PAPA JOHNS INTERNATIONAL INC
Form 10-Q
August 04, 2015
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UNITED STATES

SECURITIES AND EXCHANGE COMMISSION

Washington, D.C. 20549

FORM 10-Q

(Mark One)

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

For the quarterly period ended June 28, 2015

OR

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

Commission File Number: 0-21660

PAPA JOHN S INTERNATIONAL, INC.

(Exact name of registrant as specified in its charter)

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

2002 Papa Johns Boulevard

Louisville, Kentucky 40299-2367

(Address of principal executive offices)

(502) 261-7272

(Registrant s telephone number, including area code)

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

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

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 x	Accelerated filer o
Non-accelerated filer o	Smaller reporting company o

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

At July 28, 2015, there were outstanding 39,457,802 shares of the registrant s common stock, par value $0.01 per share.

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PART 1. FINANCIAL INFORMATION

Item 1. Financial Statements

Papa John s International, Inc. and Subsidiaries

Condensed Consolidated Balance Sheets

(In thousands, except per share amounts)	June 28, 2015 (Unaudited)	December 28, 2014
Assets		
Current assets:		
Cash and cash equivalents	$ 22,447	$ 20,122
Accounts receivable, net	53,083	56,047
Notes receivable, net	6,422	6,106
Income taxes receivable	10,808	9,527
Inventories	23,848	27,394
Deferred income taxes	9,312	8,248
Prepaid expenses	17,737	18,736
Other current assets	9,535	9,828
Total current assets	153,192	156,008
Property and equipment, net	215,208	219,457
Notes receivable, less current portion, net	12,009	12,801
Goodwill	82,291	82,007
Deferred income taxes	3,537	3,914
Other assets	36,805	38,616
Total assets	$ 503,042	$ 512,803
Liabilities and stockholders equity		
Current liabilities:		
Accounts payable	$ 35,029	$ 38,832
Income and other taxes payable	9,709	9,637
Accrued expenses and other current liabilities	73,161	58,293
Total current liabilities	117,899	106,762
Deferred revenue	3,926	4,257
Long-term debt	234,000	230,451
Deferred income taxes	19,792	22,188
Other long-term liabilities	42,262	41,875
Total liabilities	417,879	405,533
Redeemable noncontrolling interests	7,741	8,555
Stockholders equity:		
Preferred stock ($0.01 par value per share; no shares issued)		
Common stock ($0.01 par value per share; issued 43,684 at June 28, 2015 and 43,331 at December 28, 2014)	437	433
Additional paid-in capital	152,569	147,912
Accumulated other comprehensive income	639	671

Retained earnings		114,908		92,876
Treasury stock (4,290 shares at June 28, 2015 and 3,549 shares at December 28, 2014, at cost)		(204,309)		(155,659)
Total stockholders equity, net of noncontrolling interests		64,244		86,233
Noncontrolling interests in subsidiaries		13,178		12,482
Total stockholders equity		77,422		98,715
Total liabilities, redeemable noncontrolling interests and stockholders equity	$	503,042	$	512,803

See accompanying notes.

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Papa John s International, Inc. and Subsidiaries

Condensed Consolidated Statements of Income

(Unaudited)

(In thousands, except per share amounts)	Three Months Ended June 28, 2015	Three Months Ended June 29, 2014	Six Months Ended June 28, 2015	Six Months Ended June 29, 2014
North America revenues:				
Domestic Company-owned restaurant sales	$ 185,962	$ 170,000	$ 383,249	$ 348,193
Franchise royalties	23,081	20,983	48,440	43,597
Franchise and development fees	195	132	460	276
Domestic commissary sales	149,007	150,581	311,340	314,628
Other sales	14,420	13,595	36,034	26,345
International revenues:				
Royalties and franchise and development fees	6,641	6,317	13,139	12,096
Restaurant and commissary sales	19,685	19,256	38,613	37,106
Total revenues	398,991	380,864	831,275	782,241
Costs and expenses:				
Domestic Company-owned restaurant expenses:				
Cost of sales	43,289	42,030	90,793	87,186
Salaries and benefits	51,502	45,805	105,160	93,388
Advertising and related costs	16,492	15,354	33,262	31,610
Occupancy costs and other restaurant operating expenses	36,073	34,666	73,173	69,264
Total domestic Company-owned restaurant expenses	147,356	137,855	302,388	281,448
Domestic commissary expenses:				
Cost of sales	113,777	118,470	238,903	247,394
Salaries and benefits and other commissary operating expenses	23,781	23,062	48,391	45,941
Total domestic commissary expenses	137,558	141,532	287,294	293,335
Other operating expenses	13,648	13,221	34,251	24,652
International restaurant and commissary expenses	16,250	15,876	31,728	30,761
General and administrative expenses	42,043	33,562	83,976	70,528
Other general expenses	1,004	1,964	2,820	3,497
Depreciation and amortization	10,136	9,855	20,177	19,019
Total costs and expenses	367,995	353,865	762,634	723,240
Operating income	30,996	26,999	68,641	59,001
Legal settlement expense	(12,278)		(12,278)	
Net interest (expense) income	(1,187)	(763)	(2,396)	(1,355)
Income before income taxes	17,531	26,236	53,967	57,646
Income tax expense	5,063	8,397	17,260	19,266
Net income before attribution to noncontrolling interests	12,468	17,839	36,707	38,380
Income attributable to noncontrolling interests	(1,688)	(1,091)	(3,691)	(2,321)
Net income attributable to the Company	$ 10,780	$ 16,748	$ 33,016	$ 36,059
Calculation of income for earnings per share:				
Net income attributable to the Company	$ 10,780	$ 16,748	$ 33,016	$ 36,059
Decrease (increase) in noncontrolling interest redemption value	73	(31)	143	(39)
Net income attributable to participating securities	(50)	(81)	(150)	(218)
Net income attributable to common shareholders	$ 10,803	$ 16,636	$ 33,009	$ 35,802

Basic earnings per common share	$ 0.27	$ 0.40	$ 0.83	$ 0.86
Diluted earnings per common share	$ 0.27	$ 0.40	$ 0.82	$ 0.85
Basic weighted average common shares outstanding	39,692	41,225	39,764	41,501
Diluted weighted average common shares outstanding	40,217	41,970	40,368	42,332
Dividends declared per common share	$ 0.14	$ 0.125	$ 0.28	$ 0.25

See accompanying notes.

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Papa John s International, Inc. and Subsidiaries

Consolidated Statements of Comprehensive Income

(Unaudited)

(In thousands)	Three Months Ended June 28, 2015	Three Months Ended June 29, 2014	Six Months Ended June 28, 2015	Six Months Ended June 29, 2014
Net income before attribution to noncontrolling interests	$ 12,468	$ 17,839	$ 36,707	$ 38,380
Other comprehensive income (loss), before tax:				
Foreign currency translation adjustments	2,116	959	575	926
Interest rate swaps (1)	459	(404)	(625)	(447)
Other comprehensive income (loss), before tax	2,575	555	(50)	479
Income tax effect:				
Foreign currency translation adjustments	(783)	(355)	(213)	(343)
Interest rate swaps (2)	(170)	149	231	165
Income tax effect	(953)	(206)	18	(178)
Other comprehensive income (loss), net of tax	1,622	349	(32)	301
Comprehensive income before attribution to noncontrolling interests	14,090	18,188	36,675	38,681
Comprehensive loss, redeemable noncontrolling interests	(1,015)	(1,086)	(2,328)	(2,341)
Comprehensive (loss) income, nonredeemable noncontrolling interests	(673)	(5)	(1,363)	20
Comprehensive income attributable to the Company	$ 12,402	$ 17,097	$ 32,984	$ 36,360

(1) Amounts reclassified out of accumulated other comprehensive income (AOCI) into net interest (expense) income included $393 and $787 for the three and six months ended June 28, 2015, respectively and $250 and $499 for the three and six months ended June 29, 2014, respectively.

(2) The income tax effects of amounts reclassified out of AOCI into net interest (expense) income were $145 and $291 for the three and six months ended June 28, 2015, respectively and $93 and $185 for the three and six months ended June 29, 2014, respectively.

See accompanying notes.

