentage of revenue: |                |                |                   |                |
| Restaurant                                   | 27.5           | % 27.1         | % 28.0            | % 27.5         |
| Retail                                       | 49.6           | % 49.9         | % 52.1            | % 52.2         |

The increase in restaurant cost of goods sold as a percentage of restaurant revenue in the third quarter of 2015 as compared to the same period in the prior year was due to commodity inflation partially offset by our menu price increase referenced above. The increase in restaurant cost of goods sold as a percentage of restaurant revenue in the first nine months of 2015 as compared to the same period in the prior year was primarily due to commodity inflation and a shift to higher cost menu items partially offset by our menu price increase referenced above and lower food waste. Higher cost menu items accounted for an increase of 0.2% in restaurant cost of goods sold as a percentage of restaurant revenue for the first nine months of 2015 as compared to the same period in the prior year. Lower food waste accounted for a decrease of 0.1% in restaurant cost of goods sold as a percentage of restaurant revenue for the first nine months of 2015 as compared to the same period in the prior year. Commodity inflation was 4.0% and 3.9%, respectively, in the third quarter and first nine months of 2015.

We presently expect the rate of commodity inflation to be approximately 3.0% for 2015.

The decrease in retail cost of goods sold as a percentage of retail revenue in the third quarter of 2015 as compared to the prior year quarter resulted primarily from lower markdowns, lower damages and vendor allowances and lower shrinkage partially offset by lower initial markup on merchandise.

|                                     | Third<br>Quarter<br>(Decrease)<br>Increase<br>as a<br>Percentage<br>of Retail<br>Revenue |
|-------------------------------------|--|
| Markdowns                           | (0.3 %)  |
| Damages and vendor allowances       | (0.2 %)  |
| Retail inventory shrinkage          | (0.1 %)  |
| Lower initial markup on merchandise | 0.3 %  |

Retail cost of goods sold as a percentage of retail revenue remained relatively constant in the first nine months of 2015 as compared to the same period in the prior year.



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## Labor and Related Expenses

Labor and related expenses include all direct and indirect labor and related costs incurred in store operations. Labor and related expenses as a percentage of total revenue decreased to 36.1% in the third quarter of 2015 as compared to 37.8% in the third quarter of 2014. This percentage change resulted primarily from the following:

|                                      | Third<br>Quarter<br>(Decrease)<br>Increase<br>as a<br>Percentage<br>of Total<br>Revenue |    |
|--------------------------------------|---|----|
| Employee health care expenses        | (0.8  | %) |
| Store hourly labor                   | (0.6  | %) |
| Store management compensation        | (0.4  | %) |
| Payroll tax expense                  | (0.2  | %) |
| Store incentive compensation expense | 0.5   | %) |

Labor and related expenses as a percentage of total revenue decreased to 34.9% in the first nine months of 2015 as compared to 36.1% in the same period in the prior year. This percentage change resulted from the following:

|                                      | First Nine<br>Months<br>(Decrease)<br>Increase<br>as a<br>Percentage<br>of Total<br>Revenue |    |
|--------------------------------------|---|----|
| Store hourly labor                   | (0.7  | %) |
| Store management compensation        | (0.4  | %) |
| Employee health care expenses        | (0.3  | %) |
| Payroll tax expense                  | (0.2  | %) |
| Store incentive compensation expense | 0.4   | %) |

The decreases in our employee health care expenses as a percentage of total revenue for the third quarter and the first nine months of 2015 as compared to the same periods in the prior year resulted primarily from lower claims in 2015 and the recognition of premium credits related to claims for the plan year ending December 31, 2014.

The decreases in store hourly labor costs as a percentage of total revenue for the third quarter and first nine months of 2015 as compared to the same periods in the prior year resulted from menu price increases being higher than wage inflation and improved productivity driven by the successful implementation of labor savings initiatives in the first quarter of 2015.

The decreases in store management compensation expense as a percentage of total revenue for the third quarter and first nine months of 2015 as compared to the same periods in the prior year resulted primarily from the increases in revenue in the third quarter and first nine months of 2015 as compared to the prior year periods.

