

DENNYS CORP  
Form 10-Q  
October 30, 2018

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 September 26, 2018

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 0-18051

DENNY'S CORPORATION

(Exact name of registrant as specified in its charter)

Delaware 13-3487402

(State or other jurisdiction of (I.R.S. Employer incorporation or organization Identification No.)

203 East Main Street

Spartanburg, South Carolina 29319-0001

(Address of principal executive offices)

(Zip Code)

(864) 597-8000

(Registrant's telephone number, including area code)

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

Yes  No

Indicate by check mark whether the registrant has submitted electronically every Interactive Data File required to be submitted pursuant to Rule 405 of Regulation S-T during the preceding 12 months (or for such shorter period that the registrant was required to submit such files).

Yes  No

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

Large accelerated filer  Accelerated filer  Non-accelerated filer  Smaller reporting company  Emerging growth company

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If an emerging growth company, indicate by check mark if the registrant has elected not to use the extended transition period for complying with any new or revised financial accounting standards provided pursuant to Section 13(a) of the Exchange Act. "

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

As of October 24, 2018, 62,587,274 shares of the registrant's common stock, par value \$0.01 per share, were outstanding.

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## PART I - FINANCIAL INFORMATION

## Item 1. Financial Statements

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

|   | September 26,<br>2018 | December 27,<br>2017 |
|---|-----------------------|----------------------|
|   | (In thousands)        |                      |
| Assets  |                       |                      |
| Current assets:   |                       |                      |
| Cash and cash equivalents   | \$ 1,871              | \$ 4,983             |
| Investments   | 1,709                 | —                    |
| Receivables, net  | 17,186                | 21,384               |
| Inventories   | 3,051                 | 3,134                |
| Assets held for sale  | 193                   | —                    |
| Prepaid and other current assets  | 10,495                | 11,788               |
| Total current assets  | 34,505                | 41,289               |
| Property, net of accumulated depreciation of \$248,062 and \$243,325, respectively  | 143,459               | 139,856              |
| Goodwill  | 39,843                | 38,269               |
| Intangible assets, net  | 59,907                | 57,109               |
| Deferred financing costs, net   | 2,487                 | 2,942                |
| Deferred income taxes   | 15,595                | 16,945               |
| Other noncurrent assets   | 32,962                | 27,372               |
| Total assets  | \$ 328,758            | \$ 323,782           |
| Liabilities   |                       |                      |
| Current liabilities:  |                       |                      |
| Current maturities of capital lease obligations   | \$ 3,282              | \$ 3,168             |
| Accounts payable  | 20,327                | 32,487               |
| Other current liabilities   | 53,911                | 59,246               |
| Total current liabilities   | 77,520                | 94,901               |
| Long-term liabilities:  |                       |                      |
| Long-term debt, less current maturities   | 278,000               | 259,000              |
| Capital lease obligations, less current maturities  | 27,305                | 27,054               |
| Liability for insurance claims, less current portion  | 12,025                | 12,236               |
| Other noncurrent liabilities  | 43,888                | 27,951               |
| Total long-term liabilities   | 361,218               | 326,241              |
| Total liabilities   | 438,738               | 421,142              |
| Commitments and contingencies   |                       |                      |
| Shareholders' equity (deficit)  |                       |                      |
| Common stock \$0.01 par value; shares authorized - 135,000; September 27, 2018: 108,493 shares issued and 62,905 shares outstanding; December 27, 2017: 107,740 shares issued and 64,589 shares outstanding | \$ 1,085              | \$ 1,077             |
| Paid-in capital   | 597,344               | 594,166              |
| Deficit   | (317,917 )            | (334,661 )           |

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|   |            |            |   |
|---|------------|------------|---|
| Accumulated other comprehensive income (loss), net of tax       | 2,541      | (2,316     | ) |
| Shareholders' equity before treasury stock                      | 283,053    | 258,266    |   |
| Treasury stock, at cost, 45,588 and 43,151 shares, respectively | (393,033   | ) (355,626 | ) |
| Total shareholders' deficit                                     | (109,980   | ) (97,360  | ) |
| Total liabilities and shareholders' deficit                     | \$ 328,758 | \$ 323,782 |   |

See accompanying notes

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

|  | Quarter Ended                            |                       | Three Quarters Ended  |                       |
|--|--|-----------------------|-----------------------|-----------------------|
|  | September 26,<br>2018                    | September 27,<br>2017 | September 26,<br>2018 | September 27,<br>2017 |
|  | (In thousands, except per share amounts) |                       |                       |                       |
| Revenue:   |  |                       |                       |                       |
| Company restaurant sales                         | \$103,609                                | \$ 97,915             | \$307,543             | \$ 290,049            |
| Franchise and license revenue                    | 54,414                                   | 34,469                | 163,087               | 103,621               |
| Total operating revenue                          | 158,023                                  | 132,384               | 470,630               | 393,670               |
| Costs of company restaurant sales:               |  |                       |                       |                       |
| Product costs                                    | 25,303                                   | 24,896                | 75,292                | 72,798                |
| Payroll and benefits                             | 41,041                                   | 37,332                | 123,332               | 113,221               |
| Occupancy  | 6,083                                    | 5,054                 | 17,165                | 15,291                |
| Other operating expenses                         | 15,419                                   | 14,040                | 45,490                | 39,544                |
| Total costs of company restaurant sales          | 87,846                                   | 81,322                | 261,279               | 240,854               |
| Costs of franchise and license revenue           | 28,174                                   | 9,493                 | 85,779                | 29,483                |
| General and administrative expenses              | 15,981                                   | 16,446                | 48,138                | 50,536                |
| Depreciation and amortization                    | 6,760                                    | 5,958                 | 19,965                | 17,493                |
| Operating (gains), losses and other charges, net | 793                                      | 630                   | 1,615                 | 3,459                 |
| Total operating costs and expenses, net          | 139,554                                  | 113,849               | 416,776               | 341,825               |
| Operating income                                 | 18,469                                   | 18,535                | 53,854                | 51,845                |
| Interest expense, net                            | 5,314                                    | 4,067                 | 15,324                | 11,348                |
| Other nonoperating income, net                   | (460)                                    | (286)                 | (877)                 | (1,053)               |
| Net income before income taxes                   | 13,615                                   | 14,754                | 39,407                | 41,550                |
| Provision for income taxes                       | 2,810                                    | 5,429                 | 7,217                 | 15,103                |
| Net income                                       | \$10,805                                 | \$ 9,325              | \$32,190              | \$ 26,447             |
| Basic net income per share                       | \$0.17                                   | \$ 0.14               | \$0.50                | \$ 0.38               |
| Diluted net income per share                     | \$0.16                                   | \$ 0.13               | \$0.49                | \$ 0.37               |
| Basic weighted average shares outstanding        | 63,246                                   | 66,873                | 63,774                | 69,095                |
| Diluted weighted average shares outstanding      | 65,522                                   | 69,210                | 66,122                | 71,377                |

See accompanying notes

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

|  | Quarter Ended  |                | Three Quarters Ended |                |
|--|----------------|----------------|----------------------|----------------|
|  | September 2018 | September 2017 | September 2018       | September 2017 |
|  | (In thousands) |                |                      |                |
| Net income   | \$10,805       | \$ 9,325       | \$32,190             | \$ 26,447      |
| Other comprehensive income, net of tax:  |                |                |                      |                |
| Minimum pension liability adjustment, net of tax of \$7, \$9, \$20 and \$27, respectively                                      | 21             | 14             | 64                   | 42             |
| Recognition of unrealized gain (loss) on hedge transactions, net of tax of \$1,583, \$133, \$1,673 and \$(1,249), respectively | 4,537          | 209            | 4,793                | (1,958 )       |
| Other comprehensive income (loss)  | 4,558          | 223            | 4,857                | (1,916 )       |
| Total comprehensive income   | \$15,363       | \$ 9,548       | \$37,047             | \$ 24,531      |

See accompanying notes

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

|   | Common Stock   |          | Treasury Stock |             | Paid-in<br>Capital | Deficit     | Accumulated<br>Other<br>Comprehensive<br>Income<br>(Loss), Net | Total<br>Shareholders'<br>Deficit |
|---|----------------|----------|----------------|-------------|--------------------|-------------|--|-----------------------------------|
|   | Shares         | Amount   | Shares         | Amount      |                    |             |  |                                   |
|   | (In thousands) |          |                |             |                    |             |  |                                   |
| Balance, December 27,<br>2017                                   | 107,740        | \$ 1,077 | (43,151)       | \$(355,626) | \$594,166          | \$(334,661) | \$ (2,316 )  | \$(97,360 )                       |
| Cumulative effect<br>adjustment                                 | —              | —        | —              | —           | —                  | (15,446 )   | —  | (15,446 )                         |
| Net income  | —              | —        | —              | —           | —                  | 32,190      | —  | 32,190                            |
| Other comprehensive<br>income                                   | —              | —        | —              | —           | —                  | —           | 4,857  | 4,857                             |
| Share-based compensation<br>on equity classified<br>awards, net | —              | —        | —              | —           | 2,128              | —           | —  | 2,128                             |
| Purchase of treasury stock                                      | —              | —        | (2,437 )       | \$(37,407 ) | —                  | —           | —  | \$(37,407 )                       |
| Issuance of common stock<br>for share-based<br>compensation     | 447            | 5        | —              | —           | (5 )               | —           | —  | —                                 |
| Exercise of common stock<br>options                             | 306            | 3        | —              | —           | 1,055              | —           | —  | 1,058                             |
| Balance, September 26,<br>2018                                  | 108,493        | \$ 1,085 | (45,588)       | \$(393,033) | \$597,344          | \$(317,917) | \$ 2,541   | \$(109,980 )                      |