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Papa John s International, Inc. and Subsidiaries

Consolidated Statements of Cash Flows

(Unaudited)

(In thousands)	**Six Months Ended June 28, 2015**	**Six Months Ended June 29, 2014**
Operating activities		
Net income before attribution to noncontrolling interests	$ 36,707	$ 38,380
Adjustments to reconcile net income to net cash provided by operating activities:		
Provision for uncollectible accounts and notes receivable	631	936
Depreciation and amortization	20,177	19,019
Deferred income taxes	6,424	6,298
Stock-based compensation expense	4,985	3,612
Excess tax benefit on equity awards	(9,488)	(7,890)
Other	2,239	2,270
Changes in operating assets and liabilities, net of acquisitions:		
Accounts receivable	1,682	3,400
Income taxes receivable	(1,281)	
Inventories	3,474	(7,295)
Prepaid expenses	999	180
Other current assets	293	(152)
Other assets and liabilities	(773)	(17)
Accounts payable	(3,877)	(1,934)
Income and other taxes payable	72	1,423
Accrued expenses and other current liabilities	15,495	(3,970)
Deferred revenue	223	305
Net cash provided by operating activities	77,982	54,565
Investing activities		
Purchases of property and equipment	(16,501)	(26,239)
Loans issued	(1,571)	(2,642)
Repayments of loans issued	2,787	1,880
Acquisitions, net of cash acquired	(491)	(3,179)
Other	348	3
Net cash used in investing activities	(15,428)	(30,177)
Financing activities		
Net proceeds on line of credit facility	3,549	52,100
Cash dividends paid	(11,083)	(10,404)
Excess tax benefit on equity awards	9,488	7,890
Tax payments for equity award issuances	(10,654)	(7,498)
Proceeds from exercise of stock options	3,915	3,361
Acquisition of Company common stock	(52,083)	(63,304)
Contributions from noncontrolling interest holders	683	100
Distributions to noncontrolling interest holders	(4,350)	(600)
Other	319	293
Net cash used in financing activities	(60,216)	(18,062)
Effect of exchange rate changes on cash and cash equivalents	(13)	(25)
Change in cash and cash equivalents	2,325	6,301
Cash and cash equivalents at beginning of period	20,122	13,670
Cash and cash equivalents at end of period	$ 22,447	$ 19,971

See accompanying notes.

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Papa John s International, Inc. and Subsidiaries

Notes to Condensed Consolidated Financial Statements (Unaudited)

June 28, 2015

1. Basis of Presentation

The accompanying unaudited condensed consolidated financial statements have been prepared in accordance with accounting principles generally accepted in the United States (GAAP) for interim financial information and with the instructions to Form 10-Q and Article 10 of Regulation S-X. Accordingly, they do not include all of the information and footnotes required by GAAP for complete financial statements. In the opinion of management, all adjustments, consisting of normal recurring accruals, considered necessary for a fair presentation have been included. Operating results for the six months ended June 28, 2015 are not necessarily indicative of the results that may be expected for the fiscal year ended December 27, 2015. For further information, refer to the consolidated financial statements and footnotes thereto included in the Annual Report on Form 10-K for Papa John s International, Inc. (referred to as the Company, Papa John s or in the first person notations of we, and our) for the year ended December 28, 2014.

2. Significant Accounting Policies

Noncontrolling Interests

Papa John s has joint ventures in which there are noncontrolling interests, including the following as of June 28, 2015 and June 29, 2014:

	Number of Restaurants	Restaurant Locations	Papa John s Ownership	Noncontrolling Interest Ownership
June 28, 2015				
Star Papa, LP	84	Texas	51%	49%
Colonel s Limited, LLC	61	Maryland and Virginia	70%	30%
PJ Minnesota, LLC	35	Minnesota	70%	30%
PJ Denver, LLC	26	Colorado	60%	40%
June 29, 2014				
Star Papa, LP	81	Texas	51%	49%
Colonel s Limited, LLC	52	Maryland and Virginia	70%	30%
PJ Minnesota, LLC	34	Minnesota	80%	20%

PJ Denver, LLC	25	Colorado	60%	40%

We are required to report consolidated net income at amounts attributable to the Company and the noncontrolling interests. Additionally, disclosures are required to clearly identify and distinguish between the interests of the Company and the interests of the noncontrolling owners, including a disclosure on the face of the condensed consolidated statements of income attributable to the noncontrolling interest holder.

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The income before income taxes attributable to these joint ventures for the three and six months ended June 28, 2015 and June 29, 2014 was as follows (in thousands):

	Three Months Ended		Six Months Ended	
	June 28, 2015	June 29, 2014	June 28, 2015	June 29, 2014
Papa John s International, Inc.	$ 2,660	$ 1,744	$ 5,670	$ 3,592
Noncontrolling interests	1,688	1,091	3,691	2,321
Total income before income taxes	$ 4,348	$ 2,835	$ 9,361	$ 5,913

The following summarizes the redemption feature, location within the condensed consolidated balance sheets and the value at which the noncontrolling interests are recorded for each joint venture as of June 28, 2015:

Joint Venture	Redemption Feature	Location within the Condensed Consolidated Balance Sheets	Recorded Value
Star Papa, LP	Redeemable	Temporary equity	Carrying value
PJ Denver, LLC	Redeemable	Temporary equity	Redemption value
Colonel s Limited, LLC	No redemption feature	Permanent equity	Carrying value
PJ Minnesota, LLC	No redemption feature	Permanent equity	Carrying value

The noncontrolling interest holders of two joint ventures have the option to require the Company to purchase their interests. Since redemption of the noncontrolling interests is outside of the Company s control, the noncontrolling interests are presented in the caption Redeemable noncontrolling interests in the condensed consolidated balance sheets and include the following joint ventures:

- The Star Papa, LP agreement contains a redemption feature that is not currently redeemable, but it is probable to become redeemable in the future. Due to specific valuation provisions contained in the agreement, this noncontrolling interest has been recorded at its carrying value.

- The PJ Denver, LLC agreement contains a redemption feature that is currently redeemable and, therefore, this noncontrolling interest has been recorded at its current redemption value. The change in redemption value is recorded as an adjustment to Redeemable noncontrolling interests and Retained earnings in the condensed consolidated balance sheets.

The following summarizes changes in these redeemable noncontrolling interests (in thousands):

Balance at December 28, 2014	$	8,555
Net income		2,329
Distributions		(3,000)
Change in redemption value		(143)
Balance at June 28, 2015	$	7,741

The noncontrolling interests of our Colonel s Limited, LLC and PJ Minnesota, LLC joint ventures are recorded at carrying value in Stockholders equity in the condensed consolidated balance sheets at both June 28, 2015 and December 28, 2014, as the noncontrolling interest holders agreements had no redemption features.

Deferred Income Tax Accounts and Tax Reserves

We are subject to income taxes in the United States and several foreign jurisdictions. Significant judgment is required in determining our provision for income taxes and the related assets and liabilities. The provision for

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income taxes includes income taxes paid, currently payable or receivable and those deferred. We use an estimated annual effective rate based on expected annual income to determine our quarterly provision for income taxes. Discrete items are recorded in the quarter in which they occur.

Deferred tax assets and liabilities are determined based on differences between financial reporting and tax basis of assets and liabilities and are measured using enacted tax rates and laws that are expected to be in effect when the differences reverse. Deferred tax assets are also recognized for the estimated future effects of tax loss carryforwards. The effect on deferred taxes of changes in tax rates is recognized in the period in which the new tax rate is enacted. As a result, our effective tax rate may fluctuate. Valuation allowances are established when necessary on a jurisdictional basis to reduce deferred tax assets to the amounts we expect to realize. As of June 28, 2015, we had a net deferred tax liability of approximately $6.9 million.

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

Fair Value Measurements and Disclosures

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

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

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

Our financial assets and liabilities that were measured at fair value on a recurring basis as of June 28, 2015 and December 28, 2014 are as follows (in thousands):

	Carrying	**Fair Value Measurements**

	Value	Level 1	Level 2	Level 3
June 28, 2015				
Financial assets:				
Cash surrender value of life insurance policies (a)	$ 18,758	$ 18,758	$	$
Financial liabilities:				
Interest rate swaps (b)	1,021		1,021	
December 28, 2014				
Financial assets:				
Cash surrender value of life insurance policies (a)	$ 18,238	$ 18,238	$	$
Financial liabilities:				
Interest rate swaps (b)	376		376	

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

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

There were no transfers among levels within the fair value hierarchy during the six months ended June 28, 2015.

