



## **PIZZA PIZZA LIMITED**

Consolidated Financial Statements  
For the fifty-two weeks ended January 1, 2017 and fifty-three weeks  
ended January 3, 2016

## INDEPENDENT AUDITORS' REPORT

To the Shareholders of **Pizza Pizza Limited**

We have audited the accompanying consolidated financial statements of Pizza Pizza Limited, which comprise the consolidated statements of financial position as at January 1, 2017 and January 3, 2016 and the consolidated statements of income, comprehensive income, changes in shareholders' deficiency and cash flows for the 52-week period ended January 1, 2017 and 53-week period ended January 3, 2016 and a summary of significant accounting policies and other explanatory information.

### **Management's responsibility for the consolidated financial statements**

Management is responsible for the preparation and fair presentation of these consolidated financial statements in accordance with International Financial Reporting Standards, and for such internal control as management determines is necessary to enable the preparation of consolidated financial statements that are free from material misstatement, whether due to fraud or error.

### **Auditors' responsibility**


Our responsibility is to express an opinion on these consolidated financial statements based on our audits. We conducted our audits in accordance with Canadian generally accepted auditing standards. Those standards require that we comply with ethical requirements and plan and perform the audit to obtain reasonable assurance about whether the consolidated financial statements are free from material misstatement.

An audit involves performing procedures to obtain audit evidence about the amounts and disclosures in the consolidated financial statements. The procedures selected depend on the auditors' judgment, including the assessment of the risks of material misstatement of the consolidated financial statements, whether due to fraud or error. In making those risk assessments, the auditors consider internal control relevant to the entity's preparation and fair presentation of the consolidated financial statements in order to design audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the entity's internal control. An audit also includes evaluating the appropriateness of accounting policies used and the reasonableness of accounting estimates made by management, as well as evaluating the overall presentation of the consolidated financial statements.

We believe that the audit evidence we have obtained in our audits is sufficient and appropriate to provide a basis for our audit opinion.

### **Opinion**

In our opinion, the consolidated financial statements present fairly, in all material respects, the financial position of Pizza Pizza Limited as at January 1, 2017 and January 3, 2016 and its financial performance and cash flows for the 52-week period ended January 1, 2017 and 53-week period ended January 3, 2016 in accordance with International Financial Reporting Standards.



Chartered Professional Accountants  
Licensed Public Accountants

Toronto, Canada  
March 8, 2017

**Pizza Pizza Limited**  
**Consolidated Statements of Financial Position**  
**As at January 1, 2017 and January 3, 2016**  
**(Expressed in thousands of Canadian dollars)**

	January 1, 2017 \$	January 3, 2016 \$
<b>Assets</b>		
<b>Current assets</b>		
Cash and cash equivalents	13,024	14,360
Short-term investment	7,000	23,000
Trade and other receivables (note 3)	17,907	12,688
Inventories	6,161	6,041
Income taxes recoverable	5,017	-
Receivables from jointly-controlled companies (note 22)	2,702	1,182
Recoverable franchisee expenses (note 4)	3,876	9,662
<b>Total current assets</b>	<b>55,687</b>	<b>66,933</b>
<b>Non-current assets</b>		
Property, plant and equipment (note 5)	11,860	8,474
Notes receivable (note 6)	14,841	12,304
Renovation funds (note 7)	6,075	7,076
Deferred tax asset (note 15)	45,471	46,489
Investment in Pizza Pizza Royalty Limited Partnership (note 8)	23,648	23,562
Investment in jointly-controlled companies (note 9)	19,235	18,937
Intangible assets (note 10)	130	453
<b>Total non-current assets</b>	<b>121,260</b>	<b>117,295</b>
<b>Total assets</b>	<b>176,947</b>	<b>184,228</b>
<b>Liabilities and shareholders' deficiency</b>		
<b>Current liabilities</b>		
Trade and other payables (note 11)	43,558	43,490
Income taxes payable	-	7,651
Deposits from franchisees	2,486	2,370
Borrowings (note 12)	570	64
Provisions (note 13)	489	934
<b>Total current liabilities</b>	<b>47,103</b>	<b>54,509</b>
<b>Non-current liabilities</b>		
Borrowings (note 12)	747	357
Unearned vendor allowances	1,096	1,744
Advances from related party (note 22)	17,452	18,878
Leasehold inducements	8	10
Renovation funds (note 7)	3,227	2,438
Deferred gain (note 14)	203,879	206,209
<b>Total non-current liabilities</b>	<b>226,409</b>	<b>229,636</b>
<b>Shareholders' deficiency</b>		
Common shares and special voting shares (note 17)	-	-
Accumulated other comprehensive loss	(102)	(198)
Deficit	(96,463)	(99,719)
<b>Total shareholders' deficiency attributable to the shareholders</b>	<b>(96,565)</b>	<b>(99,917)</b>
<b>Total liabilities and shareholders' deficiency</b>	<b>176,947</b>	<b>184,228</b>
Commitments and contingencies (note 16)		