See accompanying notes



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

|   | Three Quarters Ended<br>September 26, 2018<br>(In thousands) | September 27, 2017 |
|---|--|--------------------|
| Cash flows from operating activities:   |  |                    |
| Net income  | \$ 32,190  | \$ 26,447          |
| Adjustments to reconcile net income to cash flows provided by operating activities: |  |                    |
| Depreciation and amortization   | 19,965   | 17,493             |
| Operating (gains), losses and other charges, net                                    | 1,615  | 3,459              |
| Amortization of deferred financing costs  | 455  | 446                |
| (Gain) loss on early extinguishments of debt and leases                             | (159 )   | 68                 |
| Deferred income tax expense   | 5,044  | 9,936              |
| Share-based compensation  | 3,661  | 6,546              |
| Changes in assets and liabilities:  |  |                    |
| Decrease (increase) in assets:  |  |                    |
| Receivables   | 3,582  | 3,279              |
| Inventories   | 83   | (55 )              |
| Other current assets  | 1,292  | 834                |
| Other assets  | (565 )   | (5,068 )           |
| Increase (decrease) in liabilities:   |  |                    |
| Accounts payable  | (11,948 )  | (5,121 )           |
| Accrued salaries and vacations  | (858 )   | (9,094 )           |
| Accrued taxes   | 1,974  | 1,474              |
| Other accrued liabilities   | (7,733 )   | (4,834 )           |
| Other noncurrent liabilities  | (2,339 )   | (2,285 )           |
| Net cash flows provided by operating activities                                     | 46,259   | 43,525             |
| Cash flows from investing activities:   |  |                    |
| Capital expenditures  | (17,294 )  | (13,558 )          |
|   | (10,416 )  | (10,043 )          |

|  |          |   |          |   |
|--|----------|---|----------|---|
| Acquisition of<br>restaurants and real<br>estate       |          |   |          |   |
| Proceeds from<br>disposition of property               | 969      |   | 2,318    |   |
| Investment purchases                                   | (1,709   | ) | —        |   |
| Collections on notes<br>receivable                     | 2,478    |   | 3,773    |   |
| Issuance of notes<br>receivable                        | (2,525   | ) | (2,278   | ) |
| Net cash flows used in<br>investing activities         | (28,497  | ) | (19,788  | ) |
| Cash flows from<br>financing activities:               |          |   |          |   |
| Revolver borrowings                                    | 91,000   |   | 105,900  |   |
| Revolver payments                                      | (72,000  | ) | (62,600  | ) |
| Long-term debt<br>payments                             | (2,429   | ) | (2,467   | ) |
| Proceeds from exercise<br>of stock options             | 1,058    |   | 173      |   |
| Tax withholding on<br>share-based payments             | (1,714   | ) | —        |   |
| Purchase of treasury<br>stock                          | (37,108  | ) | (65,951  | ) |
| Net bank overdrafts                                    | 319      |   | 279      |   |
| Net cash flows used in<br>financing activities         | (20,874  | ) | (24,666  | ) |
| Decrease in cash and<br>cash equivalents               | (3,112   | ) | (929     | ) |
| Cash and cash<br>equivalents at beginning<br>of period | 4,983    |   | 2,592    |   |
| Cash and cash<br>equivalents at end of<br>period       | \$ 1,871 |   | \$ 1,663 |   |

See accompanying notes

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

Note 1. Introduction and Basis of Presentation

Denny's Corporation, or Denny's or the Company, is one of America's largest full-service restaurant chains based on number of restaurants. At September 26, 2018, the Denny's brand consisted of 1,715 restaurants, 1,534 of which were franchised/licensed restaurants and 181 of which were company operated.

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

These interim condensed consolidated financial statements should be read in conjunction with our consolidated financial statements and notes thereto for the year ended December 27, 2017 and the related Management's Discussion and Analysis of Financial Condition and Results of Operations, both of which are contained in our Annual Report on Form 10-K for the fiscal year ended December 27, 2017. The results of operations for the interim periods presented are not necessarily indicative of the results for the entire fiscal year ending December 26, 2018.

Note 2. Summary of Significant Accounting Policies

Newly Adopted Accounting Standards

Effective December 28, 2017, the first day of fiscal 2018, we adopted Accounting Standards Update ("ASU") 2014-09, "Revenue from Contracts with Customers (Topic 606)" and all subsequent ASUs that modified Topic 606. The new guidance clarifies the principles used to recognize revenue for all entities and requires a company to recognize revenue when it transfers goods or services to a customer in an amount that reflects the consideration to which a company expects to be entitled. We elected to apply the modified retrospective method of adoption to those contracts which were not completed as of December 28, 2017. In doing so, we applied the practical expedient to aggregate all contract modifications that occurred before December 28, 2017 in determining the satisfied and unsatisfied performance obligations, the transaction price and the allocation of the transaction price to the satisfied and unsatisfied performance obligations. Results for reporting periods beginning after December 28, 2017 are presented under Topic 606. Prior period amounts are not adjusted and continue to be reported in accordance with our historical accounting under Topic 605 "Revenue Recognition." Our transition to Topic 606 represents a change in accounting principle. See Note 3 for further information about our transition to Topic 606 and the newly required disclosures.

Effective December 28, 2017, we adopted ASU 2016-01, "Financial Instruments—Overall (Subtopic 825-10): Recognition and Measurement of Financial Assets and Financial Liabilities". The new guidance requires equity investments (except those accounted for under the equity method of accounting, or those that result in consolidation of the investee) to be measured at fair value with changes in fair value recognized in net income, requires public business entities to use the exit price notion when measuring the fair value of financial instruments for disclosure purposes, requires separate presentation of financial assets and financial liabilities by measurement category and form of

financial asset, and eliminates the requirement for public business entities to disclose the method(s) and significant assumptions used to estimate the fair value that is required to be disclosed for financial instruments measured at amortized cost. The adoption of this guidance did not have any impact on our Consolidated Financial Statements.

Effective December 28, 2017, we adopted ASU 2017-07, “Compensation—Retirement Benefits (Topic 715): Improving the Presentation of Net Periodic Pension Cost and Net Periodic Postretirement Benefit Cost”. The new guidance requires an entity to report the service cost component in the same line on the income statement as other compensation costs arising from services rendered by the pertinent employees during the period. The other components of net benefit cost are required to be presented in the income statement separately from the service cost component and outside the subtotal of income from operations, if one is presented. If a separate line item is not used, the line item used in the income statement must be disclosed. The adoption of this guidance did not have any impact on our Consolidated Financial Statements.

Effective December 28, 2017, we early adopted ASU 2018-02, “Income Statement—Reporting Comprehensive Income (Topic 220): Reclassification of Certain Tax Effects from Accumulated Other Comprehensive Income”. The new guidance allows a reclassification from accumulated other comprehensive income to retained earnings for stranded tax effects resulting from the Tax Cuts and Jobs Act of 2017 (the “Tax Act”) and requires certain disclosures about stranded tax effects. Due to the immateriality of the stranded tax effects resulting from the implementation of the Tax Act, we have elected not to reclassify these amounts from accumulated other comprehensive income to retained earnings. Therefore the adoption of this guidance did not have any impact on our Consolidated Financial Statements.

Effective December 28, 2017, we early adopted ASU 2017-12, “Derivatives and Hedging (Topic 815): Targeted Improvements to Accounting for Hedging Activities”. The new update better aligns an entity’s risk management activities and financial reporting for hedging relationships, simplifies the hedge accounting requirements, and improves the disclosures of hedging arrangements. The amended presentation and disclosure guidance has been applied on a prospective basis. The adoption of this guidance did not have any impact on our Consolidated Financial Statements.

Effective September 26, 2018, we early adopted ASU 2018-13, “Fair Value Measurement (Topic 820): Disclosure Framework—Changes to the Disclosure Requirements for Fair Value Measurement”, which modifies the disclosure requirements on fair value measurements. The adoption of this guidance did not have any impact on our disclosures.

Effective September 26, 2018, we early adopted ASU 2018-14, “Compensation—Retirement Benefits—Defined Benefit Plans—General (Topic 715-20): Disclosure Framework—Changes to the Disclosure Requirements for Defined Benefit Plans”, which modifies the disclosure requirements for defined benefit pension plans and other postretirement plans. The adoption of this guidance will have an immaterial impact on our annual disclosures.

Effective September 26, 2018, we early adopted ASU 2018-15, “Intangibles—Goodwill and Other—Internal-Use Software (Subtopic 350-40): Customer’s Accounting for Implementation Costs Incurred in a Cloud Computing Arrangement That Is a Service Contract (a consensus of the FASB Emerging Issues Task Force)”, which aligns the requirements for capitalizing implementation costs incurred in a hosting arrangement that is a service contract with the requirements for capitalizing implementation costs incurred to develop or obtain internal-use software. The guidance was adopted on a prospective basis and did not have a material impact on our Consolidated Financial Statements.

Additional new accounting guidance became effective for us as of December 28, 2017 that we reviewed and concluded was either not applicable to our operations or had no material effect on the our Consolidated Financial Statements and related disclosures.

#### Accounting Standards to be Adopted

In February 2016, the Financial Accounting Standards Board (“FASB”) issued ASU 2016-02, “Leases (Topic 842)”, which provides guidance for accounting for leases. The new guidance requires companies to recognize a right-of-use asset and a lease liability for all operating and capital (financing) leases with lease terms greater than 12 months. The FASB has subsequently amended this guidance by issuing ASU 2018-10 and ASU 2018-11 in July 2018 to provide clarification and further guidance around areas identified as potential implementation issues and to allow an alternative transition method. The alternative transition method allows entities to initially apply the new leases standard at the adoption date by recognizing a cumulative-effect adjustment to the opening balance of retained earnings in the period of adoption rather than retroactive restatement of all periods presented. All of the standards are effective for annual and interim periods beginning after December 15, 2018 (our fiscal 2019) with early adoption permitted. The guidance will be adopted using the alternative transition method.

The adoption of ASU 2016-02 will have a material impact on our Consolidated Balance Sheets resulting from the recognition of operating lease right-of-use assets and liabilities. Although the new guidance is also expected to impact the measurement and presentation of certain expenses and cash flows related to leasing arrangements, we do not believe there will be a material impact to our Consolidated Statements of Income or Consolidated Statements of Cash Flows. We do not expect the recognition of the additional operating lease liabilities will impact any credit facility debt covenants as these liabilities are not considered to be debt.

We have decided to elect the package of practical expedients that do not require us to reassess whether existing contracts are or contain leases, lease classification or initial direct costs. In addition, we have decided not to elect the hindsight practical expedient which would allow us to reassess lease terms and impairment of the right-to-use assets. We have completed the implementation of a new lease management system in preparation for adoption and continue to assess the impact that the new guidance will have on our financial statements and related disclosures.

In June 2016, the FASB issued ASU 2016-13, “Financial Instruments—Credit Losses (Topic 326): Measurement of Credit Losses on Financial Instruments”. The new guidance replaces the incurred loss impairment methodology in current GAAP with a methodology that reflects expected credit losses and requires consideration of a broader range of reasonable and supportable information to inform financial statement users of credit loss estimates. ASU 2016-13 is effective for annual and interim periods beginning after December 15, 2019 (our fiscal 2020) with early adoption permitted for annual and interim periods beginning after December 15, 2018 (our fiscal 2019). We do not expect the adoption of this guidance to have a material impact on our Consolidated Financial Statements.

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

### Note 3. Revenues

Our revenues are derived primarily from two sales channels, which we operate as one segment: company restaurants and franchised and licensed restaurants. The following table disaggregates our revenue by sales channels and types of goods or services.

|                                | Quarter Ended          |                           | Three Quarters Ended |                           |
|--------------------------------|------------------------|---------------------------|----------------------|---------------------------|
|                                | September 26, 2018     | September 27, 2017<br>(1) | September 26, 2018   | September 26, 2017<br>(1) |
|                                | (Dollars in thousands) |                           |                      |                           |
| Company restaurant sales       | \$ 103,609             | \$ 97,915                 | \$ 307,543           | \$ 290,049                |
| Franchise and license revenue: |                        |                           |                      |                           |
| Royalties                      | 25,518                 | 25,174                    | 75,875               | 75,056                    |
| Advertising revenue            | 19,546                 | —                         | 58,386               | —                         |
| Initial and other fees         | 1,415                  | 507                       | 4,642                | 1,579                     |
| Occupancy revenue              | 7,935                  | 8,788                     | 24,184               | 26,986                    |
| Franchise and license revenue  | 54,414                 | 34,469                    | 163,087              | 103,621                   |
| Total operating revenue        | \$ 158,023             | \$ 132,384                | \$ 470,630           | \$ 393,670                |

(1) As disclosed in Note 2, prior period amounts have not been adjusted under the modified retrospective method of adoption of Topic 606.