The decreases in payroll tax expense as a percentage of total revenue for the third quarter and first nine months of 2015 as compared to the same periods in the prior year resulted primarily from a reduction in state unemployment tax rates.

The increases in store incentive compensation expense as a percentage of total revenue for the third quarter and first nine months of 2015 as compared to the same periods in the prior year reflected better performance against financial objectives in 2015 as compared to the prior year.

#### Other Store Operating Expenses

Other store operating expenses include all store-level operating costs, the major components of which are utilities, operating supplies, repairs and maintenance, depreciation and amortization, advertising, rent, credit card fees, real and personal property taxes, general insurance and costs associated with our store manager conference.

Other store operating expenses as a percentage of total revenue decreased to 18.5% in the third quarter of 2015 as compared to 18.8% in the third quarter of 2014. This percentage decrease resulted from lower utilities expense.

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Other store operating expenses as a percentage of total revenue decreased to 18.4% in the first nine months of 2015 as compared to 18.8% in the same period in the prior year. This percentage change resulted primarily from the following:

|                                  | First Nine<br>Months<br>(Decrease)<br>as a<br>Percentage<br>of Total<br>Revenue |
|----------------------------------|---|
| Maintenance expense              | (0.2 %)   |
| Utilities expense                | (0.2 %)   |
| Store manager conference expense | (0.1 %)   |

The decreases in utilities expense as a percentage of total revenue for the third quarter and first nine months of 2015 as compared to the same periods in the prior year resulted primarily from milder winter weather and lower natural gas prices.

The decrease in maintenance expense as a percentage of total revenue for the first nine months of 2015 as compared to the same period in the prior year resulted primarily from the increase in revenue.

In the first quarter of 2014, we held a manager conference which was attended by our store operations management team. We did not hold a manager's conference in the first nine months of 2015 and we expect to hold our next conference in the first quarter of 2016.

General and Administrative Expenses

General and administrative expenses as a percentage of total revenue increased to 5.7% in the third quarter of 2015 as compared to 5.1% in the third quarter of 2014. This percentage change resulted from the following:

|  | Third<br>Quarter<br>Increase<br>(Decrease)<br>as a<br>Percentage<br>of Total<br>Revenue |
|--|---|
| Incentive compensation expense           | 0.8 %   |
| Proxy contest expenses in the prior year | (0.2 %)   |

General and administrative expenses as a percentage of total revenue increased to 5.1% in the first nine months of 2015 as compared to 5.0% in the same period in the prior year. This percentage change resulted primarily from the following:

First Nine  
Months  
Increase  
(Decrease)

|  | as a<br>Percentage<br>of Total<br>Revenue |    |
|--|---|----|
| Incentive compensation expense           | 0.4                                       | %  |
| Litigation accrual                       | 0.2                                       | %  |
| Proxy contest expenses in the prior year | (0.2)                                     | %) |
| Payroll and related expenses             | (0.2)                                     | %) |

Higher incentive compensation in the third quarter and first nine months of 2015 as compared to the same periods in the prior year resulted primarily from better performance against financial objectives as compared to the prior year and an increase in the price of our common stock in 2015.

In the third quarter and first nine months of 2014, we incurred \$1,113 and \$4,313, respectively, in costs related to a proxy contest at our Annual Shareholders Meeting and a Special Meeting of Shareholders.

We recorded a total provision of approximately \$3,500 for the first nine months of 2015 related to the potential liability associated with the previously disclosed Fair Labor Standards Act (“FLSA”) litigation. See Note 12 to our Condensed Consolidated Financial Statements and “Item 1. Legal Proceedings” of Part II of this Quarterly Report on Form 10-Q for further information related to the FLSA litigation.

Lower payroll and related expenses in the first nine months of 2015 as compared to the same period in the prior year resulted primarily from a reduction in employee health care costs and the increase in revenue.