The accompanying notes are an integral part of these consolidated financial statements.

Approved by the Directors on March 8, 2017

**Pizza Pizza Limited**  
**Consolidated Statements of Income**  
**For the 52-week period ended January 1, 2017 and the 53-week period ended January 3, 2016**  
**(Expressed in thousands of Canadian dollars)**

	January 1, 2017 \$	January 3, 2016 \$
<b>Revenue</b>		
Food sales (note 19)	189,222	190,047
Royalties, franchise fees and other revenue (note 20)	30,104	29,889
<b>Total revenue</b>	<b>219,326</b>	<b>219,936</b>
Cost of food sales	(152,200)	(151,552)
General and administrative expenses (note 21)	(48,790)	(46,850)
Royalty payments	(35,333)	(34,808)
Equity income from Pizza Pizza Royalty Limited Partnership (note 8)	6,531	6,483
Equity income from jointly-controlled companies (note 9)	5,382	6,413
Gain on sale of Company-owned restaurants	331	131
<b>Operating loss</b>	<b>(4,753)</b>	<b>(247)</b>
Interest and other income	1,426	1,691
Amortization of deferred gain (note 14)	2,330	2,330
Gain on sale of Class B Partnership Units (note 8)	-	28,852
Income from Class D Partnership Units vend-in	-	38
Interest on borrowings	(56)	(60)
<b>Income (loss) for the period before income taxes</b>	<b>(1,053)</b>	<b>32,604</b>
Current income tax recovery (expense) (note 15)	5,290	(7,651)
Deferred tax recovery (expense) (note 15)	(981)	2,848
<b>Income for the period attributable to the shareholders of Pizza Pizza Limited</b>	<b>3,256</b>	<b>27,801</b>

**Pizza Pizza Limited**  
**Consolidated Statements of Comprehensive Income**  
**For the 52-week period ended January 1, 2017 and the 53-week period ended January 3, 2016**  
**(Expressed in thousands of Canadian dollars)**

	January 1, 2017 \$	January 3, 2016 \$
<b>Income for the period</b>	<b>3,256</b>	<b>27,801</b>
<b>Other comprehensive income (loss)</b>		
<i>Items that may be reclassified subsequently to net income:</i>		
Sale of Class B Partnership Units (note 8)	-	59
Share of other comprehensive income (loss) of the Pizza Pizza Royalty Limited Partnership (note 8)	140	(88)
Deferred tax impact of share of other comprehensive income (loss) of Pizza Pizza Royalty Limited Partnership	(44)	23
<i>Items that will not be reclassified subsequently to net income:</i>		
Employee benefits	-	534
Deferred tax impact of employee benefits	-	(143)
<b>Total comprehensive income attributable to shareholders</b>	<b>3,352</b>	<b>28,186</b>

The accompanying notes are an integral part of these consolidated financial statements.