#### Company Restaurant Revenue

Company restaurant revenue is recognized at the point in time when food and beverage products are sold at company restaurants. We present company restaurant sales net of sales-related taxes collected from customers and remitted to governmental taxing authorities. The adoption of Topic 606 did not impact the recognition of company restaurant sales.

#### Franchise Revenue

Franchise and license revenues consist primarily of royalties, advertising revenue, initial and other fees and occupancy revenue.

Under franchise agreements we provide franchisees with a license of our brand's symbolic intellectual property, administration of advertising programs (including local co-operatives), and other ongoing support functions. These services are highly interrelated so we do not consider them to be individually distinct performance obligations, and therefore account for them under Topic 606 as a single performance obligation. Revenue from franchise agreements is recognized evenly over the term of the agreement with the exception of sales-based royalties.



Royalty and advertising revenues represent sales-based royalties that are recognized in the period in which the sales occur. Sales-based royalties are variable consideration related to our performance obligation to our franchisees to maintain the intellectual property being licensed. Under our franchise agreements, franchisee advertising contributions must be spent on marketing and related activities. The adoption of Topic 606 did not impact the recognition of royalties. Upon adoption of Topic 606, advertising revenues and expenditures are recorded on a gross basis within the Consolidated Statements of Income. Under the previous guidance of Topic 605, we recorded franchise advertising expense net of contributions from franchisees to our advertising programs, including local co-operatives. While this change materially impacts the gross amount of reported franchise and license revenue and costs of franchise and license revenue, the impact is generally an offsetting increase to both revenue and expense with little, if any, impact on operating income and net income.

Initial and other fees consist of initial, successor and assignment franchise fees (“initial franchise fees”). Initial franchise fees are billed and received upon the signing of the franchise agreement. Under Topic 606, recognition of these fees is deferred until the commencement date of the agreement and occurs over time based on the term of the underlying franchise agreement. In the event a franchise agreement is terminated, any remaining deferred fees are recognized in the period of termination. Under the previous guidance, initial franchise fees were recognized upon the opening of a franchise restaurant.

Initial and other fees also includes revenue that are distinct from the franchise agreement and are separate performance obligations. Training and other franchise services fees are billed and recognized at a point in time as services are rendered. Similar to advertising revenue, upon adoption of Topic 606, other franchise services fees are recorded on a gross basis within the Consolidated Statements of Income, whereas, under previous guidance, they were netted against the related expenses.

Occupancy revenue results from leasing or subleasing restaurants to franchisees and is recognized over the term of the lease agreement.

With the exception of initial and other franchise fees, revenues are typically billed and collected on a weekly basis.

#### Gift Card Breakage

Under previous guidance, we recorded gift card breakage when the likelihood of redemption was remote. Breakage was recorded as a benefit to our advertising fund or reduction to other operating expenses, depending on where the gift cards were sold. Upon adoption of Topic 606, gift card breakage is recognized proportionally as redemptions occur. Our gift card breakage primarily relates to cards sold by third parties. Breakage revenue related to third party sales is recorded as advertising revenue (included as a component of franchise and license revenue).

#### Financial Statement Impact of Adoption

The following tables summarize the impact of adopting Topic 606 on our financial statement line items as of September 26, 2018 and for the quarter and three quarters ended September 26, 2018.

| Consolidated Balance Sheet       | Quarter ended September 26,<br>2018 |             |   |
|----------------------------------|-------------------------------------|-------------|---|
|                                  | As<br>Reported                      | Adjustments | Amounts<br>without<br>adoption<br>of Topic<br>606 |
|                                  | (In thousands)                      |             |   |
| Prepaid and other current assets | \$ 10,495                           | \$ 509      | \$ 11,004   |
| Deferred income taxes            | 15,595                              | (5,040 )    | 10,555  |
| Other current liabilities        | 53,911                              | (360 )      | 53,551  |
| Other noncurrent liabilities     | 43,888                              | (18,618 )   | 25,270  |
| Deficit                          | (317,917)                           | 14,447      | (303,470)   |



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| Consolidated Statement of Income       | Quarter ended September 26, 2018         |              |                                       | Three quarters ended September 26, 2018 |              |                                       |
|--|--|--------------|---------------------------------------|---|--------------|---------------------------------------|
|  | As Reported                              | Adjustments  | Amounts without adoption of Topic 606 | As Reported                             | Adjustments  | Amounts without adoption of Topic 606 |
|  | (In thousands, except per share amounts) |              |                                       |   |              |                                       |
| Franchise and license revenue          | \$54,414                                 | \$ (20,397 ) | \$ 34,017                             | \$163,087                               | \$ (61,653 ) | \$101,434                             |
| Costs of franchise and license revenue | 28,174                                   | (20,007 )    | 8,167                                 | 85,779                                  | (60,306 )    | 25,473                                |
| Provision for income taxes             | 2,810                                    | (101 )       | 2,709                                 | 7,217                                   | (348 )       | 6,869                                 |
| Net income                             | 10,805                                   | (289 )       | 10,516                                | 32,190                                  | (999 )       | 31,191                                |
| Basic net income per share             | \$0.17                                   | \$ —         | \$ 0.17                               | \$0.50                                  | \$ (0.01 )   | \$0.49                                |
| Diluted net income per share           | \$0.16                                   | \$ —         | \$ 0.16                               | \$0.49                                  | \$ (0.02 )   | \$0.47                                |

| Consolidated Statement of Comprehensive Income | Quarter ended September 26, 2018 |             |                                       | Three quarters ended September 26, 2018 |             |                                       |
|--|----------------------------------|-------------|---------------------------------------|---|-------------|---------------------------------------|
|  | As Reported                      | Adjustments | Amounts without adoption of Topic 606 | As Reported                             | Adjustments | Amounts without adoption of Topic 606 |
|  | (In thousands)                   |             |                                       |   |             |                                       |
| Net income                                     | \$10,805                         | \$ (289 )   | \$ 10,516                             | \$32,190                                | \$ (999 )   | \$ 31,191                             |
| Total comprehensive income                     | 15,363                           | (289 )      | 15,074                                | 37,047                                  | (999 )      | 36,048                                |

| Consolidated Statement of Cash Flow             | Three quarters ended September 26, 2018 |             |                                       |
|---|---|-------------|---------------------------------------|
|   | As Reported                             | Adjustments | Amounts without adoption of Topic 606 |
|   | (In thousands)                          |             |                                       |
| Net income                                      | \$32,190                                | \$ (999 )   | \$31,191                              |
| Deferred income tax expense                     | 5,044                                   | (348 )      | 4,696                                 |
| Changes in assets and liabilities:              |   |             |                                       |
| Other current assets                            | 1,292                                   | (509 )      | 783                                   |
| Other accrued liabilities                       | (7,733 )                                | 621         | (7,112 )                              |
| Other noncurrent liabilities                    | (2,339 )                                | 1,235       | (1,104 )                              |
| Net cash flows provided by operating activities | 46,259                                  | —           | 46,259                                |

The following significant changes impacted our financial statement line items as of September 26, 2018 and for the quarter and three quarters ended September 26, 2018:

Upon adoption of Topic 606, we recorded a cumulative effect adjustment related to previously recognized initial franchise fees resulting in a \$21.0 million increase to deferred franchise revenue, a \$15.6 million increase to opening deficit and a \$5.4 million increase to deferred tax assets. The deferred franchise revenue resulting from the cumulative effect adjustment will be amortized over the remaining lives of the individual franchise agreements. Also upon adoption, we recorded a cumulative effect adjustment to recognize breakage in proportion to redemptions that

occurred prior to December 28, 2017 resulting in a decrease of \$0.6 million to gift card liability (a component of other current liabilities), a \$0.5 million increase to accrued advertising (a component of other current liabilities) and a \$0.1 million decrease to opening deficit.

We recognized franchise and license revenue and costs of franchise and license revenue of \$19.5 million for the quarter and \$58.4 million year-to-date resulting from the recording of advertising revenues and expenditures on a gross basis under Topic 606 versus recording these amounts on a net basis under Topic 605.

We recognized additional franchise and license revenue of \$0.4 million for the quarter and \$1.4 million year-to-date under Topic 606 than we would have recognized under Topic 605, resulting from the timing of recognition of initial franchise fees.

We recognized franchise and license revenue and costs of franchise and license revenue of \$0.5 million for the quarter and \$1.9 million year-to-date resulting from the recording of other franchise services fees on a gross basis under Topic 606 versus recording these amount on a net basis under Topic 605.

#### Contract Balances

Contract balances related to contracts with customers consists of receivables, deferred franchise revenue and deferred gift card revenue. See Note 4 for details on our receivables.

Deferred franchise revenue consists primarily of the unamortized portion of initial franchise fees that are currently being amortized into revenue and amounts related to development agreements and unopened restaurants that will begin amortizing into revenue when the related restaurants are opened. Deferred franchise revenue represents our remaining performance obligations to our franchisees, excluding amounts of variable consideration related to sales-based royalties and advertising. The components of the change in deferred franchise revenue are as follows:

|   |                   |
|---|-------------------|
|   | (In<br>thousands) |
| Balance, December 27, 2017  | \$ 1,643          |
| Cumulative effect adjustment recognized upon adoption of Topic 606  | 20,976            |
| Fees received from franchisees                                      | 795               |
| Revenue recognized <sup>(1)</sup>                                   | (2,628 )          |
| Balance, September 26, 2018   | 20,786            |
| Less current portion included in other current liabilities          | 2,168             |
| Deferred franchise revenue included in other noncurrent liabilities | \$ 18,618         |

(1) Of this amount \$2.6 million was included in either the deferred franchise revenue balance as of December 27, 2017 or the cumulative effect adjustment.

As of September 26, 2018, the deferred franchise revenue expected to be recognized in the future is as follows:

|                            |                   |
|----------------------------|-------------------|
|                            | (In<br>thousands) |
| Remainder of 2018          | \$ 546            |
| 2019                       | 2,114             |
| 2020                       | 1,967             |
| 2021                       | 1,783             |
| 2022                       | 1,675             |
| Thereafter                 | 12,701            |
| Deferred franchise revenue | \$ 20,786         |

Deferred gift card liabilities consist of the unredeemed portion of gift cards sold in company restaurants and at third party locations. We recognize revenue when a gift card is redeemed in one of our company restaurants. Gift card

breakage is recognized proportionally as redemptions occur. The balance of deferred gift card liabilities represents our remaining performance obligations to our customers. The balance of deferred gift card liabilities as of September 26, 2018 and December 27, 2017 was \$4.1 million and \$6.5 million, respectively. During the three quarters ended September 26, 2018, we recognized revenue of \$1.4 million from gift card redemptions at company restaurants.