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### Interest Expense

Interest expense for the third quarter of 2015 was \$4,030 as compared to \$4,327 in the third quarter of 2014. Interest expense for the first nine months of 2015 was \$13,138 as compared to \$13,205 in the same period in the prior year. The decrease in interest expense for the third quarter of 2015 as compared to the third quarter of 2014 resulted primarily from the reduction in our credit spread by 0.25% as a result of our debt refinancing in January 2015. The decrease in interest expense for the first nine months of 2015 as compared to the same period in the prior year resulted primarily from the reduction in our credit spread by 0.25% partially offset by the write-off of \$412 in deferred financing costs as a result of our debt refinancing. See the discussion below under “Borrowing Capacity and Debt Covenants” for further information on our debt refinancing.

### Provision for Income Taxes

Provision for income taxes as a percentage of income before income taxes (the “effective tax rate”) was 31.4% and 29.7%, respectively in the third quarters of 2015 and 2014. The increase in the effective tax rate from the third quarter of 2014 to the third quarter of 2015 resulted primarily from an increase in pretax income. The effective tax rate remained flat at 31.1% in the first nine months of 2015 and 2014 primarily due an increase in pretax income offset by the impact of the retroactive reinstatement of the Work Opportunity Tax Credit through December 31, 2014. We presently expect our effective tax rate for 2015 to be between 31% and 32%.

## Liquidity and Capital Resources

Our primary sources of liquidity are cash generated from our operations and our borrowing capacity under our \$750,000 revolving credit facility (the “2015 Revolving Credit Facility”). Our internally generated cash, along with cash on hand at August 1, 2014, was sufficient to finance all of our growth, dividend payments, working capital needs and other cash payment obligations in the third quarter of 2015.

We believe that cash on hand at May 1, 2015, along with cash generated from our operating activities and the borrowing capacity under our 2015 Revolving Credit Facility will be sufficient to finance our continuing operations, expected dividend payments and our continuing expansion plans for at least the next twelve months.

### Cash Generated From Operations

Our operating activities provided net cash of \$216,680 for the third quarter of 2015, which represented an increase from the \$101,197 net cash provided during the third quarter of 2014. This increase primarily reflected lower retail inventory, lower accounts payable disbursements, higher net income and the timing of payments for estimated income taxes.

### Borrowing Capacity and Debt Covenants

On January 8, 2015, we entered into a five-year \$750,000 revolving credit facility. The 2015 Revolving Credit Facility replaced a term loan totaling \$181,250 and a \$218,750 revolving credit facility (“Prior Credit Facility”). At May 1, 2015, we had \$400,000 of outstanding borrowings under the 2015 Revolving Credit Facility and we had \$11,530 of standby letters of credit related to securing reserved claims under our workers’ compensation insurance which reduce our borrowing availability under the 2015 Revolving Credit Facility. At May 1, 2015, we had \$338,470 in borrowing availability under our 2015 Revolving Credit Facility. See Note 4 to our Condensed Consolidated Financial Statements for further information on our long-term debt.

Similar to the Prior Credit Facility, the 2015 Revolving Credit Facility contains customary financial covenants, which include maintenance of a maximum consolidated total leverage ratio and a minimum consolidated interest coverage



ratio. We presently are in compliance with all financial covenants.

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### Capital Expenditures

Capital expenditures (purchase of property and equipment) net of proceeds from insurance recoveries were \$60,055 for the first nine months of 2015 as compared to \$62,337 for the same period in the prior year. Our capital expenditures consisted primarily of capital expenditures for maintenance programs, technology and operations improvements and costs of new store locations. We estimate that our capital expenditures during 2015 will be approximately \$95,000. This estimate includes the acquisition of sites and construction costs of approximately six new stores that have opened or are expected to open during 2015, as well as for acquisition and construction costs for store locations to be opened in 2016, capital expenditures for maintenance programs and technology and operations improvements. We intend to fund our capital expenditures with cash flows from operations and borrowings under our 2015 Revolving Credit Facility, as necessary.