Variable Interest Entities

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

Revenue from Contracts with Customers

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

We are required to adopt the new requirements in the first quarter of 2018 based on the FASB s decision to defer the effective date by one year. We are evaluating the method of adoption and its impact of the new requirements on our consolidated financial statements. We currently do not believe the impact will be significant.

3. Calculation of Earnings Per Share

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

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

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

	Three Months Ended		Six Months Ended	
	June 28, 2015	June 29, 2014	June 28, 2015	June 29, 2014
Basic earnings per common share:				
Net income attributable to the Company	$ 10,780	$ 16,748	$ 33,016	$ 36,059
Decrease (increase) in noncontrolling interest redemption value	73	(31)	143	(39)
Net income attributable to participating securities	(50)	(81)	(150)	(218)
Net income attributable to common shareholders	$ 10,803	$ 16,636	$ 33,009	$ 35,802
Weighted average common shares outstanding	39,692	41,225	39,764	41,501
Basic earnings per common share	$ 0.27	$ 0.40	$ 0.83	$ 0.86
Diluted earnings per common share:				
Net income attributable to common shareholders	$ 10,803	$ 16,636	$ 33,009	$ 35,802
Weighted average common shares outstanding	39,692	41,225	39,764	41,501
Dilutive effect of outstanding equity awards (a)	525	745	604	831
Diluted weighted average common shares outstanding	40,217	41,970	40,368	42,332
Diluted earnings per common share	$ 0.27	$ 0.40	$ 0.82	$ 0.85

(a) Excludes 292 and 198 awards for the three and six months ended June 28, 2015 and 284 and 176 awards for the three and six months ended June 29, 2014, as the effect of including such awards would have been antidilutive.

4. Debt

Our debt is comprised entirely of an unsecured revolving line of credit (Credit Facility). The outstanding balance was $234.0 million as of June 28, 2015 and $230.5 million as of December 28, 2014. On October 31, 2014, we amended our Credit Facility to increase the amount available to $400 million from the previous $300 million availability and to extend the maturity date from April 30, 2018 to October 31, 2019. Additionally, we have the option to increase the Credit Facility an additional $100 million. The interest rate charged on outstanding balances is LIBOR plus 75 to 175 basis points. The commitment fee on the unused balance ranges from 15 to 25 basis points. The remaining availability under the Credit Facility, reduced for outstanding letters of credit, was approximately $147.2 million as of June 28, 2015.

The Credit Facility contains customary affirmative and negative covenants, including financial covenants requiring the maintenance of specified fixed charges and leverage ratios. At June 28, 2015, we were in compliance with these covenants.

We use interest rate swaps to hedge against the effects of potential interest rate increases on borrowings under our Credit Facility. We currently have the following interest rate swaps:

Effective Dates	Debt Amount	Fixed Rates
July 30, 2013 through April 30, 2018	$75 million	1.42%
December 30, 2014 through April 30, 2018	$50 million	1.36%

Our swaps are derivative instruments that are designated as cash flow hedges because the swaps provide a hedge against the effects of rising interest rates on borrowings. The effective portion of the gain or loss on the swaps is reported as a component of accumulated other comprehensive income and reclassified into earnings in the same

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period or periods during which the swaps affect earnings. Gains or losses on the swaps representing either hedge ineffectiveness or hedge components excluded from the assessment of effectiveness are recognized in current earnings. Amounts payable or receivable under the swaps are accounted for as adjustments to interest expense. As of June 28, 2015, the swaps were highly effective cash flow hedges with no ineffectiveness for the three and six month periods ended June 28, 2015.

The weighted average interest rate for the Credit Facility, including the impact of the previously mentioned swaps, were 2.0% and 1.7% for the three months ended June 28, 2015 and June 29, 2014, respectively, and 2.0% and 1.6% for the six months ended June 28, 2015 and June 29, 2014, respectively. Interest paid, including payments made or received under the swaps, was $1.3 million and $853,000 for the three months ended June 28, 2015 and June 29, 2014, respectively, and $2.6 million and $1.6 million for the six months ended June 28, 2015 and June 29, 2014, respectively. As of June 28, 2015, the portion of the $1.0 million interest rate swap liability that would be reclassified into earnings during the next twelve months as interest expense approximates $360,000.

5. Litigation

Litigation

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

Perrin v. Papa John s International, Inc. and Papa John s USA, Inc. is a conditionally certified collective and class action filed in August 2009 in the United States District Court, Eastern District of Missouri (the Court), alleging that delivery drivers were not properly reimbursed for mileage and expenses in accordance with the Fair Labor Standards Act (FLSA). Approximately 3,900 drivers out of a potential class size of 28,800 opted into the action. In late December 2013, the District Court granted a motion for class certification in five additional states, which added approximately 15,000 plaintiffs to the case. The trial, originally scheduled for August 2015, was stayed in June 2015, pending U.S. Supreme Court review of another relevant case regarding certification. After the stay was granted, the parties reached a settlement in principle subject to approval by the Court. The Company continues to deny any liability or wrongdoing in this matter. In accordance with this preliminary settlement agreement, the Company has recorded a pre-tax expense of $12.3 million for the quarter ended June 28, 2015 under the provisions of ASC 450, *Contingencies*. This amount is separately reported as Legal settlement expense in the condensed consolidated statements of income.

6. Segment Information

We have five reportable segments: domestic Company-owned restaurants, domestic commissaries, North America franchising, international operations, and all other units. The domestic Company-owned restaurant segment consists of the operations of all domestic (domestic is defined as contiguous United States) Company-owned restaurants and derives its revenues principally from retail sales of pizza and side items, such as breadsticks, cheesesticks, chicken poppers and wings, dessert items and canned or bottled beverages. The domestic commissary segment consists of the operations of our regional dough production and product distribution centers and derives its revenues principally from the sale and distribution of food and paper products to domestic Company-owned and franchised restaurants. The North America franchising segment consists of our franchise sales and support activities and derives its revenues from sales of franchise and development rights and collection of royalties from our franchisees located in the United States and Canada. The international operations segment principally consists of Company-owned restaurants in China and distribution sales to franchised Papa John s restaurants located in the United Kingdom, Mexico and China and our franchise sales and support activities, which derive revenues from sales of franchise and development rights and the collection of royalties

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from our international franchisees. International franchisees are defined as all franchise operations outside of the United States and Canada. All other business units that do not meet the quantitative thresholds for determining reportable segments, which are not operating segments, we refer to as our all other segment, which consists of operations that derive revenues from the sale, principally to Company-owned and franchised restaurants, of printing and promotional items, risk management services, and information systems and related services used in restaurant operations, including our point-of-sale system, online and other technology-based ordering platforms.

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

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

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Our segment information is as follows (in thousands):

	Three Months Ended June 28, 2015	Three Months Ended June 29, 2014	Six Months Ended June 28, 2015	Six Months Ended June 29, 2014
Revenues from external customers:				
Domestic Company-owned restaurants	$ 185,962	$ 170,000	$ 383,249	$ 348,193
Domestic commissaries	149,007	150,581	311,340	314,628
North America franchising	23,276	21,115	48,900	43,873
International	26,326	25,573	51,752	49,202
All others	14,420	13,595	36,034	26,345
Total revenues from external customers	$ 398,991	$ 380,864	$ 831,275	$ 782,241
Intersegment revenues:				
Domestic commissaries	$ 54,459	$ 51,592	$ 112,346	$ 106,313
North America franchising	671	583	1,342	1,187
International	75	90	150	158
All others	3,694	8,087	7,626	11,817
Total intersegment revenues	$ 58,899	$ 60,352	$ 121,464	$ 119,475
Income (loss) before income taxes:				
Domestic Company-owned restaurants	$ 14,617	$ 10,651	$ 33,097	$ 23,936
Domestic commissaries	10,702	6,846	22,502	17,277
North America franchising	20,054	17,882	42,373	37,366
International	2,279	1,903	3,623	2,635
All others	(117)	(442)	326	148
Unallocated corporate expenses (1)	(29,949)	(10,702)	(47,154)	(23,163)
Elimination of intersegment losses (profits)	(55)	98	(800)	(553)
Total income before income taxes	$ 17,531	$ 26,236	$ 53,967	$ 57,646
Property and equipment:				
Domestic Company-owned restaurants	$ 211,511			
Domestic commissaries	109,200			
International	27,287			
All others	48,471			
Unallocated corporate assets	172,713			
Accumulated depreciation and amortization	(353,974)			
Net property and equipment	$ 215,208			

(1) Includes a $12.3 million legal settlement expense in the three- and six-month periods of 2015. See Note 5 for additional information.