## Note 4. Receivables

Receivables were comprised of the following:

|  | September 26,<br>2018 | December 27,<br>2017 |
|--|-----------------------|----------------------|
|  | (In thousands)        |                      |
| Receivables, net:                          |                       |                      |
| Trade accounts receivable from franchisees | \$9,267               | \$ 10,688            |
| Financing receivables from franchisees     | 3,559                 | 5,084                |
| Vendor receivables                         | 2,039                 | 3,256                |
| Credit card receivables                    | 1,030                 | 1,870                |
| Other                                      | 1,566                 | 762                  |
| Allowance for doubtful accounts            | (275 )                | (276 )               |
| Total receivables, net                     | \$17,186              | \$ 21,384            |
| Other noncurrent assets:                   |                       |                      |
| Financing receivables from franchisees     | \$ 1,110              | \$ 427               |

During the three quarters ended September 26, 2018, we recorded an allowance for doubtful accounts of \$0.2 million of financing receivables from a franchisee.

## Note 5. Goodwill and Other Intangible Assets

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

|                                   | (In<br>thousands) |
|-----------------------------------|-------------------|
| Balance, December 27, 2017        | \$ 38,269         |
| Additions related to acquisitions | 1,574             |
| Balance, September 26, 2018       | \$ 39,843         |

Other intangible assets were comprised of the following:

|  | September 26, 2018          |                             | December 27, 2017           |                             |
|--|-----------------------------|-----------------------------|-----------------------------|-----------------------------|
|  | Gross<br>Carrying<br>Amount | Accumulated<br>Amortization | Gross<br>Carrying<br>Amount | Accumulated<br>Amortization |
|  | (In thousands)              |                             |                             |                             |
| Intangible assets with indefinite lives: |                             |                             |                             |                             |
| Trade names                              | \$44,087                    | \$ —                        | \$44,080                    | \$ —                        |
| Liquor licenses                          | 166                         | —                           | 166                         | —                           |
| Intangible assets with definite lives:   |                             |                             |                             |                             |
| Reacquired franchise rights              | 20,121                      | 4,467                       | 15,252                      | 2,389                       |
| Intangible assets, net                   | \$64,374                    | \$ 4,467                    | \$59,498                    | \$ 2,389                    |

During the three quarters ended September 26, 2018, we acquired six franchised restaurants for \$8.1 million, of which \$5.4 million was allocated to reacquired franchise rights, \$1.1 million to property and \$1.6 million to goodwill. In addition, we recorded \$2.4 million of capital leases in connection with the acquired franchised restaurants. We

account for the acquisition of franchised restaurants using the acquisition method of accounting for business combinations. The purchase price allocations were based on Level 3 fair value estimates.



## Note 6. Other Current Liabilities

Other current liabilities consisted of the following:

|  | September 26,<br>2018 | December 27,<br>2017 |
|--|-----------------------|----------------------|
|  | (In thousands)        |                      |
| Accrued payroll  | \$20,214              | \$ 20,998            |
| Accrued insurance, primarily current portion of liability for insurance claims | 7,067                 | 6,922                |
| Accrued taxes  | 9,358                 | 7,384                |
| Accrued advertising  | 4,738                 | 8,417                |
| Gift cards   | 4,129                 | 6,480                |
| Other  | 8,405                 | 9,045                |
| Other current liabilities  | \$53,911              | \$ 59,246            |

## Note 7. Operating (Gains), Losses and Other Charges, Net

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

|  | Quarter Ended<br>September 26,<br>2018 |          | September 27,<br>2017 |          | Three Quarters Ended<br>September 26,<br>2018 |  | September 27,<br>2017 |  |
|--|--|----------|-----------------------|----------|---|--|-----------------------|--|
|  | (In thousands)                         |          |                       |          |   |  |                       |  |
| Software implementation costs                    | \$—                                    | \$ 1,001 | \$—                   | \$ 4,669 |   |  |                       |  |
| Gains on sales of assets and other, net          | (695 )                                 | (411 )   | (759 )                | (1,646 ) |   |  |                       |  |
| Restructuring charges and exit costs             | 48                                     | 40       | 816                   | 436      |   |  |                       |  |
| Impairment charges                               | 1,440                                  | —        | 1,558                 | —        |   |  |                       |  |
| Operating (gains), losses and other charges, net | \$793                                  | \$ 630   | \$1,615               | \$ 3,459 |   |  |                       |  |

Software implementation costs of \$4.7 million for the three quarters ended September 27, 2017 were the result of our investment in a new cloud-based Enterprise Resource Planning system. Gains on sales of assets and other, net for the quarter and three quarters ended September 26, 2018 primarily related to insurance settlements on fire-damaged restaurants. Gains on sales of assets and other, net of \$1.6 million for the three quarters ended September 27, 2017 primarily related to real estate sold to franchisees.

Restructuring charges and exit costs were comprised of the following:

|  | Quarter Ended<br>September 26,<br>2018 |       | September 27,<br>2017 |        | Three Quarters Ended<br>September 26,<br>2018 |  | September 27,<br>2017 |  |
|--|--|-------|-----------------------|--------|---|--|-----------------------|--|
|  | (In thousands)                         |       |                       |        |   |  |                       |  |
| Exit costs                                 | \$48                                   | \$ 40 | \$ 347                | \$ 366 |   |  |                       |  |
| Severance and other restructuring charges  | —                                      | —     | 469                   | 70     |   |  |                       |  |
| Total restructuring charges and exit costs | \$48                                   | \$ 40 | \$ 816                | \$ 436 |   |  |                       |  |

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

|  | (In<br>thousands) |
|--|-------------------|
| Balance, December 27, 2017                                 | \$ 1,180          |
| Exit costs <sup>(1)</sup>                                  | 347               |
| Payments, net of sublease receipts                         | (440 )            |
| Interest accretion   | 57                |
| Balance, September 26, 2018                                | 1,144             |
| Less current portion included in other current liabilities | 489               |
| Long-term portion included in other noncurrent liabilities | \$ 655            |

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

As of September 26, 2018 and December 27, 2017, we had accrued severance and other restructuring charges of \$0.1 million and less than \$0.1 million, respectively. The balance as of September 26, 2018 is expected to be paid during the next 12 months.

Impairment charges for the quarter and three quarters ended September 26, 2018 primarily resulted from the impairment of an underperforming unit.

#### Note 8. Fair Value of Financial Instruments

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

|   | Total          | Quoted Prices in<br>Active Markets<br>for Identical<br>Assets/Liabilities<br>(Level 1) | Significant<br>Other<br>Observable<br>Inputs<br>(Level 2) | Significant<br>Unobservable<br>Inputs<br>(Level 3) |
|---|----------------|--|---|--|
|   | (In thousands) |  |   |  |
| Fair value measurements as of September 26, 2018:     |                |  |   |  |
| Deferred compensation plan investments <sup>(1)</sup> | \$ 12,808      | \$ 12,808  | \$ —  | \$ —   |
| Interest rate swaps, net <sup>(2)</sup>               | 4,280          | —  | 4,280   | —  |
| Investments <sup>(3)</sup>                            | 1,709          | —  | 1,709   | —  |
| Total   | \$ 18,797      | \$ 12,808  | \$ 5,989  | \$ —   |
| Fair value measurements as of December 27, 2017:      |                |  |   |  |
| Deferred compensation plan investments <sup>(1)</sup> | \$ 12,663      | \$ 12,663  | \$ —  | \$ —   |
| Interest rate swaps, net <sup>(2)</sup>               | (2,187 )       | —  | (2,187 )  | —  |
| Total   | \$ 10,476      | \$ 12,663  | \$ (2,187 )   | \$ —   |

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

(2) The fair values of our interest rate swaps are based upon Level 2 inputs, which include valuation models as reported by our counterparties. The key inputs for the valuation models are quoted market prices, interest rates and forward yield curves. See Note 9 for details on the interest rate swaps.

(3)

The fair value of investments is valued using a readily determinable net asset value per share based on the fair value of the underlying securities. There are no significant redemption restrictions associated with these investments.

## Note 9. Long-Term Debt

Denny's and certain of its subsidiaries have a credit facility consisting of a five-year \$400 million senior secured revolver (with a \$30 million letter of credit sublimit). The credit facility includes an accordion feature that would allow us to increase the size of the revolver to \$450 million. As of September 26, 2018, we had outstanding revolver loans of \$278.0 million and outstanding letters of credit under the senior secured revolver of \$19.8 million. These balances resulted in availability of \$102.2 million under the credit facility. Prior to considering the impact of our interest rate swaps, described below, the weighted-average interest rate on outstanding revolver loans was 4.12% and 3.42% as of September 26, 2018 and December 27, 2017, respectively. Taking into consideration our interest rate swaps, the weighted-average interest rate of outstanding revolver loans was 4.35% and 3.32% as of September 26, 2018 and December 27, 2017, respectively.

A commitment fee, which is based on our consolidated leverage ratio, is paid on the unused portion of the credit facility and was 0.30% as of September 26, 2018. Borrowings under the credit facility bear a tiered interest rate, also based on our leverage ratio, and was set at LIBOR plus 200 basis points as of September 26, 2018. The maturity date for the credit facility is October 26, 2022.

The credit facility is available for working capital, capital expenditures and other general corporate purposes. The credit facility is guaranteed by Denny's and its material subsidiaries and is secured by assets of Denny's and its subsidiaries, including the stock of its subsidiaries (other than our insurance captive subsidiary). It includes negative covenants that are usual for facilities and transactions of this type. The credit facility also includes certain financial covenants with respect to a maximum consolidated leverage ratio and a minimum consolidated fixed charge coverage ratio. We were in compliance with all financial covenants as of September 26, 2018.

## Interest Rate Hedges

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

Under the interest rate swaps, we pay a fixed rate on the notional amount in addition to the current interest rate as determined by our consolidated leverage ratio in effect at the time. A summary of our interest rate swaps as of September 26, 2018 is as follows:

| Trade Date        | Effective Date | Maturity Date     | Notional Amount<br>(In thousands) | Fixed Rate           |
|-------------------|----------------|-------------------|-----------------------------------|----------------------|
| March 20, 2015    | March 29, 2018 | March 31, 2025    | \$ 120,000                        | 2.44%                |
| October 1, 2015   | March 29, 2018 | March 31, 2026    | 50,000                            | 2.46%                |
| February 15, 2018 | March 31, 2020 | December 31, 2033 | 80,000                            | <sup>(1)</sup> 3.19% |

<sup>(1)</sup> The notional amount of the swaps entered into on February 15, 2018 increases annually beginning September 30, 2020 until they reach the maximum notional amount of \$425.0 million on September 28, 2029.