### Dividends, Share Repurchases and Share-Based Compensation Awards

The 2015 Revolving Credit Facility imposes restrictions on the amount of dividends we are permitted to pay and the amount of shares we are permitted to repurchase. Under the 2015 Revolving Credit Facility, provided there is no default existing and the total of our availability under the 2015 Revolving Credit Facility plus our cash and cash equivalents on hand is at least \$100,000 (the "cash availability"), we may declare and pay cash dividends on shares of our common stock and repurchase shares of our common stock (1) in an unlimited amount if at the time of the dividend or the repurchase is made our consolidated total leverage ratio is 3.00 to 1.00 or less and (2) in an aggregate amount not to exceed \$100,000 in any fiscal year if our consolidated total leverage ratio is greater than 3.00 to 1.00 at the time the dividend or repurchase is made; notwithstanding (1) and (2), so long as immediately after giving effect to the payment of any such dividends, cash availability is at least \$100,000, we may declare and pay cash dividends on shares of our common stock in an aggregate amount not to exceed in any fiscal year the product of the aggregate amount of dividends declared in the fourth quarter of the immediately preceding fiscal year multiplied by four.

During the first nine months of 2015, we paid dividends of \$3.00 per share, or an aggregate of \$71,750. During the third quarter of 2015, we declared a dividend of \$1.00 per share that was paid on May 5, 2015 to shareholders of record on April 17, 2015. On June 2, 2015, we declared a regular dividend of \$1.10 per share and a special dividend of \$3.00 per share, both payable on August 5, 2015 to shareholders of record on July 17, 2015.

We have been authorized by our Board of Directors to repurchase shares at management's discretion up to \$25,000 during 2015. We did not repurchase any shares during the first nine months of 2015.

During the first nine months of 2015, we issued 127,857 shares of our common stock resulting from the vesting of share-based compensation awards and stock option exercises. Related tax withholding payments on certain share-based compensation awards exceeded proceeds received from the exercise of stock options, which resulted in a net use of cash of \$3,432.

### Working Capital

In the restaurant industry, virtually all sales are either for cash or first-party credit or debit card. Restaurant inventories purchased through our principal food distributor are on terms of net zero days, while restaurant inventories purchased locally are generally financed from normal trade credit. Because of our retail gift shops, which have a lower product turnover than the restaurant business, we carry larger inventories than many other companies in the restaurant industry. Retail inventories purchased domestically are generally financed from normal trade credit, while imported retail inventories are generally purchased through wire transfers. These various trade terms are aided by the rapid turnover of the restaurant inventory. Employees generally are paid on weekly or semi-monthly schedules in arrears for hours worked except for bonuses that are paid either quarterly or annually in arrears. Many other operating expenses have normal trade terms and certain expenses, such as certain taxes and some benefits, are deferred for

longer periods of time.

We had positive working capital of \$75,447 at May 1, 2015 versus negative working capital of \$14,789 at August 1, 2014. Working capital increased from August 1, 2014 primarily because of an increase in cash generated from operations and a decrease in our current maturities on our long-term debt due to our debt refinancing partially offset by lower retail inventories.

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Off-Balance Sheet Arrangements

Other than various operating leases, we have no other material off-balance sheet arrangements. Refer to the sub-section entitled “Off-Balance Sheet Arrangements” under the section entitled “Liquidity and Capital Resources” presented in the MD&A of our 2014 Form 10-K for additional information regarding our operating leases.

Material Commitments

There have been no material changes in our material commitments other than in the ordinary course of business since the end of 2014. Refer to the sub-section entitled “Material Commitments” under the section entitled “Liquidity and Capital Resources” presented in the MD&A of our 2014 Form 10-K for additional information regarding our material commitments.

Critical Accounting Estimates

We prepare our Consolidated Financial Statements in conformity with GAAP. The preparation of these financial statements requires us to make estimates and assumptions about future events and apply judgments that affect the reported amounts of assets, liabilities, revenue, expenses and related disclosures. We base our estimates and judgments on historical experience, current trends, outside advice from parties believed to be experts in such matters and on various other assumptions that are believed to be reasonable under the circumstances, the results of which form the basis for making judgments about the carrying value of assets and liabilities that are not readily apparent from other sources. However, because future events and their effects cannot be determined with certainty, actual results could differ from those assumptions and estimates, and such differences could be material.

Our significant accounting policies are discussed in Note 2 to the Consolidated Financial Statements contained in the 2014 Form 10-K. Judgments and uncertainties affecting the application of those policies may result in materially different amounts being reported under different conditions or using different assumptions.