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

Overview

Papa John s International, Inc. (referred to as the Company, Papa John s or in the first person notations of we, us and our) began operations 1984. At June 28, 2015, there were 4,734 Papa John s restaurants (741 Company-owned and 3,993 franchised) operating in all 50 states and in 38 international countries and territories. Our revenues are principally derived from retail sales of pizza and other food and beverage products to the general public by Company-owned restaurants, franchise royalties, sales of franchise and development rights, sales to franchisees of food and paper products, printing and promotional items, risk management services, and information systems and related services used in their operations.

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

Restaurant Progression

	Three Months Ended		Six Months Ended	
	June 28, 2015	June 29, 2014	June 28, 2015	June 29, 2014
North America Company-owned:				
Beginning of period	691	666	686	665
Opened	1	2	4	4
Closed		(1)		(2)
Acquired from franchisees	1	5	3	5
End of period	693	672	693	672
International Company-owned:				
Beginning of period	48	58	49	58
Opened		1		1
Closed			(1)	
End of period	48	59	48	59
North America franchised:				
Beginning of period	2,650	2,615	2,654	2,621
Opened	19	28	37	49
Closed	(15)	(24)	(35)	(51)
Sold to Company	(1)	(5)	(3)	(5)
End of period	2,653	2,614	2,653	2,614
International franchised:				
Beginning of period	1,310	1,101	1,274	1,084
Opened	42	46	92	69
Closed	(12)	(5)	(26)	(11)
End of period	1,340	1,142	1,340	1,142

Total restaurants - end of period	4,734	4,487	4,734	4,487

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Item Impacting Comparability; Non-GAAP Measure

The following table reconciles our GAAP financial results to the adjusted (non-GAAP) financial results, excluding the legal settlement expense for *Perrin v. Papa John s International, Inc. and Papa John s USA, Inc.*, a conditionally certified collective and class action, for the three and six months ended June 28, 2015. We present these non-GAAP measures because we believe the legal settlement impacts the comparability of our results of operations. For additional information about the legal settlement, see Note 5 of Notes to Condensed Consolidated Financial Statements.

(In thousands, except per share amounts)	Three Months Ended June 28, 2015	Three Months Ended June 29, 2014	Six Months Ended June 28, 2015	Six Months Ended June 29, 2014
Income before income taxes, as reported	$ 17,531	$ 26,236	$ 53,967	$ 57,646
Legal settlement expense	12,278		12,278	
Income before income taxes, as adjusted	$ 29,809	$ 26,236	$ 66,245	$ 57,646
Net income, as reported	$ 10,780	$ 16,748	$ 33,016	$ 36,059
Legal settlement expense	7,986		7,986	
Net income, as adjusted	$ 18,766	$ 16,748	$ 41,002	$ 36,059
Diluted earnings per share, as reported	$ 0.27	$ 0.40	$ 0.82	$ 0.85
Legal settlement expense	0.20		0.20	
Diluted earnings per share, as adjusted	$ 0.47	$ 0.40	$ 1.02	$ 0.85

The non-GAAP results shown above and within this document, which exclude the legal settlement, should not be construed as a substitute for or a better indicator of the Company s performance than the Company s GAAP results. Management believes presenting certain financial information without the legal settlement is important for purposes of comparison to prior year results and analyzing each segment s operating results. In addition, management uses this metric to evaluate the Company s underlying operating performance and to analyze trends.

FOCUS System

As of June 28, 2015, we have implemented our new, proprietary point-of-sale system (FOCUS) in our domestic restaurants. FOCUS had the following impact on our condensed consolidated statements of income for the three and six months ended June 28, 2015 and June 29, 2014 (in thousands):

	Three Months Ended June 28, 2015	Three Months Ended June 29, 2014	Six Months Ended June 28, 2015	Six Months Ended June 29, 2014
Franchise royalties (a)	$ (737)	$	$ (1,307)	$
Other sales (b)	1,268	123	9,808	135
Other operating expenses (c)	(1,374)	(462)	(9,903)	(651)
Depreciation and amortization (d)	(1,239)	(529)	(2,476)	(579)

Net decrease in income before income taxes	$	(2,082)	$	(868)	$	(3,878)	$	(1,095)
Diluted earnings per common share	$	(0.04)	$	(0.01)	$	(0.06)	$	(0.02)

(a) Royalty incentive program tied to franchise rollout of FOCUS.

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(b) Represents revenues for equipment installed at domestic franchised restaurants.

(c) Includes cost of sales associated with equipment installed at franchised restaurants and other costs to support the rollout of the program.

(d) Includes depreciation expense for both the capitalized software and for equipment installed at Company-owned restaurants, which are being depreciated over five to seven years, respectively.

Results of Operations

Summary of Operating Results - Segment Review

Discussion of Revenues

Consolidated revenues were $399.0 million for the three months ended June 28, 2015, an increase of $18.1 million, or 4.8%, over the corresponding 2014 period. For the six months ended June 28, 2015, total revenues were $831.3 million, an increase of $49.0 million, or 6.3%, over the corresponding 2014 period. The increases in revenues for the three and six months ended June 28, 2015, were primarily due to the following:

- Domestic Company-owned restaurant sales increased $16.0 million, or 9.4%, and $35.1 million, or 10.1%, for the three and six months ended June 28, 2015, respectively, primarily due to increases of 7.4% and 7.7% in comparable sales and increases of 2.8% and 3.0% in equivalent units during the three and six months ended June 28, 2015, respectively. Comparable sales represents the change in year-over-year sales for the same base of restaurants for the same fiscal periods. Equivalent units represents the number of restaurants open at the beginning of a given period, adjusted for restaurants opened, closed, acquired or sold during the period on a weighted average basis.

- North America franchise royalty revenue increased approximately $2.1 million, or 10.0%, and $4.8 million or 11.1%, for the three and six months ended June 28, 2015, respectively, primarily due to increases of 4.8% and 5.4% in franchise comparable sales and due to reduced levels of royalty incentives.

- Domestic commissary sales decreased $1.6 million, or 1.0%, and $3.3 million, or 1.0%, for the three and six months ended June 28, 2015, respectively, as lower revenues associated with lower cheese prices were somewhat offset by increases in sales volumes.

- Other sales increased approximately $800,000, or 6.1%, and $9.7 million, or 36.8%, for the three and six months ended June 28, 2015, respectively. The increases were primarily due to FOCUS equipment sales to franchisees. See the FOCUS System section above for additional information.

- International royalties and franchise and development fees increased approximately $300,000, or 5.1%, and $1.0 million, or 8.6%, for the three and six months ended June 28, 2015, respectively, primarily due to increases in the number of franchised restaurants and increases in comparable sales of 7.0% and 7.5%, calculated on a constant dollar basis. The increases were somewhat offset by the negative impact of foreign currency exchange rates of approximately $700,000 and $1.3 million for the three- and six-month periods.

- International restaurant and commissary sales increased approximately $400,000, or 2.2%, and $1.5 million, or 4.1%, for the three and six months ended June 28, 2015, respectively, primarily due to an increase in commissary revenues from increases in units and higher comparable sales. This increase was partially offset by lower sales at China Company-owned restaurants due to the disposition of eleven restaurants in 2014. Additionally, sales were negatively impacted $1.3 million and $2.5 million for the three- and six month periods, respectively, by foreign currency exchange rates.

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Discussion of Operating Results

Second quarter 2015 income before income taxes was $17.5 million compared to $26.2 million in the prior year comparable period. Excluding the previously discussed legal settlement, income before income taxes was $29.8 million for the second quarter of 2015, or an increase of 13.6%. Income before income taxes was $54.0 million for the six months ended June 28, 2015, compared to $57.6 million for the prior year comparable period. Excluding the previously discussed legal settlement, income before income taxes was $66.2 million for the six months ended June 29, 2015, or an increase of 14.9%. Income before income taxes is summarized in the following table on a reporting segment basis. Alongside the GAAP income before income taxes data, we have included adjusted income before income taxes to exclude the legal settlement expense. We believe this non-GAAP measure is important for purposes of comparing to prior year results.