As of September 26, 2018, the fair value of the interest rate swaps was a net asset of \$4.3 million, which is comprised of assets of \$5.2 million recorded as a component of other noncurrent assets and liabilities of \$0.9 million recorded as a component of other noncurrent liabilities in our Condensed Consolidated Balance Sheets. See Note 14 for the amounts recorded in accumulated other comprehensive loss related to the interest rate swaps.



## Note 10. Share-Based Compensation

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

|  | Quarter Ended      |                    | Three Quarters Ended |                    |
|--|--------------------|--------------------|----------------------|--------------------|
|  | September 26, 2018 | September 27, 2017 | September 26, 2018   | September 27, 2017 |
|  | (In thousands)     |                    |                      |                    |
| Performance share awards                 | \$902              | \$ 2,246           | \$2,922              | \$ 6,090           |
| Restricted stock units for board members | 198                | 247                | 739                  | 456                |
| Total share-based compensation           | \$1,100            | \$ 2,493           | \$3,661              | \$ 6,546           |

## Performance Share Units

During the three quarters ended September 26, 2018, we granted certain employees approximately 0.2 million performance share units that vest based on the total shareholder return (“TSR”) of our common stock compared to the TSRs of a group of peer companies and 0.3 million performance share units that vest based on our Adjusted EPS growth rate versus plan, as defined under the terms of the award. As the TSR based performance share units contain a market condition, a Monte Carlo valuation was used to determine the grant date fair value of \$18.17 per share. The performance share units based on the Adjusted EPS growth rate have a grant date fair value of \$15.93 per share, the market value of our common stock on the date of grant. The awards granted to our named executive officers also contain a performance condition based on the attainment of an operating measure for the fiscal year ended December 26, 2018. The performance period for these performance share units is the three year fiscal period beginning December 28, 2017 and ending December 30, 2020. They will vest and be earned (from 0% to 150% of the target award for each such increment) at the end of the performance period.

During the three quarters ended September 26, 2018, we issued 0.2 million shares of common stock related to vested performance share units. In addition 0.3 million shares of common stock were deferred and 0.1 million shares of common stock were withheld in lieu of taxes related to vested performance share units.

As of September 26, 2018, we had approximately \$9.3 million of unrecognized compensation cost related to all unvested performance share awards outstanding, which have a weighted average remaining contractual term of 1.2 years.

## Restricted Stock Units for Board Members

During the three quarters ended September 26, 2018, we granted less than 0.1 million deferred stock units (which are equity classified) with a weighted average grant date fair value of \$15.50 per unit to non-employee members of our Board of Directors. The deferred stock units vest after a one year service period. A director may elect to convert these awards into shares of common stock either on a specific date in the future (while still serving as a member of our Board of Directors) or upon termination as a member of our Board of Directors. During the three quarters ended September 26, 2018, 0.2 million deferred stock units were converted into shares of common stock. As of September 26, 2018, we had approximately \$0.6 million of unrecognized compensation cost related to all unvested restricted stock unit awards outstanding, which have a weighted average remaining contractual term of 0.6 years.

## Note 11. Income Taxes

The effective income tax rate was 20.6% for the quarter ended September 26, 2018 and 18.3% for the three quarters ended September 26, 2018 compared to 36.8% and 36.3%, respectively, for the prior year periods. The 2018 periods

were impacted by the Tax Act. In addition, the 2018 quarterly and year-to-date rates benefited from a discrete item relating to share-based compensation of 0.4% and 3.1%, respectively. The Tax Act reduces the U.S. statutory tax rate from 35% to 21% for years after 2017. We revalued our deferred taxes during fiscal 2017 to reflect the reduced rate that will apply in future periods when these deferred taxes are realized. The implementation of the Tax Act resulted in certain stranded tax effects in accumulated other comprehensive income. Due to the immateriality of the stranded tax effects, we have elected not to reclassify these amounts from accumulated other comprehensive income to retained earnings.

## Note 12. Net Income Per Share

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

|  | Quarter Ended                                |                    | Three Quarters Ended |                    |
|--|--|--------------------|----------------------|--------------------|
|  | September 26, 2018                           | September 27, 2017 | September 26, 2018   | September 27, 2017 |
|  | (In thousands, except for per share amounts) |                    |                      |                    |
| Net income   | \$10,805                                     | \$ 9,325           | \$32,190             | \$ 26,447          |
| Weighted average shares outstanding - basic        | 63,246                                       | 66,873             | 63,774               | 69,095             |
| Effect of dilutive share-based compensation awards | 2,276  | 2,337              | 2,348                | 2,282              |
| Weighted average shares outstanding - diluted      | 65,522                                       | 69,210             | 66,122               | 71,377             |
| Basic net income per share                         | \$0.17                                       | \$ 0.14            | \$0.50               | \$ 0.38            |
| Diluted net income per share                       | \$0.16                                       | \$ 0.13            | \$0.49               | \$ 0.37            |
| Anti-dilutive share-based compensation awards      | —  | 606                | 471                  | 606                |

## Note 13. Supplemental Cash Flow Information

|  | Three Quarters Ended |                    |
|--|----------------------|--------------------|
|  | September 26, 2018   | September 27, 2017 |
|  | (In thousands)       |                    |
| Income taxes paid, net   | \$2,347              | \$ 5,039           |
| Interest paid  | \$14,349             | \$ 10,547          |
| Noncash investing and financing activities:                          |                      |                    |
| Property acquisition payable   | \$—                  | \$ 500             |
| Insurance proceeds receivable  | \$19                 | \$ —               |
| Issuance of common stock, pursuant to share-based compensation plans | \$4,671              | \$ 4,961           |
| Execution of capital leases  | \$2,850              | \$ 4,959           |
| Treasury stock payable   | \$419                | \$ 741             |
| Notes received in connection with disposition of property            | \$—                  | \$ 1,750           |

## Note 14. Shareholders' Equity

## Share Repurchase

Our credit facility permits the purchase of Denny's stock and the payment of cash dividends subject to certain limitations. In October 2017, our Board of Directors approved a share repurchase program authorizing us to repurchase up to \$200 million of our common stock (in addition to prior authorizations). Under this program, we may, from time to time, purchase shares in the open market (including pre-arranged stock trading plans in accordance with the guidelines specified in Rule 10b5-1 under the Securities Exchange Act of 1934, as amended) or in privately negotiated transactions, subject to market and business conditions.

During the three quarters ended September 26, 2018, we repurchased 2.4 million shares of our common stock for approximately \$37.4 million. This brings the total amount repurchased under the current repurchase program to 2.7 million shares of our common stock for approximately \$41.1 million, leaving approximately \$158.9 million that can



be used to repurchase our common stock under this program as of September 26, 2018. Repurchased shares are included as treasury stock in our Condensed Consolidated Balance Sheets and our Condensed Consolidated Statement of Shareholders' Equity.

## Accumulated Other Comprehensive Income (Loss)

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

|   | Defined<br>Benefit Plans | Derivatives | Accumulated<br>Other<br>Comprehensive<br>Income (Loss) |
|---|--------------------------|-------------|--|
|   | (In thousands)           |             |  |
| Balance as of December 27, 2017   | \$ (982)                 | \$ (1,334 ) | \$ (2,316 )  |
| Amortization of net loss <sup>(1)</sup>                                   | 84                       | —           | 84   |
| Net change in fair value of derivatives                                   | —                        | 6,225       | 6,225  |
| Reclassification of derivatives to interest expense, net <sup>(2)</sup>   | —                        | 241         | 241  |
| Income tax (expense) benefit related to items of other comprehensive loss | (20 )                    | (1,673 )    | (1,693 )   |
| Balance as of September 26, 2018  | \$ (918)                 | \$ 3,459    | \$ 2,541   |

Before-tax amount related to our defined benefit plans that was reclassified from accumulated other comprehensive (1) loss and included as a component of pension expense within general and administrative expenses in our Condensed Consolidated Statements of Income during the three quarters ended September 26, 2018.

Amounts reclassified from accumulated other comprehensive loss into income represent payments either received from or made to the counterparty for the effective portions of the interest rate swaps. These amounts are included (2) as a component of interest expense, net in our Condensed Consolidated Statements of Income. We expect to make payments to the counterparty and reclassify approximately \$0.6 million from accumulated other comprehensive loss related to our interest rate swaps during the next twelve months. See Note 9 for additional details.

## Note 15. Commitments and Contingencies

We have guarantees related to certain franchisee loans. Payments under these guarantees would result from the inability of a franchisee to fund required payments when due. Through September 26, 2018, no events had occurred that caused us to make payments under these guarantees. There were \$2.8 million and \$5.1 million of loans outstanding under these programs as of September 26, 2018 and December 27, 2017, respectively. As of September 26, 2018, the maximum amount payable under the loan guarantees was \$0.9 million. As a result of these guarantees, we have recorded liabilities of less than \$0.1 million as of both September 26, 2018 and December 27, 2017, which are included as a component of other noncurrent liabilities in our Condensed Consolidated Balance Sheets and other nonoperating expense in our Condensed Consolidated Statements of Income.

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

## Note 16. Subsequent Events

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

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

Forward-Looking Statements

This report contains forward-looking statements within the meaning of the Private Securities Litigation Reform Act of 1995. The forward-looking statements reflect our best judgment based on factors currently known and are intended to speak only as of the date such statements are made. Forward-looking statements involve risks, uncertainties, and other factors which may cause our actual performance to be materially different from the performance indicated or implied by such statements. You should consider our forward-looking statements in light of the risks discussed under Part I, Item 1A, "Risk Factors" in our most recent Annual Report on Form 10-K, as well as our consolidated financial statements, related notes, and the other financial information appearing elsewhere in this report and our other filings with the United States Securities and Exchange Commission. While we may elect to update forward-looking statements at some point in the future, we expressly disclaim any obligation to update any forward-looking statements, whether as a result of new information, future events, or otherwise, except as required by law.

Factors Impacting Comparability

Impact of New Revenue Recognition Standard

Effective December 28, 2017, the first day of fiscal 2018, the Company adopted Accounting Standards Update 2014-09, "Revenue from Contracts with Customers (Topic 606)" and all subsequent ASUs that modified Topic 606 on a modified retrospective basis. Results for reporting periods beginning after December 28, 2017 are presented under Topic 606. Prior period amounts are not adjusted and continue to be reported in accordance with our historical accounting under Topic 605 "Revenue Recognition."

The most significant effects of the new guidance on the comparability of our results of operations between 2018 and 2017 include the following:

Under Topic 606, advertising revenues and expenditures are recorded on a gross basis within the Consolidated Statements of Income. Under the previous guidance of Topic 605, we recorded franchise advertising expense net of contributions from franchisees to our advertising programs, including local co-operatives. While this change materially impacts the gross amount of reported franchise and license revenue and costs of franchise and license revenue, the impact is generally an offsetting increase to both revenue and expense with little, if any, impact on operating income and net income. Similarly, upon adoption, other franchise services fees are recorded on a gross basis within the Consolidated Statements of Income, whereas, under previous guidance, they were netted against the related expenses.