Critical accounting estimates are those that:

· management believes are most important to the accurate portrayal of both our financial condition and operating results, and  
· require management’s most difficult, subjective or complex judgments, often as a result of the need to make estimates about the effect of matters that are inherently uncertain.

We consider the following accounting estimates to be most critical in understanding the judgments that are involved in preparing our Consolidated Financial Statements:

- Impairment of Long-Lived Assets and Provision for Asset Dispositions
- Insurance Reserves
- Retail Inventory Valuation
- Tax Provision
- Share-Based Compensation
- Legal Proceedings

Management has reviewed these critical accounting estimates and related disclosures with the Audit Committee of our Board of Directors.

Impairment of Long-Lived Assets and Provision for Asset Dispositions

We assess the impairment of long-lived assets whenever events or changes in circumstances indicate that the carrying value of an asset may not be recoverable. Recoverability of assets is measured by comparing the carrying value of the asset to the undiscounted future cash flows expected to be generated by the asset. If the total expected future cash flows are less than the carrying amount of the asset, the carrying value is written down, for an asset to be held and used, to the estimated fair value or, for an asset to be disposed of, to the fair value, net of estimated costs of disposal. Any loss resulting from impairment is recognized by a charge to income. Judgments and estimates that we make related to the expected useful lives of long-lived assets and future cash flows are affected by factors such as changes in economic conditions and changes in operating performance. The accuracy of such provisions can vary materially from original estimates and management regularly monitors the adequacy of the provisions until final disposition occurs.

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We have not made any material changes in our methodology for assessing impairments during the first nine months of 2015, and we do not believe that there is a reasonable likelihood that there will be a material change in the estimates or assumptions used by us in the future to assess impairment of long-lived assets. However, if actual results are not consistent with our estimates and assumptions used in estimating future cash flows and fair values of long-lived assets, we may be exposed to losses that could be material.

## Insurance Reserves

We self-insure a significant portion of our expected workers' compensation and general liability insurance programs. We purchase insurance for individual workers' compensation claims that exceed \$250, \$500 or \$1,000 depending on the state in which the claim originates. We purchase insurance for individual general liability claims that exceed \$500. We record a reserve for workers' compensation and general liability for all unresolved claims and for an estimate of incurred but not reported ("IBNR") claims. These reserves and estimates of IBNR claims are based upon a full scope actuarial study which is performed annually at the end of our third quarter and is adjusted by the actuarially determined losses and actual claims payments for the fourth quarter. Additionally, we perform limited scope actuarial studies on a quarterly basis to verify and/or modify our reserves. The reserves and losses in the actuarial study represent a range of possible outcomes within which no given estimate is more likely than any other estimate. As such, we record the losses in the lower end of that range and discount them to present value using a risk-free interest rate based on projected timing of payments. We also monitor actual claims development, including incidence or settlement of individual large claims during the interim periods between actuarial studies as another means of estimating the adequacy of our reserves.

Our group health plans combine the use of self-insured and fully-insured programs. Benefits for any individual (employee or dependents) in the self-insured group health program are limited. We record a liability for the self-insured portion of our group health program for all unpaid claims based upon a loss development analysis derived from actual group health claims payment experience. Additionally, we record a liability for unpaid prescription drug claims based on historical experience. The fully-insured portion of our health insurance program contains a retrospective feature which could increase or decrease premiums based on actual claims experience.

Our accounting policies regarding workers' compensation, general insurance and health insurance reserves include certain actuarial assumptions and management judgments regarding economic conditions, the frequency and severity of claims and claim development history and settlement practices. We have not made any material changes in the accounting methodology used to establish our insurance reserves during the first nine months of 2015 and do not believe there is a reasonable likelihood that there will be a material change in the estimates or assumptions used to calculate the insurance reserves. However, changes in these actuarial assumptions, management judgments or claims experience in the future may produce materially different amounts of expense that would be reported under these insurance programs.