**Pizza Pizza Limited**  
**Consolidated Statements of Changes in Shareholders' Deficiency**  
**For the 52-week period ended January 1, 2017 and the 53-week period ended January 3, 2016**  
**(Expressed in thousands of Canadian dollars)**

	Common shares and special voting shares (note 17) \$	Accumulated other comprehensive income (loss) \$	Deficit \$	Total \$
<b>As at January 3, 2016</b>	-	(198)	(99,719)	(99,917)
<b>Comprehensive income (loss)</b>				
Income for the 52-week period ended January 1, 2017	-	-	3,256	3,256
Employee benefits	-	-	-	-
Tax effect of employee benefits	-	-	-	-
Sale of Class B Partnership Units	-	-	-	-
Share of other comprehensive income on Pizza Pizza Royalty Limited Partnership's cash flow hedge	-	140	-	140
Tax effect of cash flow hedge	-	(44)	-	(44)
<b>Total comprehensive income</b>	-	96	3,256	3,352
<b>Transaction with shareholder</b>				
Dividend paid to shareholder	-	-	-	-
<b>As at January 1, 2017</b>	-	(102)	(96,463)	(96,565)
<b>As at December 28, 2014</b>	-	(192)	(88,911)	(89,103)
<b>Comprehensive income (loss)</b>				
Income for the 53-week period ended January 3, 2016	-	-	27,801	27,801
Employee benefits	-	-	534	534
Tax effect of employee benefits	-	-	(143)	(143)
Sale of Class B Partnership Units	-	59	-	59
Share of other comprehensive loss on Pizza Pizza Royalty Limited Partnership's cash flow hedge	-	(88)	-	(88)
Tax effect of cash flow hedge	-	23	-	23
<b>Total comprehensive income</b>	-	(6)	28,192	28,186
<b>Transaction with shareholder</b>				
Dividends paid to shareholder	-	-	(39,000)	(39,000)
<b>As at January 3, 2016</b>	-	(198)	(99,719)	(99,917)

The accompanying notes are an integral part of these consolidated financial statements.

**Pizza Pizza Limited**  
**Consolidated Statements of Cash Flows**  
**For the 52-week period ended January 1, 2017 and the 53-week period ended January 3, 2016**  
**(Expressed in thousands of Canadian dollars)**

	January 1, 2017 \$	January 3, 2016 \$
<b>Operating activities</b>		
Income for the period	3,256	27,801
Depreciation of property, plant and equipment (note 5)	2,852	2,459
Amortization of intangible assets (note 10)	323	376
Amortization of leasehold inducements	(2)	-
Amortization of unearned vendor allowances	(648)	(664)
Amortization of deferred gain (note 14)	(2,330)	(2,330)
Net provision for notes receivable (note 6)	(143)	(466)
Net provisions during the period (note 13)	(445)	459
Gain on sale of Company-owned restaurants	(331)	(131)
Net gain on sale of Class B Partnership Units (note 8)	-	(28,957)
Income from Class D vend-in	-	(38)
Equity income from Pizza Pizza Royalty Limited Partnership (note 8)	(6,531)	(6,483)
Equity income from jointly-controlled companies (note 9)	(5,382)	(6,413)
Deferred income tax expense (recovery) (note 15)	981	(2,848)
	<b>(8,400)</b>	<b>(17,235)</b>
Changes in non-cash operating elements of working capital (note 24)	(13,557)	15,991
<b>Cash used in operating activities</b>	<b>(21,957)</b>	<b>(1,244)</b>
<b>Investing activities</b>		
Additions to property, plant and equipment (note 5)	(7,331)	(4,704)
Additions to intangible assets (note 10)	-	(77)
Proceeds from sale of Company-owned restaurants	1,417	1,458
Net proceeds from sale of Class B Partnership Units	-	39,959
Proceeds from Class D Partnership Units vend-in	-	323
Distributions from Pizza Pizza Royalty Limited Partnership (note 8)	6,585	6,764
Dividends from jointly-controlled companies (note 9)	5,084	6,294
Repayment of notes receivable	8,024	7,415
Issuance of notes receivable	(10,418)	(7,987)
Contributions to renovation funds	13,500	11,566
Disbursement from renovation funds	(11,710)	(11,984)
Withdrawals from (additions to) short-term investments	16,000	(10,000)
<b>Cash provided by investing activities</b>	<b>21,151</b>	<b>39,027</b>
<b>Financing activities</b>		
Proceeds from borrowings	1,025	375
Repayments of borrowings	(129)	(368)
Repayment of advances from related party (note 22)	(3,193)	(40,477)
Advances from related party (note 22)	1,767	41,775
Dividend paid to shareholders (note 22)	-	(39,000)
<b>Cash used in financing activities</b>	<b>(530)</b>	<b>(37,695)</b>
<b>Increase in cash and cash equivalents</b>	<b>(1,336)</b>	<b>88</b>
Cash and cash equivalents, beginning of period	14,360	14,272
<b>Cash and cash equivalents, end of period</b>	<b>13,024</b>	<b>14,360</b>

See supplementary cash flow information (note 24)  
The accompanying notes are an integral part of these consolidated financial statements.