Under Topic 606, recognition of initial franchise fees is deferred until the commencement date of the agreement and occurs over time based on the term of the underlying franchise agreement. In the event a franchise agreement is terminated, any remaining deferred fees are recognized in the period of termination. Under the previous guidance, initial franchise fees were recognized upon the opening of a franchise restaurant. The effect of the required deferral of initial franchise fees received in a given year is mitigated by the recognition of revenue from fees received in prior periods.

Under previous guidance, we recorded gift card breakage when the likelihood of redemption was remote. Breakage was recorded as a benefit to our advertising fund or reduction to other operating expenses, depending on where the gift cards were sold. Under Topic 606, gift card breakage is recognized proportionally as redemptions occur. Our gift card breakage primarily relates to cards sold by third parties. Breakage revenue related to third party sales is recorded as advertising revenue (included as a component of franchise and license revenue) with an offsetting amount recorded

as advertising expense (included as a component of costs of franchise and license revenue).

See Note 2 and Note 3 for information on the implementation of Topic 606 and its impact on our Consolidated Financial Statements.

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Statements of Income

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

|  | Quarter Ended          |         |                    |         | Three Quarters Ended |         |                    |         |
|--|------------------------|---------|--------------------|---------|----------------------|---------|--------------------|---------|
|  | September 26, 2018     |         | September 27, 2017 |         | September 26, 2018   |         | September 27, 2017 |         |
|  | (Dollars in thousands) |         |                    |         |                      |         |                    |         |
| Revenue:   |                        |         |                    |         |                      |         |                    |         |
| Company restaurant sales                         | \$103,609              | 65.6 %  | \$97,915           | 74.0 %  | \$307,543            | 65.3 %  | \$290,049          | 73.7 %  |
| Franchise and license revenue                    | 54,414                 | 34.4 %  | 34,469             | 26.0 %  | 163,087              | 34.7 %  | 103,621            | 26.3 %  |
| Total operating revenue                          | 158,023                | 100.0 % | 132,384            | 100.0 % | 470,630              | 100.0 % | 393,670            | 100.0 % |
| Costs of company restaurant sales (a):           |                        |         |                    |         |                      |         |                    |         |
| Product costs                                    | 25,303                 | 24.4 %  | 24,896             | 25.4 %  | 75,292               | 24.5 %  | 72,798             | 25.1 %  |
| Payroll and benefits                             | 41,041                 | 39.6 %  | 37,332             | 38.1 %  | 123,332              | 40.1 %  | 113,221            | 39.0 %  |
| Occupancy  | 6,083                  | 5.9 %   | 5,054              | 5.2 %   | 17,165               | 5.6 %   | 15,291             | 5.3 %   |
| Other operating expenses                         | 15,419                 | 14.9 %  | 14,040             | 14.3 %  | 45,490               | 14.8 %  | 39,544             | 13.6 %  |
| Total costs of company restaurant sales          | 87,846                 | 84.8 %  | 81,322             | 83.1 %  | 261,279              | 85.0 %  | 240,854            | 83.0 %  |
| Costs of franchise and license revenue (a)       | 28,174                 | 51.8 %  | 9,493              | 27.5 %  | 85,779               | 52.6 %  | 29,483             | 28.5 %  |
| General and administrative expenses              | 15,981                 | 10.1 %  | 16,446             | 12.4 %  | 48,138               | 10.2 %  | 50,536             | 12.8 %  |
| Depreciation and amortization                    | 6,760                  | 4.3 %   | 5,958              | 4.5 %   | 19,965               | 4.2 %   | 17,493             | 4.4 %   |
| Operating (gains), losses and other charges, net | 793                    | 0.5 %   | 630                | 0.5 %   | 1,615                | 0.3 %   | 3,459              | 0.9 %   |
| Total operating costs and expenses, net          | 139,554                | 88.3 %  | 113,849            | 86.0 %  | 416,776              | 88.6 %  | 341,825            | 86.8 %  |
| Operating income                                 | 18,469                 | 11.7 %  | 18,535             | 14.0 %  | 53,854               | 11.4 %  | 51,845             | 13.2 %  |
| Interest expense, net                            | 5,314                  | 3.4 %   | 4,067              | 3.1 %   | 15,324               | 3.3 %   | 11,348             | 2.9 %   |
| Other nonoperating income, net                   | (460)                  | (0.3)%  | (286)              | (0.2)%  | (877)                | (0.2)%  | (1,053)            | (0.3)%  |
| Net income before income taxes                   | 13,615                 | 8.6 %   | 14,754             | 11.1 %  | 39,407               | 8.4 %   | 41,550             | 10.6 %  |
| Provision for income taxes                       | 2,810                  | 1.8 %   | 5,429              | 4.1 %   | 7,217                | 1.5 %   | 15,103             | 3.8 %   |
| Net income                                       | \$10,805               | 6.8 %   | \$9,325            | 7.0 %   | \$32,190             | 6.8 %   | \$26,447           | 6.7 %   |
| Other Data:                                      |                        |         |                    |         |                      |         |                    |         |
| Company average unit sales                       | \$582                  |         | \$577              |         | \$1,716              |         | \$1,706            |         |
| Franchise average unit sales                     | \$409                  |         | \$403              |         | \$1,207              |         | \$1,188            |         |
| Company equivalent units (b)                     | 178                    |         | 170                |         | 179                  |         | 170                |         |
| Franchise equivalent units (b)                   | 1,536                  |         | 1,550              |         | 1,541                |         | 1,557              |         |
| Company same-store sales increase (c)(d)         | 2.1 %                  |         | 0.6 %              |         | 1.7 %                |         | 0.6 %              |         |

Domestic franchise  
same-store sales increase    0.8    %                    0.6    %                    0.4    %                    0.7    %  
(c)(d)

- Costs of company restaurant sales percentages are as a percentage of company restaurant sales. Costs of franchise (a) and license revenue percentages are as a percentage of franchise and license revenue. All other percentages are as a percentage of total operating revenue.
- (b) Equivalent units are calculated as the weighted average number of units outstanding during a defined time period.
- (c) Same-store sales include sales from company restaurants or non-consolidated franchised and licensed restaurants that were open the same period in the prior year.
- (d) Prior year amounts have not been restated for 2018 comparable units.

## Unit Activity

|  | Quarter Ended  |                | Three Quarters Ended |                |
|--|----------------|----------------|----------------------|----------------|
|  | September 2018 | September 2017 | September 2018       | September 2017 |
| Company restaurants, beginning of period                 | 180            | 172            | 178                  | 169            |
| Units opened   | 1              | 1              | 1                    | 2              |
| Units acquired from franchisees                          | —              | 1              | 6                    | 7              |
| Units sold to franchisees                                | —              | —              | —                    | (4)            |
| Units closed   | —              | —              | (4)                  | —              |
| End of period  | 181            | 174            | 181                  | 174            |
| Franchised and licensed restaurants, beginning of period | 1,540          | 1,552          | 1,557                | 1,564          |
| Units opened   | 6              | 8              | 24                   | 23             |
| Units purchased from Company                             | —              | —              | —                    | 4              |
| Units acquired by Company                                | —              | (1)            | (6)                  | (7)            |
| Units closed   | (12)           | (8)            | (41)                 | (33)           |
| End of period  | 1,534          | 1,551          | 1,534                | 1,551          |
| Total restaurants, end of period                         | 1,715          | 1,725          | 1,715                | 1,725          |

## Company Restaurant Operations

During the quarter ended September 26, 2018, company restaurant sales increased \$5.7 million, or 5.8%, primarily resulting from an eight equivalent unit increase in company restaurants as compared to the prior year period and a 2.1% increase in company same-store sales. During the three quarters ended September 26, 2018, company restaurant sales increased \$17.5 million, or 6.0%, primarily resulting from a nine equivalent unit increase in company restaurants as compared to the prior year period and a 1.7% increase in company same-store sales.

Total costs of company restaurant sales as a percentage of company restaurant sales increased to 84.8% for the quarter and 85.0% year-to-date from 83.1% and 83.0%, respectively, in the prior year periods.

Product costs were 24.4% for the quarter and 24.5% year-to-date compared to 25.4% and 25.1%, respectively, for the prior year periods. The decrease for the quarter was primarily due to leverage gained from increased pricing and lower commodity costs. The decrease year-to-date was primarily due to leverage gained from increased pricing.

Payroll and benefits were 39.6% for the quarter and 40.1% year-to-date compared to 38.1% and 39.0%, respectively, in the prior year periods. The increase for the quarter was primarily due to a 0.6 percentage point increase in workers' compensation costs and a 0.7 percentage point increase in labor costs partially resulting from minimum wage increases. The quarter ended September 26, 2018 included \$0.7 million in favorable workers' compensation experience, as compared to \$1.3 million of favorable workers' compensation experience in the prior year period. The increase year-to-date was primarily due to a 0.9 percentage point increase in labor costs resulting from minimum wage increases and a 0.3 percentage point increase in workers' compensation costs. The three quarters ended September 26, 2018 included \$0.6 million in favorable workers' compensation experience, as compared to \$1.6 million of favorable workers' compensation experience in the prior year period.

Occupancy costs were 5.9% for the quarter and 5.6% year-to-date compared to 5.2% and 5.3%, respectively, for the prior year periods. The increases for the quarter and year-to-date periods were primarily related to increases in general liability insurance costs, as the current year periods included negative claims development of \$0.4 million and \$0.3 million, respectively, and the prior year periods included favorable claims development of \$0.2 million and \$0.5

million, respectively.

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

|                          | Quarter Ended          |                       |          | Three Quarters Ended  |                       |       |
|--------------------------|------------------------|-----------------------|----------|-----------------------|-----------------------|-------|
|                          | September 26,<br>2018  | September 27,<br>2017 |          | September 26,<br>2018 | September 27,<br>2017 |       |
|                          | (Dollars in thousands) |                       |          |                       |                       |       |
| Utilities                | \$3,926                | 3.8 %                 | \$3,767  | 3.8 %                 | \$10,690              | 3.5 % |
| Repairs and maintenance  | 1,870                  | 1.8 %                 | 1,642    | 1.7 %                 | 5,647                 | 1.8 % |
| Marketing                | 3,791                  | 3.7 %                 | 3,740    | 3.8 %                 | 11,267                | 3.7 % |
| Other direct costs       | 5,832                  | 5.6 %                 | 4,891    | 5.0 %                 | 17,886                | 5.8 % |
| Other operating expenses | \$15,419               | 14.9%                 | \$14,040 | 14.3%                 | \$45,490              | 14.8% |

The increase in other direct costs was primarily related to increased delivery sales resulting in higher third party delivery fees of \$0.7 million for the quarter and \$2.2 million year-to-date.