## Retail Inventory Valuation

Cost of goods sold includes the cost of retail merchandise sold at our stores utilizing the retail inventory method ("RIM"). Under RIM, the valuation of our retail inventories at cost and the resulting gross margins are calculated by applying a cost-to-retail ratio to the retail value of our inventories. Inherent in the RIM calculation are certain significant management judgments and estimates, including initial markons, markups, markdowns and shrinkage, which may significantly impact the gross margin calculation as well as the ending inventory valuation.

Inventory valuation provisions are included for retail inventory obsolescence and retail inventory shrinkage. Retail inventory is reviewed on a quarterly basis for obsolescence and adjusted as appropriate based on assumptions made by management and judgments regarding inventory aging and future promotional activities. Cost of goods sold includes an estimate of shrinkage that is adjusted upon physical inventory counts. Annual physical inventory counts are

conducted throughout the third and fourth quarters based upon a cyclical inventory schedule. An estimate of shrinkage is recorded for the time period between physical inventory counts by using a three-year average of the physical inventories' results on a store-by-store basis.

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We have not made any material changes in the methodologies, estimates or assumptions related to our merchandise inventories during the first nine months of 2015 and do not believe there is a reasonable likelihood that there will be a material change in the estimates or assumptions in the future. However, actual obsolescence or shrinkage recorded may produce materially different amounts than we have estimated.

## Tax Provision

We must make estimates of certain items that comprise our income tax provision. These estimates include effective state and local income tax rates, employer tax credits for items such as FICA taxes paid on employee tip income, Work Opportunity and Welfare to Work credits, as well as estimates related to certain depreciation and capitalization policies. Our estimates are made based on current tax laws, the best available information at the time of the provision and historical experience.

We recognize (or derecognize) a tax position taken or expected to be taken in a tax return in the financial statements when it is more likely than not (i.e., a likelihood of more than fifty percent) that the position would be sustained (or not sustained) upon examination by tax authorities. A recognized tax position is then measured at the largest amount of benefit that is greater than fifty percent likely of being realized upon ultimate settlement.

We file our income tax returns many months after our year end. These returns are subject to audit by various federal and state governments years after the returns are filed and could be subject to differing interpretations of the tax laws. We then must assess the likelihood of successful legal proceedings or reach a settlement with the relevant taxing authority. Although we believe that the judgments and estimates used in establishing our tax provision are reasonable, an unsuccessful legal proceeding or a settlement could result in material adjustments to our Consolidated Financial Statements and our consolidated financial position (see Note 13 to our Consolidated Financial Statements contained in the 2014 Form 10-K for additional information).

## Share-Based Compensation

Our share-based compensation consists of nonvested stock awards and performance-based market stock units (“MSU Grants”). Share-based compensation expense is recognized based on the grant date fair value and the achievement of performance conditions for certain awards. We recognize share-based compensation expense on a straight-line basis over the requisite service period, which is generally the award’s vesting period, or the date on which retirement is achieved, if shorter.

Compensation expense is recognized for only the portion of our share-based compensation awards that are expected to vest. Therefore, an estimated forfeiture rate is derived from historical employee termination behavior and is updated annually. The forfeiture rate is applied on a straight-line basis over the service (vesting) period for each separately vesting portion of the award as if the award were, in substance, multiple awards.

Beginning in 2014, our share-based compensation awards accrue dividends. Dividends will be forfeited for any share-based compensation awards that do not vest.

Our nonvested stock awards are time vested except for awards under our long-term incentive plans, which also contain performance conditions. At each reporting period, we reassess the probability of achieving the performance conditions under our long-term incentive plans. Determining whether the performance conditions will be achieved involves judgment, and the estimate of expense for nonvested stock awards may be revised periodically based on changes in our determination of the probability of achieving the performance conditions. Revisions are reflected in the period in which the estimate is changed. If any performance conditions are not met, no shares will be granted, no compensation will ultimately be recognized and, to the extent previously recognized, compensation expense will be reversed.



Generally, the fair value of each nonvested stock award that does not accrue dividends is equal to the market price of our common stock at the date of grant reduced by the present value of expected dividends to be paid prior to the vesting period, discounted using an appropriate risk-free interest rate. Other nonvested stock awards accrue dividends and their fair value is equal to the market price of our stock at the date of grant.