		Three Months Ended			
(In thousands)	**As Reported June 28, 2015**	**Legal Settlement Expense**	**Adjusted June 28, 2015**	**June 29, 2014**	**Adjusted Increase (Decrease)**
Domestic company-owned restaurants	$ 14,617	$	$ 14,617	$ 10,651	$ 3,966
Domestic commissaries	10,702		10,702	6,846	3,856
North America franchising	20,054		20,054	17,882	2,172
International	2,279		2,279	1,903	376
All others	(117)		(117)	(442)	325
Unallocated corporate expenses	(29,949)	12,278	(17,671)	(10,702)	(6,969)
Elimination of intersegment losses (profits)	(55)		(55)	98	(153)
Total income before income taxes (a)	$ 17,531	$ 12,278	$ 29,809	$ 26,236	$ 3,573

		Six Months Ended			
(In thousands)	**As Reported June 28, 2015**	**Legal Settlement Expense**	**Adjusted June 28, 2015**	**June 29, 2014**	**Adjusted Increase (Decrease)**
Domestic company-owned restaurants	$ 33,097	$	$ 33,097	$ 23,936	$ 9,161
Domestic commissaries	22,502		22,502	17,277	5,225
North America franchising	42,373		42,373	37,366	5,007
International	3,623		3,623	2,635	988
All others	326		326	148	178
Unallocated corporate expenses	(47,154)	12,278	(34,876)	(23,163)	(11,713)
Elimination of intersegment losses (profits)	(800)		(800)	(553)	(247)
Total income before income taxes (a)	$ 53,967	$ 12,278	$ 66,245	$ 57,646	$ 8,599

(a) Includes FOCUS system costs of approximately $2.1 million and $868,000 for the three months ended June 28, 2015 and June 29, 2014, respectively, and approximately $3.9 million and $1.1 million for the six months ended June 28, 2015 and June 29, 2014, respectively. See the Focus System section above for additional information.

The increases of $3.6 million, or 13.6%, and $8.6 million, or 14.9%, excluding the legal settlement, for the three- and six-month periods in 2015, respectively, were primarily due to the following:

- **Domestic Company-owned Restaurant Segment.** Domestic Company-owned restaurants income before income taxes increased $4.0 million and $9.2 million for the three and six months ended June 28, 2015, respectively, compared to the corresponding prior year periods. The increases were primarily due to higher profits from the 7.4% and 7.7% increases in comparable sales and lower commodity costs. The market price for cheese averaged $1.63 and $1.58 per pound for the three- and six-month periods in 2015, compared to $2.13 and $2.17 per pound in the prior year comparable periods. This was slightly offset by higher depreciation expense associated with FOCUS equipment of approximately $400,000 and $900,000 for the three- and six-month periods.

- **Domestic Commissary Segment.** Domestic commissaries income before income taxes increased approximately $3.9 million and $5.2 million for the three and six months ended June 28, 2015,

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respectively, compared to the corresponding prior year periods primarily due to higher margins and incremental profits from higher restaurant volumes.

- **North America Franchising Segment.** North America Franchising income before income taxes increased $2.2 million and $5.0 million for the three and six months ended June 28, 2015, respectively, compared to the corresponding prior year periods. The increases were primarily due to higher royalties from the 4.8% and 5.4% comparable sales increases and reduced levels of royalty incentives.

- **International Segment.** Income before income taxes increased approximately $400,000 and $1.0 million for the three and six months ended June 28, 2015, respectively, compared to the corresponding prior year periods. The increases were primarily due to increases in units and comparable sales increases of 6.8% and 7.2%, which resulted in both higher royalties and increases of approximately $300,000 and $600,000 in United Kingdom profits for the three- and six-month periods, respectively. These increases were somewhat offset by the impact of negative foreign currency exchange rates of approximately $500,000 and $1.0 million for the three- and six-month periods, respectively.

- **All Others Segment.** The All Others reporting segment income before income taxes, which primarily includes our online and mobile ordering business and our wholly-owned print and promotions subsidiary, Preferred Marketing Solutions, increased approximately $300,000 and $200,000 for the three and six months ended June 28, 2015, respectively, compared to the corresponding prior year periods. The increases were primarily due to improvements in our online and mobile ordering business due to higher online volumes. The increase for the six-month period was somewhat offset by reduced operating results at Preferred Marketing Solutions, primarily associated with an increased number of discounted direct mail campaigns.

- **Unallocated Corporate Expenses.** Unallocated corporate expenses increased approximately $7.0 million and $11.7 million for the three and six months ended June 28, 2015, respectively, compared to the corresponding 2014 periods. The components of unallocated corporate expenses were as follows (in thousands):

	Three Months Ended			Six Months Ended		
	June 28, 2015	June 29, 2014	Increase (Decrease)	June 28, 2015	June 29, 2014	Increase (Decrease)
General and administrative (a)	$ 14,896	$ 8,146	$ 6,750	$ 28,850	$ 18,475	$ 10,375
Net interest expense (income) (b)	1,230	781	449	2,477	1,386	1,091
Depreciation	2,138	1,839	299	4,219	3,614	605
Other (income) expense (c)	(1,402)	(502)	(900)	(2,163)	(895)	(1,268)
FOCUS system costs (d)	809	438	371	1,493	583	910
Total unallocated corporate expenses	$ 17,671	$ 10,702	$ 6,969	$ 34,876	$ 23,163	$ 11,713

(a) The increases in unallocated general and administrative costs for the three- and six-month periods in 2015 were primarily due to higher management incentive compensation, tied to higher projected annual operating results, higher salaries and benefits, including health insurance, and increased legal costs. The second quarter of 2015 had $1.4 million of higher expenses due to a shift in the timing of the annual operators conference (shift in timing from the first quarter in 2014 to the second quarter in 2015). For the six-month period, there was not a significant change in the cost of the operators conference.

(b) The increase in net interest expense (income) was primarily due to a higher average outstanding debt balance with a higher effective interest rate.

(c) Other (income) expense is favorable primarily due to lower provisions for uncollectible accounts and notes receivable in the three- and six-month periods of 2015.

(d) Includes depreciation expense for capitalized FOCUS software development costs and other costs to support the rollout of the program.

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Diluted earnings per share were $0.27 ($0.47, excluding the $0.20 legal settlement), for the three months ended June 28, 2015, compared to $0.40 in the corresponding prior year period. Diluted earnings per share were $0.82 ($1.02, excluding the $0.20 legal settlement), for the six months ended June 28, 2015, compared to $0.85 in the corresponding prior year period. Diluted earnings per share increased $0.02 and $0.05 for the three- and six-month periods, respectively, due to reductions in shares outstanding (a 4.2% reduction for the three-month period and a 4.6% reduction for the six-month period). Additionally, FOCUS system costs reduced diluted earnings per share by $0.04 and $0.01 for the three months ended June 28, 2015 and June 29, 2014, respectively, and $0.06 and $0.02 for the six months ended June 28, 2015 and June 29, 2014, respectively.

Review of Consolidated Operating Results

Revenues. Domestic Company-owned restaurant sales were $186.0 million for the three months ended June 28, 2015, compared to $170.0 million for the same period in 2014, and $383.2 million for the six months ended June 28, 2015, compared to $348.2 million for the same period in 2014. The increases of $16.0 million and $35.1 million were primarily due to the previously mentioned increases of 7.4% and 7.7% in comparable sales and increases of 2.8% and 3.0% in equivalent units during the three and six months ended June 28, 2015, respectively.

North America franchise royalties were $23.1 million and $48.4 million for the three and six months ended June 28, 2015, respectively, representing increases of approximately $2.1 million, or 10.0%, and $4.8 million, or 11.1%, from the comparable periods in the prior year. The increases in royalties were primarily due to increases in North America franchise sales and reduced levels of royalty incentives in 2015. North America franchise sales increased 5.3% to $523.2 million for the three months ended June 29, 2015, compared to $496.7 million for the same period in 2014, and increased 5.8% to $1.09 billion for the six months ended June 28, 2015, compared to $1.03 billion for the same period in 2014. The increases were primarily due to the 4.8% and 5.4% increases in comparable sales for the three- and six-month periods, respectively. Franchise restaurant sales are not included in Company revenues; however, our domestic royalty revenue is derived from these sales.