#### Franchise Operations

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

|  | Quarter Ended          |                       |          | Three Quarters Ended  |                       |        |
|--|------------------------|-----------------------|----------|-----------------------|-----------------------|--------|
|  | September 26,<br>2018  | September 27,<br>2017 |          | September 26,<br>2018 | September 27,<br>2017 |        |
|  | (Dollars in thousands) |                       |          |                       |                       |        |
| Royalties                              | \$25,518               | 46.9 %                | \$25,174 | 73.0 %                | \$75,875              | 46.5 % |
| Advertising revenue                    | 19,546                 | 35.9 %                | —        | — %                   | 58,386                | 35.8 % |
| Initial and other fees                 | 1,415                  | 2.6 %                 | 507      | 1.5 %                 | 4,642                 | 2.8 %  |
| Occupancy revenue                      | 7,935                  | 14.6 %                | 8,788    | 25.5 %                | 24,184                | 14.8 % |
| Franchise and license revenue          | \$54,414               | 100.0%                | \$34,469 | 100.0%                | \$163,087             | 100.0% |
| Advertising costs                      | \$19,546               | 35.9 %                | \$364    | 1.1 %                 | \$58,386              | 35.8 % |
| Occupancy costs                        | \$5,585                | 10.3 %                | \$6,343  | 18.4 %                | \$17,059              | 10.5 % |
| Other direct costs                     | 3,043                  | 5.6 %                 | 2,786    | 8.1 %                 | 10,334                | 6.3 %  |
| Costs of franchise and license revenue | \$28,174               | 51.8 %                | \$9,493  | 27.5 %                | \$85,779              | 52.6 % |

Royalties increased \$0.3 million, or 1.4%, for the quarter and \$0.8 million, or 1.1%, for the three quarters ended September 26, 2018. The increases primarily resulted from higher average royalty rates and increases in domestic same-store sales, partially offset by equivalent unit decreases in franchised and licensed restaurants. Domestic same-store sales increased 0.8% and 0.4% and equivalent units decreased by 14 and 16 for the quarter and three quarters ended September 26, 2018, respectively.

The increases in initial and other fees and advertising revenue primarily resulted from the implementation of Topic 606 related to revenue recognition. We recognized additional franchise and license revenue of \$0.4 million for the quarter and \$1.4 million year-to-date, resulting from the timing of recognition of initial franchise fees under the new guidance. In addition, we recognized other franchise fees of \$0.5 million for the quarter and \$1.9 million year-to-date resulting from the recording of other franchise services fees on a gross basis under the new guidance versus recording these amounts on a net basis as previously presented. Advertising revenue and costs are also now required to be presented on a gross basis, instead of a net basis as previously presented. The decrease in occupancy revenue of \$0.9 million, or 9.7%, for the quarter and \$2.8 million, or 10.4%, year-to-date was primarily the result of scheduled lease

expirations.

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Costs of franchise and license revenue increased \$18.7 million, or 196.8%, for the quarter and \$56.3 million, or 190.9%, year-to-date. These increases were primarily related to the increase in advertising costs related to the implementation of Topic 606, as advertising revenue is no longer netted with advertising expense. Occupancy costs decreased \$0.8 million, or 12.0%, for the quarter and \$2.4 million, or 12.2%, year-to-date primarily resulting from scheduled lease expirations. The increase in other direct costs primarily related to the implementation of Topic 606, as certain other franchise expenses are no longer netted with the related fees received from franchisees. As a result, costs of franchise and license revenue as a percentage of franchise and license revenue increased to 51.8% for the quarter from 27.5% for the prior year quarter and 52.6% year-to-date from 28.5% for the prior year period.

#### Other Operating Costs and Expenses

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

General and administrative expenses were comprised of the following:

|   | Quarter Ended      |                    | Three Quarters Ended |                    |
|---|--------------------|--------------------|----------------------|--------------------|
|   | September 26, 2018 | September 27, 2017 | September 26, 2018   | September 27, 2017 |
|   | (In thousands)     |                    |                      |                    |
| Share-based compensation                  | \$1,100            | \$ 2,493           | \$3,661              | \$ 6,546           |
| Other general and administrative expenses | 14,881             | 13,953             | 44,477               | 43,990             |
| Total general and administrative expenses | \$15,981           | \$ 16,446          | \$48,138             | \$ 50,536          |

Share-based compensation decreased \$1.4 million for the quarter and \$2.9 million year-to-date primarily resulting from decreases in the expected performance of certain share-based compensation awards. Other general and administrative expenses increased by \$0.9 million for the quarter and \$0.5 million year-to-date. The increases for the quarter and year-to-date periods primarily resulted from increases in investments in personnel.

Depreciation and amortization was comprised of the following:

|   | Quarter Ended      |                    | Three Quarters Ended |                    |
|---|--------------------|--------------------|----------------------|--------------------|
|   | September 26, 2018 | September 27, 2017 | September 26, 2018   | September 27, 2017 |
|   | (In thousands)     |                    |                      |                    |
| Depreciation of property and equipment      | \$4,717            | \$ 4,261           | \$13,788             | \$ 12,711          |
| Amortization of capital lease assets        | 1,003              | 1,021              | 3,092                | 3,011              |
| Amortization of intangible and other assets | 1,040              | 676                | 3,085                | 1,771              |
| Total depreciation and amortization expense | \$6,760            | \$ 5,958           | \$19,965             | \$ 17,493          |

The increases in depreciation of property and equipment and amortization of intangible and other assets primarily relate to acquisitions of franchised restaurants during the current and prior year.

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

|  | Quarter Ended      |                    | Three Quarters Ended |                    |
|--|--------------------|--------------------|----------------------|--------------------|
|  | September 26, 2018 | September 27, 2017 | September 26, 2018   | September 27, 2017 |
|  | (In thousands)     |                    |                      |                    |
| Software implementation costs                    | \$—                | \$ 1,001           | \$—                  | \$ 4,669           |
| Gains on sales of assets and other, net          | (695 )             | (411 )             | (759 )               | (1,646 )           |
| Restructuring charges and exit costs             | 48                 | 40                 | 816                  | 436                |
| Impairment charges                               | 1,440              | —                  | 1,558                | —                  |
| Operating (gains), losses and other charges, net | \$793              | \$ 630             | \$1,615              | \$ 3,459           |

Software implementation costs of \$4.7 million for the three quarters ended September 27, 2017 were the result of our investment in a new cloud-based Enterprise Resource Planning system. Gains on sales of assets and other, net for the quarter and three quarters ended September 26, 2018 primarily related to insurance settlements on fire-damaged restaurants. Gains on sales of assets and other, net of \$1.6 million for the three quarters ended September 27, 2017 primarily related to real estate sold to franchisees.

Restructuring charges and exit costs were comprised of the following:

|   | Quarter Ended      |                    | Three Quarters Ended |                    |
|---|--------------------|--------------------|----------------------|--------------------|
|   | September 26, 2018 | September 27, 2017 | September 26, 2018   | September 27, 2017 |
|   | (In thousands)     |                    |                      |                    |
| Exit costs                                | \$48               | \$ 40              | \$ 347               | \$ 366             |
| Severance and other restructuring charges | —                  | —                  | 469                  | 70                 |
| Total restructuring and exit costs        | \$48               | \$ 40              | \$ 816               | \$ 436             |

Impairment charges for the quarter and three quarters ended September 26, 2018 primarily resulted from the impairment of an underperforming unit.

Operating income was \$18.5 million for the quarter and \$53.9 million year-to-date compared to \$18.5 million and \$51.8 million, respectively, for the prior year periods.

Interest expense, net was comprised of the following:

|  | Quarter Ended      |                    | Three Quarters Ended |                    |
|--|--------------------|--------------------|----------------------|--------------------|
|  | September 30, 2018 | September 30, 2017 | September 30, 2018   | September 30, 2017 |
|  | (In thousands)     |                    |                      |                    |
| Interest on credit facilities            | \$3,045            | \$ 2,078           | \$8,656              | \$ 5,333           |
| Interest on interest rate swaps          | 155                | (30                | ) 241                | 116                |
| Interest on capital lease liabilities    | 1,542              | 1,470              | 4,716                | 4,286              |
| Letters of credit and other fees         | 322                | 303                | 980                  | 886                |
| Interest income                          | (47                | ) (21              | ) (125               | ) (85              |
| Total cash interest                      | 5,017              | 3,800              | 14,468               | 10,536             |
| Amortization of deferred financing costs | 152                | 149                | 455                  | 446                |
| Interest accretion on other liabilities  | 145                | 118                | 401                  | 366                |
| Total interest expense, net              | \$5,314            | \$ 4,067           | \$15,324             | \$ 11,348          |

Interest expense, net increased by \$1.2 million for the quarter and \$4.0 million year-to-date primarily due to increases in the balance of our credit facility and related interest rates.

Other nonoperating income, net was \$0.5 million for the quarter and \$0.9 million year-to-date compared to \$0.3 million and \$1.1 million, respectively, for the prior year periods. The income for the 2018 periods related to gains on deferred compensation plan investments, positive valuation adjustments on our self-insured insurance liabilities, which resulted from an increased discount rate, and gains on lease terminations. The income for the 2017 periods primarily resulted from gains on deferred compensation plan investments.

Provision for income taxes was \$2.8 million for the quarter and \$7.2 million year-to-date compared to \$5.4 million and \$15.1 million, respectively, for the prior year periods. The effective tax rate was 20.6% for the quarter and 18.3% year-to-date compared to 36.8% and 36.3%, respectively, for the prior year periods. The 2018 periods were impacted by the Tax Act. In addition, the 2018 quarterly and year-to-date rates benefited from a discrete item relating to share-based compensation of 0.4% and 3.1%, respectively. The Tax Act reduces the U.S. statutory tax rate from 35% to 21% for years after 2017. We revalued our deferred taxes during fiscal 2017 to reflect the reduced rate that will apply in future periods when these deferred taxes are realized. The implementation of the Tax Act resulted in certain stranded tax effects in accumulated other comprehensive income. Due to the immateriality of the stranded tax effects, we have elected not to reclassify these amounts from accumulated other comprehensive income to retained earnings. We expect the 2018 fiscal year effective tax rate to be between 16% and 19%. The annual effective tax rate cannot be determined until the end of the fiscal year; therefore, the actual rate could differ from our current estimates.

Net income was \$10.8 million for the quarter and \$32.2 million year-to-date compared with \$9.3 million and \$26.4 million, respectively, for the prior year periods.

#### Liquidity and Capital Resources

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

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

|   | Three Quarters Ended |                    |
|---|----------------------|--------------------|
|   | September 26, 2018   | September 27, 2017 |
|   | (In thousands)       |                    |
| Net cash provided by operating activities | \$46,259             | \$ 43,525          |
| Net cash used in investing activities     | (28,497 )            | (19,788 )          |
| Net cash used in financing activities     | (20,874 )            | (24,666 )          |
| Decrease in cash and cash equivalents     | \$(3,112 )           | \$ (929 )          |

Net cash flows provided by operating activities were \$46.3 million for the three quarters ended September 26, 2018 compared to \$43.5 million for the three quarters ended September 27, 2017. The increase in cash flows provided by operating activities was primarily due to the increase in net income during the three quarters ended September 26, 2018. We believe that our estimated cash flows from operations for 2018, combined with our capacity for additional borrowings under our credit facility, will enable us to meet our anticipated cash requirements and fund capital expenditures over the next 12 months.