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In addition to providing the requisite service, MSU Grants contain both a market condition based on total shareholder return and a performance condition based on operating income. Total shareholder return is defined as increases in our stock price plus dividends paid during the performance period. The number of shares awarded at the end of the performance period for each MSU Grant may increase up to 150% of target in direct proportion to any percentage increase in shareholder value during the performance period. The probability of the actual shares expected to be awarded is considered in the grant date valuation; therefore, the expense will not be adjusted to reflect the actual units awarded. However, if the performance condition is not met, no shares will be granted, no compensation will ultimately be recognized and, to the extent previously recognized, compensation expense will be reversed.

The fair value of our MSU Grants was determined using the Monte-Carlo simulation model, which simulates a range of possible future stock prices and estimates the probabilities of the potential payouts. The Monte-Carlo simulation model uses the average prices for the 60-consecutive calendar days beginning 30 days prior to and ending 30 days after the first business day of the performance period. This model also incorporates the following ranges of assumptions:

The expected volatility is a blend of implied volatility based on market-traded options on our stock and historical volatility of our stock over the period commensurate with the three-year performance period.

The risk-free interest rate is based on the U.S. Treasury rate assumption commensurate with the three-year performance period.

The expected dividend yield is based on our current dividend yield as the best estimate of projected dividend yield for periods within the three-year performance period.

We update the historical and implied components of the expected volatility assumption when new grants are made.

We have not made any material changes in our estimates or assumptions used to determine share-based compensation during the first nine months of 2015 and do not believe there is a reasonable likelihood that there will be a material change in the future estimates or assumptions used to determine share-based compensation expense. However, if actual results are not consistent with our estimates or assumptions, we may be exposed to changes in share-based compensation expense that could be material.

## Legal Proceedings

We are parties to various legal and regulatory proceedings and claims incidental to our business from time to time. We review outstanding claims and proceedings internally and with external counsel, as necessary and appropriate, to assess probability of loss and for the ability to estimate loss. These assessments are re-evaluated each quarter or as new information becomes available to determine whether a reserve should be established or if any existing reserve should be adjusted. The actual cost of resolving a claim or proceeding ultimately may be substantially different than the amount of the recorded reserve. Although we believe that the judgments and estimates used in establishing our legal reserves are reasonable, an unsuccessful legal proceeding or a settlement could result in material adjustments to our Condensed Consolidated Financial Statements and our consolidated financial position (see Note 12 to our Condensed Consolidated Financial Statements and “Item 1. Legal Proceedings” of Part II of this Quarterly Report on Form 10-Q for further information).

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ITEM 3. Quantitative and Qualitative Disclosures About Market Risk

Part II, Item 7A of the 2014 Form 10-K is incorporated in this item of this Quarterly Report on Form 10-Q by this reference. There have been no material changes in our quantitative and qualitative market risks since August 1, 2014.

ITEM 4. Controls and Procedures

Our management, including our principal executive and principal financial officers, evaluated the effectiveness of our disclosure controls and procedures (as defined in Rules 13a-15(e) and 15d-15(e) promulgated under the Exchange Act) as of the end of the period covered by this report. Based upon this evaluation, our Chief Executive Officer and Chief Financial Officer each concluded that as of May 1, 2015, our disclosure controls and procedures were effective for the purposes set forth in the definition thereof in Exchange Act Rule 13a-15(e).

There have been no changes (including corrective actions with regard to significant deficiencies and material weaknesses) during the quarter ended May 1, 2015 in our internal control over financial reporting (as defined in Exchange Act Rule 13a-15(f)) that have materially affected, or are reasonably likely to materially affect, our internal control over financial reporting.