Average weekly sales for comparable units include restaurants that were open throughout the periods presented below. The comparable sales base for domestic Company-owned and North America franchised restaurants, respectively, includes restaurants acquired by the Company or divested to franchisees during the previous twelve months. Average weekly sales for non-comparable units include restaurants that were not open throughout the periods presented below and include non-traditional sites. Average weekly sales for non-traditional units not subject to continuous operations are calculated based upon actual days open.

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The comparable sales base and average weekly sales for 2015 and 2014 for domestic Company-owned and North America franchised restaurants consisted of the following:

	Three Months Ended			
	June 28, 2015		June 29, 2014	
	Company	Franchised	Company	Franchised
Total domestic units (end of period)	693	2,653	672	2,614
Equivalent units	682	2,545	664	2,518
Comparable sales base units	665	2,347	643	2,295
Comparable sales base percentage	97.5%	92.2%	96.9%	91.1%
Average weekly sales - comparable units	$ 21,164	$ 16,289	$ 19,923	$ 15,654
Average weekly sales - total non-comparable units (a)	$ 13,448	$ 10,210	$ 13,084	$ 10,226
Average weekly sales - all units	$ 20,977	$ 15,815	$ 19,710	$ 15,173

	Six Months Ended			
	June 28, 2015		June 29, 2014	
	Company	Franchised	Company	Franchised
Total domestic units (end of period)	693	2,653	672	2,614
Equivalent units	680	2,544	660	2,522
Comparable sales base units	664	2,344	641	2,298
Comparable sales base percentage	97.6%	92.1%	97.1%	91.1%
Average weekly sales - comparable units	$ 21,866	$ 16,926	$ 20,503	$ 16,166
Average weekly sales - total non-comparable units (a)	$ 13,941	$ 10,428	$ 13,133	$ 10,426
Average weekly sales - all units	$ 21,681	$ 16,417	$ 20,289	$ 15,656

(a) Includes 121 traditional and 213 non-traditional units as of June 28, 2015 and 157 traditional and 191 non-traditional units as of June 29, 2014.

Domestic commissary sales decreased 1.0% to $149.0 million for the three months ended June 28, 2015, from $150.6 million in the comparable 2014 period and decreased 1.0% to $311.3 million for the six months ended June 28, 2015, from $314.6 million in the comparable 2014 period. The decreases were primarily due to decreases in cheese prices, which were somewhat offset by increases in sales volumes. PJ Food Service (PJFS) pricing for cheese is based on a fixed dollar markup; when cheese prices decrease, revenues will decrease with no overall impact on the related dollar margin.

Other sales increased approximately $800,000, or 6.1%, and $9.7 million, or 36.8%, for the three and six months ended June 28, 2015, respectively. The increases were primarily due to FOCUS equipment sales to franchisees. See the FOCUS System section above for additional information.

International royalties and franchise and development fees increased approximately $300,000, or 5.1%, for the three months ended June 28, 2015, and increased $1.0 million, or 8.6%, for the six months ended June 28, 2015, from the prior comparable periods. The increases were due to increases in units and comparable sales of 7.0% and 7.5%, calculated on a constant dollar basis, for the three- and six-month periods, respectively. The increases were somewhat offset by the negative impact of foreign currency exchange rates of approximately $700,000 and $1.3 million for the respective periods. International franchise sales were $150.3 million for the three months ended June 28, 2015, compared to $140.1 million for the same period in 2014, representing an increase of 7.3%. International franchise sales for the six months ended June 28, 2015 increased 8.0% to $292.8 million compared to $270.9 million for the same period in 2014. International franchise sales are not included in Company revenues; however, our international royalty revenue is derived from these sales.

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International restaurant and commissary sales increased approximately $400,000, or 2.2%, for the three months ended June 28, 2015, and increased $1.5 million, or 4.1%, for the six months ended June 28, 2015, from the prior comparable periods. The increases were primarily due to higher commissary revenues from increases in units and comparable sales. The increases were partially offset by lower sales to China Company-owned restaurants due to the disposition of eleven restaurants in 2014. Additionally, sales were negatively impacted $1.3 million and $2.5 million for the three- and six month periods, respectively, by foreign currency exchange rates.

Costs and expenses. The restaurant operating margin for domestic Company-owned units was 20.8% for the three months ended June 28, 2015, compared to 18.9% for the same period in 2014, and was 21.1% for the six months ended June 28, 2015, compared to 19.2% for the same period in 2014. The margins were comprised of the following changes for the three and six months ended June 28, 2015:

- Cost of sales were 1.4% and 1.3% lower for the three and six months ended June 28, 2015, as compared to the same periods in 2014, primarily due to lower commodity costs, primarily cheese.
- Salaries and benefits were 0.8% and 0.6% higher primarily due to higher bonuses paid to general managers.
- Advertising and related costs were 0.2% and 0.4% lower primarily due to lower discretionary spending and the benefit of higher sales.
- Occupancy costs and other restaurant operating costs were 1.0% and 0.8% lower primarily due to lower mileage reimbursement from lower gas prices.

Domestic commissary margin was 7.7% for the three months ended June 28, 2015, compared to 6.0% for the corresponding period in 2014, and 7.7% for the six months ended June 28, 2015, compared to 6.8% for the corresponding period in 2014 and consisted of the following differences:

- Cost of sales were 2.3% and 1.9% lower for the three and six months ended June 28, 2015 primarily due to lower cheese costs which have a fixed-dollar markup. As cheese prices are lower, food cost as a percentage of sales is lower.
- Salaries and benefits and other commissary operating expenses were 0.6% and 0.9% higher as a percentage of sales primarily due to lower PJFS revenues. As noted previously, PJFS revenues are lower due to lower cheese prices. Additionally, PJFS had higher overall delivery costs due to higher driver compensation costs that were somewhat offset by lower fuel costs.

Other operating expenses as a percentage of other sales were 94.6% and 95.1% for the three and six months ended June 28, 2015, respectively, compared to 97.2% and 93.6% in the prior comparable periods. The lower operating expenses for the three-month period were primarily due to the decreasing number of franchise FOCUS systems sales, and related operating expenses, as we finished the rollout. Overall, FOCUS systems sales have a low margin. The higher operating expenses for the six-month period were primarily due to the significant volume of franchise

FOCUS system sales and related operating expenses attributable to the first quarter of 2015. The six month results also reflect the impact of an increased number of direct mail campaigns offered to our domestic restaurants by Preferred Marketing Solutions.

International restaurant and commissary expenses as a percentage of sales were 82.6% for the second quarter of 2015 and approximated 82.4% in the second quarter of 2014. For the six months ended June 28, 2015, expenses were 82.2% as compared to 82.9% for the corresponding 2014 period. The decrease as a percentage of sales for the six-month period was primarily due to the benefit of higher commissary sales volumes and a higher commissary margin.

General and administrative (G&A) costs were $42.0 million, or 10.5%, of revenues for the three months ended June 28, 2015, compared to $33.6 million, or 8.8%, of revenues for the same period in 2014. G&A costs were $84.0 million, or 10.1%, of revenues for the six months ended June 28, 2015, compared to $70.5 million, or 9.0%, of revenues for the same period in 2014. The increases of $8.5 million and $13.4 million for the three- and six-month periods were primarily due to the following:

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- Corporate G&A costs increased primarily due to higher management incentive compensation, tied to higher projected annual operating results, higher salaries and benefits, including health insurance, and increased legal costs. The second quarter of 2015 also had $1.4 million of higher expenses due to a shift in the timing of our annual operators conference (shift in timing from the first quarter in 2014 to the second quarter in 2015). For the six-month period, there was not a significant change in the cost of our operators conference.

- Domestic Company-owned restaurant supervisor bonuses increased due to higher sales and higher operating profits.

- International G&A costs increased primarily due to incremental advertising spending to support our international franchise operations.