Net cash flows used in investing activities were \$28.5 million for the three quarters ended September 26, 2018. These cash flows were primarily comprised of capital expenditures of \$17.3 million, acquisitions of restaurants and real estate of \$10.4 million and note receivable issuances of \$2.5 million. Cash flows for acquisitions included \$8.1 million for the acquisition of six franchised restaurants, \$1.8 million for real estate and \$0.5 million related to a prior year acquisition. Net cash flows used in investing activities were \$19.8 million for the three quarters ended September 27, 2017. These cash flows were primarily comprised of capital expenditures of \$13.6 million and acquisitions of restaurants and real estate of \$10.0 million. Cash flows for acquisitions included \$4.0 million of real estate associated with relocating two high-performing company restaurants due to the impending loss of property control and \$6.0 million for the reacquisition of seven franchised restaurants and one former franchised restaurant, which was being remodeled and opened in the fourth quarter of fiscal 2017.

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

|   | Three Quarters Ended |                    |
|---|----------------------|--------------------|
|   | September 26, 2018   | September 27, 2017 |
|   | (In thousands)       |                    |
| Facilities                                    | \$7,440              | \$ 5,243           |
| New construction                              | 2,238                | 5,208              |
| Remodeling                                    | 3,608                | 1,521              |
| Information technology                        | 1,321                | 338                |
| Other   | 2,687                | 1,248              |
| Capital expenditures (excluding acquisitions) | \$17,294             | \$ 13,558          |

Capital expenditures and acquisitions for fiscal 2018 are expected to be approximately \$37 to \$39 million, including the above mentioned acquisition of franchised restaurants, the opening of a company restaurant, the anticipated acquisition of real estate through like-kind exchanges, remodels from recent franchise acquisitions, restaurant offsets and on-going maintenance capital.

Cash flows used in financing activities were \$20.9 million for the three quarters ended September 26, 2018, which included cash payments for stock repurchases of \$37.1 million, partially offset by net long-term debt borrowings of \$16.6 million. Cash flows used in financing activities were \$24.7 million for the three quarters ended September 27, 2017, which included cash payments for stock repurchases of \$66.0 million, partially offset by net long-term debt borrowings of \$40.8 million.

Our working capital deficit was \$43.0 million at September 26, 2018 compared to \$53.6 million at December 27, 2017. The decrease in working capital deficit was primarily related to a reduction of payables, accrued advertising and gift cards during the three quarters ended September 26, 2018. We are able to operate with a substantial working capital deficit because (1) restaurant operations and most food service operations are conducted primarily on a cash (and cash equivalent) basis with a low level of accounts receivable, (2) rapid turnover allows a limited investment in inventories, and (3) accounts payable for food, beverages and supplies usually become due after the receipt of cash from the related sales.

## Credit Facility

As of September 26, 2018, we had outstanding revolver loans of \$278.0 million and outstanding letters of credit under the senior secured revolver of \$19.8 million. These balances resulted in availability of \$102.2 million under the credit facility. The credit facility includes an accordion feature that would allow us to increase the size of the revolver to \$450 million. Prior to considering the impact of our interest rate swaps, described below, the weighted-average interest rate on outstanding revolver loans was 4.12% as of September 26, 2018. Taking into consideration our interest rate swaps, the weighted-average interest rate of outstanding revolver loans was 4.35% as of September 26, 2018.

A commitment fee, which is based on our consolidated leverage ratio, is paid on the unused portion of the credit facility and was 0.30% as of September 26, 2018. Borrowings under the credit facility bear a tiered interest rate, which is based on our consolidated leverage ratio and was set at LIBOR plus 200 basis points as of September 26, 2018. The maturity date for the credit facility is October 26, 2022.

The credit facility is available for working capital, capital expenditures and other general corporate purposes. The credit facility is guaranteed by Denny's and its material subsidiaries and is secured by assets of Denny's and its subsidiaries, including the stock of its subsidiaries (other than our insurance captive subsidiary). It includes negative covenants that are usual for facilities and transactions of this type. The credit facility also includes certain financial covenants with respect to a maximum consolidated leverage ratio and a minimum consolidated fixed charge coverage ratio. We were in compliance with all financial covenants as of September 26, 2018.

## Interest Rate Hedges

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

Under the interest rate swaps, we pay a fixed rate on the notional amount in addition to the current interest rate as determined by our consolidated leverage ratio in effect at the time. A summary of our interest rate swaps as of September 26, 2018 is as follows:

| Trade Date        | Effective Date | Maturity Date     | Notional Amount<br>(In thousands) | Fixed Rate |
|-------------------|----------------|-------------------|-----------------------------------|------------|
| March 20, 2015    | March 29, 2018 | March 31, 2025    | \$ 120,000                        | 2.44 %     |
| October 1, 2015   | March 29, 2018 | March 31, 2026    | 50,000                            | 2.46 %     |
| February 15, 2018 | March 31, 2020 | December 31, 2033 | 80,000                            | (1) 3.19 % |

(1) The notional amount of the swaps entered into on February 15, 2018 increases annually beginning September 28, 2020 until they reach the maximum notional amount of \$425.0 million on September 26, 2029.

As of September 26, 2018, the fair value of the interest rate swaps was a net asset of \$4.3 million, which is comprised of assets of \$5.2 million recorded as a component of other noncurrent assets and liabilities of \$0.9 million recorded as a component of other noncurrent liabilities in our Condensed Consolidated Balance Sheets.

## Implementation of New Accounting Standards



Information regarding the implementation of new accounting standards is incorporated by reference from Note 2 to our unaudited condensed consolidated financial statements set forth in Part I, Item 1 of this report.

Item 3. Quantitative and Qualitative Disclosures About Market Risk

With the exception of changes in the fair value of our interest rate swaps and the related expected reclassification from accumulated other comprehensive income, there have been no material changes in our quantitative and qualitative market risks since the prior reporting period. For additional information related to our interest rate swaps, including changes in the fair value, refer to Notes 8, 9 and 14 to our unaudited condensed consolidated financial statements in Part I, Item 1 of this report.

## Item 4. Controls and Procedures

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

There were no changes in our internal control over financial reporting identified in connection with the evaluation required by Rule 13a-15(d) of the Exchange Act that occurred during our last fiscal quarter that have materially affected, or are reasonably likely to materially affect, our internal control over financial reporting.

## PART II - OTHER INFORMATION

## Item 1. Legal Proceedings

Information regarding legal proceedings is incorporated by reference from Note 15 to our unaudited condensed consolidated financial statements set forth in Part I, Item 1 of this report.

## Item 1A. Risk Factors

There have been no material changes in the risk factors set forth in Part I, Item 1A, “Risk Factors” in our Annual Report on Form 10-K for the fiscal year ended December 27, 2017.

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

## Purchases of Equity Securities by the Issuer

The table below provides information concerning repurchases of shares of our common stock during the quarter ended September 26, 2018.

| Period                                   | Total<br>Number of<br>Shares<br>Purchased | Average<br>Price<br>Paid Per<br>Share <sup>(1)</sup> | Total  | Approximate  |
|--|---|--|--|--|
|  |   |  | Number of<br>Shares<br>Purchased<br>as Part of<br>Publicly<br>Announced<br>Programs <sup>(2)</sup> | Dollar Value<br>of Shares<br>that May<br>Yet be<br>Purchased<br>Under the<br>Programs <sup>(2)</sup> |
| (In thousands, except per share amounts) |   |  |  |  |
| June 28, 2018 - July 25, 2018            | 70  | \$ 15.82   | 70   | \$ 166,358   |
| July 26, 2018 - August 22, 2018          | 210                                       | 14.89  | 210  | \$ 163,235   |
| August 23, 2018 - September 26, 2018     | 295                                       | 14.66  | 295  | \$ 158,906   |

Total 575 \$ 14.88 575

(1) Average price paid per share excludes commissions.

On October 27, 2017, we announced that our Board of Directors approved a new share repurchase program, authorizing us to repurchase up to an additional \$200 million of our common stock (in addition to prior authorizations). Such repurchases may take place from time to time in the open market (including pre-arranged

(2) stock trading plans in accordance with the guidelines specified in Rule 10b5-1 under the Exchange Act) or in privately negotiated transactions, subject to market and business conditions. During the quarter ended September 26, 2018, we purchased 574,609 shares of our common stock for an aggregate consideration of approximately \$8.6 million pursuant to the share repurchase program.

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Item 6. Exhibits

The following are included as exhibits to this report:

| Exhibit No. | Description   |
|-------------|---|
| 10.1        | <u>Denny's Corporation Amended and Restated Executive and Key Employee Severance Pay Plan.</u>  |
| 10.2        | <u>First Amendment to Third Amended and Restated Credit Agreement dated June 26, 2018 among Denny's Inc., as the Borrower, Denny's Corporation, as Parent, and each of the Subsidiaries of Parent party thereto, as Guarantors, and Wells Fargo Bank, National Association, as Administrative Agent on behalf of the Lenders.</u>                 |
| 31.1        | <u>Certification of John C. Miller, President and Chief Executive Officer of Denny's Corporation, pursuant to Rule 13a-14(a), as adopted pursuant to Section 302 of the Sarbanes-Oxley Act of 2002.</u>   |
| 31.2        | <u>Certification of F. Mark Wolfinger, Executive Vice President, Chief Administrative Officer and Chief Financial Officer of Denny's Corporation, pursuant to Rule 13a-14(a), as adopted pursuant to Section 302 of the Sarbanes-Oxley Act of 2002.</u>   |
| 32.1        | <u>Certification of John C. Miller, President and Chief Executive Officer of Denny's Corporation, and F. Mark Wolfinger, Executive Vice President, Chief Administrative Officer and Chief Financial Officer of Denny's Corporation, pursuant to 18 U.S.C. Section 1350, as adopted pursuant to Section 906 of the Sarbanes-Oxley Act of 2002.</u> |
| 101.INS     | XBRL Instance Document  |
| 101.SCH     | XBRL Taxonomy Extension Schema Document   |
| 101.CAL     | XBRL Taxonomy Extension Calculation Linkbase Document   |
| 101.LAB     | XBRL Taxonomy Extension Label Linkbase Document   |
| 101.PRE     | XBRL Taxonomy Extension Presentation Linkbase Document  |
| 101.DEF     | XBRL Taxonomy Extension Definition Linkbase Document  |

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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.

DENNY'S CORPORATION

Date: October 30, 2018 By: /s/ F. Mark Wolfinger  
F. Mark Wolfinger  
Executive Vice President,  
Chief Administrative Officer and  
Chief Financial Officer

Date: October 30, 2018 By: /s/ Jay C. Gilmore  
Jay C. Gilmore  
Vice President,  
Chief Accounting Officer and  
Corporate Controller