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PART II. OTHER INFORMATION

ITEM 1. Legal Proceedings

FLSA Litigation

On April 11, 2014, a putative collective action under the Fair Labor Standards Act (“FLSA”) was filed in the United States District Court for the Northern District of New York, *Proper v. Cracker Barrel Old Country Store, Inc.*, in which the named plaintiff is challenging the Company’s classification of associate managers as being exempt from the minimum wage and overtime requirements and is asserting various New York state law wage notice claims. Two other putative collective action suits alleging claims under the FLSA, *Hill and Hernandez v. Cracker Barrel* and *Perzan et al. v. Cracker Barrel*, were filed in the United States District Courts for the Middle District of Florida in August 2014 and for the District of Massachusetts in September 2014, respectively. These lawsuits assert essentially duplicative claims under select state laws challenging the same exempt classification of associate managers. The plaintiffs in these lawsuits seek an unspecified amount of alleged back wages, liquidated damages, statutory damages and attorneys’ fees. Although we continue to believe that our associate managers are and have been properly classified as exempt employees under FLSA and have therefore aggressively challenged the plaintiffs’ claims in these lawsuits, in light of the potential cost and uncertainty involved in these lawsuits, in March 2015, we entered into a memorandum of understanding (the “MOU”) with respect to a settlement with plaintiffs’ counsel to resolve the series of lawsuits. In May 2015, the parties executed the settlement agreement based on the MOU, and the final resolution of these matters through settlement is subject to final court approval. The Company has recorded a provision of approximately \$3,500 at May 1, 2015 related to these lawsuits. With the exception of this provision relating to these lawsuits recorded at May 1, 2015, no other provision for any potential liability has been made in the condensed consolidated financial statements of the Company related to these proceedings.

In addition to the matters described above, the Company and its subsidiaries are party to various other legal and regulatory proceedings and claims incidental to their business in the ordinary course. In the opinion of management, based upon information currently available, the ultimate liability with respect to these other proceedings and claims will not materially affect the Company’s consolidated results of operations or financial position.

ITEM 1A. Risk Factors

There have been no material changes in the risk factors previously disclosed in “Item 1A. Risk Factors” of our 2014 Form 10-K.

ITEM 6. Exhibits

See Exhibit Index immediately following the signature page hereto.

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SIGNATURES

Pursuant to the requirements of the Securities Exchange Act of 1934, the registrant has duly caused this report to be signed on its behalf by the undersigned thereunto duly authorized.

CRACKER BARREL OLD COUNTRY STORE, INC.

Date: June 2, 2015 By: /s/Lawrence E. Hyatt  
Lawrence E. Hyatt, Senior Vice President and  
Chief Financial Officer

Date: June 2, 2015 By: /s/P. Douglas Couvillion  
P. Douglas Couvillion, Vice President, Corporate Controller and  
Principal Accounting Officer

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INDEX TO EXHIBITS

Exhibit

4.1 Rights Agreement, dated as of April 9, 2015, between Cracker Barrel Old Country Store, Inc. and American Stock Transfer & Trust Company, LLC, which includes the Articles of Amendment to the Amended and Restated Charter as Exhibit A, the form of Right Certificate as Exhibit B, and the Summary of Rights to Purchase Preferred Shares as Exhibit C (incorporated by reference to Exhibit 4.1 to the Company's Report on Form 8-K filed on April 9, 2015)

31.1 Certification of Chief Executive Officer pursuant to Section 302 of the Sarbanes-Oxley Act of 2002 (filed herewith)

31.2 Certification of Chief Financial Officer pursuant to Section 302 of the Sarbanes-Oxley Act of 2002 (filed herewith)

32.1 Certification of Chief Executive Officer pursuant to Section 906 of the Sarbanes-Oxley Act of 2002 (filed herewith)

32.2 Certification of Chief Financial Officer pursuant to Section 906 of the Sarbanes-Oxley Act of 2002 (filed herewith)

101.INS XBRL Instance Document (filed herewith)

101.SCHXBRL Taxonomy Extension Schema (filed herewith)

101.CALXBRL Taxonomy Extension Calculation Linkbase (filed herewith)

101.LABXBRL Taxonomy Extension Label Linkbase (filed herewith)

101.PRE XBRL Taxonomy Extension Presentation Linkbase (filed herewith)

101.DEF XBRL Taxonomy Extension Definition Linkbase (filed herewith)

Denotes management contract or compensatory plan, contract or arrangement.