Other general expenses decreased approximately $1.0 million and $700,000 for the three and six months ended June 28, 2015, respectively, primarily due to lower provisions for uncollectible accounts and notes receivable.

Depreciation and amortization was $10.1 million (2.5% of revenues) for the three months ended June 28, 2015, compared to $9.9 million (2.6% of revenues) for the same 2014 period, and $20.2 million (2.4% of revenues) for the six months ended June 28, 2015, compared to $19.0 million (2.4% of revenues) for the 2014 period. This includes incremental depreciation from both FOCUS capitalized software costs and Company-owned restaurants equipment costs.

Legal settlement expense. This line item consists of $12.3 million of settlement costs in the three- and six-month periods of 2015 for a conditionally certified collective and class action alleging our delivery drivers were not properly reimbursed for mileage and expenses in accordance with the Fair Labor Standards Act (FLSA). For additional information, see Note 5 of Notes to Condensed Consolidated Financial Statements.

Net interest (expense) income. Net interest expense increased approximately $400,000 and $1.0 million for the three and six months ended June 28, 2015, respectively, primarily due to a higher average outstanding debt balance and higher effective interest rates.

Income tax expense. Our effective income tax rates were 28.9% and 32.0% for the three and six months ended June 28, 2015, respectively, representing decreases from the prior year comparable periods of 3.1% and 1.4% for the three- and six-month periods, respectively. The legal settlement reduced our income tax rates by approximately 2.5% and 0.5% for the three- and six-month periods, respectively. The rates for 2015 also include a higher benefit from various tax deductions and credits, including the U.S. federal manufacturing deduction.

Liquidity and Capital Resources

Our debt is comprised entirely of an unsecured revolving credit facility (Credit Facility) with a maturity date of October 31, 2019. Outstanding balances under this $400 million Credit Facility were $234.0 million as of June 28, 2015 and $230.5 million as of December 28, 2014.

The interest rate charged on outstanding balances is LIBOR plus 75 to 175 basis points. The commitment fee on the unused balance ranges from 15 to 25 basis points. The increment over LIBOR and the commitment fee are determined quarterly based upon the ratio of total indebtedness to earnings before interest, taxes, depreciation and amortization (EBITDA), as defined by the Credit Facility. The remaining availability under the Credit Facility, reduced for outstanding letters of credit, was approximately $147.2 million as of June 28, 2015.

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We use interest rate swaps to hedge against the effects of potential interest rate increases on borrowings under our Credit Facility. We currently have the following interest rate swaps as of June 28, 2015:

Effective Dates	**Debt Amount**	**Fixed Rates**
July 30, 2013 through April 30, 2018	$75 million	1.42%
December 30, 2014 through April 30, 2018	$50 million	1.36%

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

	Permitted Ratio	**Actual Ratio for the Quarter Ended June 28, 2015**
Leverage Ratio	Not to exceed 3.0 to 1.0	1.5 to 1.0
Interest Coverage Ratio	Not less than 3.5 to 1.0	4.7 to 1.0

Our leverage ratio is defined as outstanding debt divided by EBITDA for the most recent four fiscal quarters. Our interest coverage ratio is defined as the sum of consolidated EBITDA and consolidated rental expense for the most recent four fiscal quarters divided by the sum of consolidated interest expense and consolidated rental expense for the most recent four fiscal quarters. We were in compliance with all covenants as of June 28, 2015.

Cash flow provided by operating activities was $78.0 million for the six months ended June 28, 2015, compared to $54.6 million for the same period in 2014. The increase of approximately $23.4 million was primarily due to higher operating income and favorable changes in inventory and other working capital items. The prior year included higher inventory levels of equipment to support the rollout of FOCUS to our domestic franchised restaurants. The legal settlement does not currently impact cash provided by operating activities as it has not yet been paid. We expect the majority of the settlement payments to be made in the next twelve months.

Our free cash flow, a non-GAAP financial measure, for the six months ended June 28, 2015 and June 29, 2014 was as follows (in thousands):

	Six Months Ended			
	June 28, 2015		**June 29, 2014**	
Net cash provided by operating activities	$	77,982	$	54,565
Purchases of property and equipment (a)		(16,501)		(26,239)
Free cash flow (b)	$	61,481	$	28,326

(a) We require capital primarily for the development, acquisition, renovation and maintenance of restaurants, the development, renovation and maintenance of commissary facilities and equipment and the enhancement of corporate systems and facilities, including technological enhancements such as our FOCUS system. The decrease of approximately $9.7 million is primarily due to the prior year including FOCUS equipment costs for domestic Company-owned restaurants and higher levels of FOCUS software development costs.

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

We also require capital for share repurchases and the payment of cash dividends, which are funded by cash flow from operations and borrowings on our revolving credit facility. We repurchased $52.1 million and $63.3 million of common stock for the six months ended June 28, 2015 and June 29, 2014, respectively. Subsequent to June 28, 2015, through July 28, 2015, we repurchased an additional $8.4 million of common stock. As of July 28, 2015, approximately $69.0 million remained available for repurchase under our Board of Directors authorization.

We paid cash dividends of $11.1 million ($0.28 per common share) and $10.4 million ($0.25 per common share) for the six months ended June 28, 2015 and June 29, 2014, respectively. Subsequent to the second quarter, on July 30, 2015, our Board of Directors approved a 25% increase in the Company s dividend rate per common share, from $0.56 on an annual basis to $0.70 on an annual basis, and declared a third quarter dividend of $0.175 per common share (approximately $6.9 million based on current shareholders of record). The dividend will be paid on August 21, 2015 to shareholders of record as of the close of business on August 11, 2015. The declaration and payment of any future dividends will be at the discretion of our Board of Directors, subject to the Company s financial results, cash requirements, and other factors deemed relevant by our Board of Directors.

Forward-Looking Statements

Certain matters discussed in this report, including information within Management s Discussion and Analysis of Financial Condition and Results of Operations, constitute forward-looking statements within the meaning of the federal securities laws. Generally, the use of words such as expect, estimate, believe, anticipate, will, forecast, plan, project, or similar words identify forward-looking statements that we inten included within the safe harbor protections provided by the federal securities laws. Such forward-looking statements may relate to projections or guidance concerning business performance, revenue, earnings, contingent liabilities, resolution of litigation, commodity costs, profit margins, unit growth, capital expenditures, and other financial and operational measures. Such statements are not guarantees of future performance and involve certain risks, uncertainties and assumptions, which are difficult to predict and many of which are beyond our control. Therefore, actual outcomes and results may differ materially from those matters expressed or implied in such forward-looking statements. The risks, uncertainties and assumptions that are involved in our forward-looking statements include, but are not limited to:

- aggressive changes in pricing or other marketing or promotional strategies by competitors, which may adversely affect sales; and new product and concept developments by food industry competitors;
- changes in consumer preferences or consumer buying habits, including the impact of adverse general economic conditions;
- the impact that product recalls, food quality or safety issues, incidences of foodborne illness, food contamination and other general public health concerns, including potential epidemics, could have system-wide on our restaurants or our results;

- failure to maintain our brand strength and quality reputation and risks related to our better ingredients marketing strategy;

- the ability of the Company and its franchisees to meet planned growth targets and operate new and existing restaurants profitably;

- increases in or sustained high costs of food ingredients or other restaurant costs. This could include increased employee compensation, benefits, insurance, tax rates, regulatory compliance and similar costs, including increased costs resulting from federal health care legislation;

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- disruption of our supply chain or commissary operations which could be caused by our sole source of supply of cheese or limited source of suppliers for other key ingredients or more generally due to weather, drought, disease, geopolitical or other disruptions beyond our control;

- increased risks associated with our international operations, including economic and political conditions, instability in our international markets, fluctuations in currency exchange rates, and difficulty in meeting planned sales targets and new store growth. This could include our expansion into emerging or underpenetrated markets, such as China, where we have a Company-owned presence. Based on prior experience in underpenetrated markets, operating losses are likely to occur as the market is being established;

- the impact of changes in interest rates on the Company or our franchisees;

- the credit performance of our franchise loan programs;

- the impact of the resolution of current or future claims and litigation;

- current or proposed legislation impacting our business;

- failure to effectively execute succession planning, and our reliance on the multiple roles of our Founder, Chairman, and Chief Executive Officer, who also serves as our brand spokesperson;

- disruption of critical business or information technology systems, and risks associated with systems failures and data privacy and security breaches, including theft of Company, employee and customer information.

For a discussion of these and other risks that may cause actual results to differ from expectations, refer to Part I. Item 1A. Risk Factors in our Annual Report on Form 10-K for the year ended December 28, 2014, as well as subsequent filings. We undertake no obligation to update publicly any forward-looking statements, whether as a result of future events, new information or otherwise, except as required by law.

Item 3. Quantitative and Qualitative Disclosures About Market Risk

Interest Rate Risk

Our debt is comprised entirely of a revolving credit facility (Credit Facility) with outstanding balances of $234.0 million as of June 28, 2015 and $230.5 million as of December 28, 2014. On October 31, 2014, we amended our Credit Facility to increase the amount available from $300 million to $400 million and extend the maturity date from April 30, 2018 to October 31, 2019. The amendment also allows for an additional $100 million in borrowings. The interest rate charged on outstanding balances is LIBOR plus 75 to 175 basis points. The commitment fee on the unused balance ranges from 15 to 25 basis points.

We attempt to minimize interest risk exposure and to lower our overall long-term borrowing costs for changes in interest rates through the utilization of interest rate swaps, which are derivative financial instruments. Our swaps are entered into with financial institutions and have reset dates and critical terms that match those of the underlying debt. By using a derivative instrument to hedge exposures to changes in interest rates, we expose ourselves to credit risk. Credit risk is the failure of the counterparty to perform under the terms of the derivative contract. We minimize the credit risk by entering into transactions with high-quality counterparties whose credit rating is evaluated on a quarterly basis.

We currently have the following interest rate swaps outstanding as of June 28, 2015:

Effective Dates	**Debt Amount**	**Fixed Rates**
July 30, 2013 through April 30, 2018	$75 million	1.42%
December 30, 2014 through April 30, 2018	$50 million	1.36%

The effective interest rate on borrowings under the Credit Facility, including the impact of the interest rate swaps, was 1.8% as of June 28, 2015. An increase in the present interest rate of 100 basis points on the

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outstanding balance as of June 28, 2015, including the impact of the interest rate swaps, would increase interest expense by $1.1 million.

Foreign Currency Exchange Rate Risk

We currently do not enter into financial instruments to manage foreign currency exchange rates. Sales to customers and royalties outside the United States represent approximately 6% of our total revenues.

Commodity Price Risk

In the ordinary course of business, the food and paper products we purchase, including cheese (historically representing 35% to 40% of our food cost), are subject to seasonal fluctuations, weather, availability, demand and other factors that are beyond our control. We have pricing agreements with some of our vendors, including forward pricing agreements for a portion of our cheese purchases for our domestic Company-owned restaurants, which are accounted for as normal purchases; however, we still remain exposed to on-going commodity volatility.

The following table presents the actual average block price for cheese by quarter through the second quarter of 2015 and the projected average block price for cheese by quarter through 2015 (based on the July 28, 2015 Chicago Mercantile Exchange cheese futures market prices):

	2015 Projected Block Price	2014 Actual Block Price
Quarter 1	$ 1.538	$ 2.212
Quarter 2	1.630	2.131
Quarter 3	1.697	2.141
Quarter 4	1.710	1.991
Full Year	$ 1.644*	$ 2.119

* The full year estimate is based on futures prices and does not include the impact of forward pricing agreements for a portion of our cheese purchases for our domestic Company-owned restaurants.

Item 4. Controls and Procedures

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

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

PART II. OTHER INFORMATION

Item 1. Legal Proceedings

The Company is involved in a number of lawsuits, claims, investigations and proceedings, including the matter identified below, consisting of intellectual property, employment, consumer, commercial and other matters

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arising in the ordinary course of business. In accordance with Accounting Standards Codification 450, *Contingencies*, the Company has made accruals with respect to these matters, where appropriate, which are reflected in the Company s financial statements. We review these provisions at least quarterly and adjust these provisions to reflect the impact of negotiations, settlements, rulings, advice of legal counsel and other information and events pertaining to a particular case.

Perrin v. Papa John s International, Inc. and Papa John s USA, Inc. is a conditionally certified collective and class action filed in August 2009 in the United States District Court, Eastern District of Missouri (the Court), alleging that delivery drivers were not properly reimbursed for mileage and expenses in accordance with the Fair Labor Standards Act (FLSA). Approximately 3,900 drivers out of a potential class size of 28,800 opted into the action. In late December 2013, the District Court granted a motion for class certification in five additional states, which added approximately 15,000 plaintiffs to the case. The trial, originally scheduled for August 2015, was stayed in June 2015, pending U.S. Supreme Court review of another relevant case regarding certification. After the stay was granted, the parties reached a settlement in principle subject to approval by the Court. The Company continues to deny any liability or wrongdoing in this matter. In accordance with this preliminary settlement agreement, the Company has recorded a pre-tax expense of $12.3 million for the quarter ended June 28, 2015 under the provisions of ASC 450, *Contingencies*. This amount is separately reported as Legal settlement expense in the condensed consolidated statements of income.

Item 1A. Risk Factors

There have been no material changes in the risk factors previously disclosed in the Company s Annual Report on Form 10-K for the fiscal year ended December 28, 2014.

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

Our Board of Directors has authorized the repurchase of up to $1.325 billion of common stock under a share repurchase program that began on December 9, 1999 and expires on December 31, 2015. Through June 28, 2015, a total of 106.4 million shares with an aggregate cost of $1.2 billion and an average price of $11.72 per share have been repurchased under this program. Subsequent to June 28, 2015, through July 28, 2015, we acquired an additional 110,000 shares at an aggregate cost of $8.4 million. As of July 28, 2015, approximately $69.0 million remained available for repurchase of common stock under this authorization.

The following table summarizes our repurchases by fiscal period during the three months ended June 28, 2015 (in thousands, except per-share amounts):

	Total Number of Shares	Average Price Paid per	Total Number of Shares Purchased as Part of Publicly Announced	Maximum Dollar Value of Shares that May Yet Be Purchased Under the

Fiscal Period	Purchased	Share	Plans or Programs	Plans or Programs
03/30/2015 - 04/26/2015	123	$ 61.56	106,135	$ 97,163
04/27/2015 - 05/24/2015	139	$ 64.63	106,274	$ 88,173
05/25/2015 - 06/28/2015	154	$ 69.89	106,428	$ 77,391

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

During fiscal quarter ended June 28, 2015, the Company acquired approximately 2,000 shares of its common stock from employees to satisfy minimum tax withholding obligations that arose upon (i) vesting of restricted stock granted pursuant to approved plans and (ii) distribution of shares of common stock issued pursuant to deferred compensation obligations.

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Item 6. Exhibits

Exhibit Number	Description
31.1	Certification of Chief Executive Officer Pursuant to Exchange Act Rule 13a-15(e), As Adopted Pursuant to Section 302 of the Sarbanes-Oxley Act of 2002.
31.2	Certification of Chief Financial Officer Pursuant to Exchange Act Rule 13a-15(e), As Adopted Pursuant to Section 302 of the Sarbanes-Oxley Act of 2002.
32.1	Certification of Chief Executive Officer Pursuant to 18 U.S.C. Section 1350, As Adopted Pursuant to Section 906 of the Sarbanes-Oxley Act of 2002.
32.2	Certification of Chief Financial Officer Pursuant to 18 U.S.C. Section 1350, As Adopted Pursuant to Section 906 of the Sarbanes-Oxley Act of 2002.
101	Financial statements from the quarterly report on Form 10-Q of Papa John s International, Inc. for the quarter ended June 28, 2015, filed on August 4, 2015, formatted in XBRL: (i) the Condensed Consolidated Balance Sheets, (ii) the Condensed Consolidated Statements of Income, (iii) the Consolidated Statements of Comprehensive Income, (iv) the Consolidated Statements of Cash Flows and (v) the Notes to Condensed Consolidated Financial Statements.

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SIGNATURE

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

PAPA JOHN S INTERNATIONAL, INC.
(Registrant)

Date: August 4, 2015

/s/ Lance F. Tucker
Lance F. Tucker
Senior Vice President,
Chief Financial Officer,
Chief Administrative Officer and Treasurer