# Pizza Pizza Limited

## Notes to the Consolidated Financial Statements

For the 52-week period ended January 1, 2017 and 53-week period ended January 3, 2016

(In thousands of Canadian dollars except common shares, special voting shares and number of shares)

### 1. Nature of Business

Pizza Pizza Limited (“PPL” or the “Company”), a privately-held corporation incorporated by Articles of Incorporation under the *Business Corporations Act* (Canada) on December 27, 1989, operates in the food service industry primarily throughout Ontario and Alberta and primarily franchises and operates quick-service restaurant (“QSR”) businesses under the brand names of Pizza Pizza and Pizza 73. PPL derives revenue from franchises through the sale of franchise restaurants, food and beverages and royalties. PPL also derives revenue from Company-owned and managed restaurants through the sale of food products to retail customers.

PPL is incorporated and domiciled in Canada and the address of its registered office is 500 Kipling Avenue, Toronto, Ontario, Canada. The ultimate parent of PPL is the Flower Trust, a private Trust that does not prepare financial statements available for public use.

During the 52-week period ended January 1, 2017, PPL acquired 17 traditional franchises (53-week period ended January 3, 2016 – 8) and franchised 30 traditional restaurants (53-week period ended January 3, 2016 – 10). Below are the number of traditional and non-traditional franchisees and licensees as at:

	January 1, 2017	January 3, 2016
Franchisees and licensees	667	651
Jointly-controlled restaurants	75	74
Company-owned restaurants	10	14

### 2. Significant Accounting Policies

The principal accounting policies applied in the preparation of these consolidated financial statements are set out below. These policies have been consistently applied to all periods presented unless otherwise stated.

#### a) Fiscal year-end and interim period

PPL has a floating year-end on the Sunday closest to December 31; accordingly, interim periods consist of four 13-week periods with an additional week added to the last interim period every 5 to 6 years.

#### b) Basis of presentation

PPL prepares its consolidated financial statements in accordance with International Financial Reporting Standards (“IFRS”) as issued by the International Accounting Standards Board (“IASB”).

The policies applied in these consolidated financial statements are based on IFRS standards, which have been applied consistently to all periods presented. These consolidated financial statements were issued and effective as of March 8, 2017, the date the Directors approved the consolidated financial statements. The Directors have the power to amend the consolidated financial statements once issued, if required.

These consolidated financial statements have been prepared using the historical cost convention and on a going concern basis.

#### c) Changes in accounting policies and disclosure

*Standards, amendments and interpretations to existing standards that are not yet effective and have not yet been early adopted by PPL:*

##### IFRS 9, Financial Instruments (“IFRS 9”)

IFRS 9, Financial Instruments, as issued in 2014, introduces new requirements for the classification and measurement of financial instruments, a new expected-loss impairment model that will require more timely recognition of expected credit losses and a substantially reformed model for hedge accounting, with enhanced disclosures about risk management activity. IFRS 9 also removes the volatility in profit or loss that was caused by changes in an entity’s own credit risk for liabilities elected to be measured at fair value. IFRS 9 is effective for

# Pizza Pizza Limited

## Notes to the Consolidated Financial Statements

For the 52-week period ended January 1, 2017 and 53-week period ended January 3, 2016

(In thousands of Canadian dollars except common shares, special voting shares and number of shares)

annual periods beginning on or after January 1, 2018. Earlier application is permitted. PPL has not yet begun the process of evaluating the impact of this standard on its consolidated financial statements.

### IFRS 15, Revenue from Contracts with Customers (“IFRS 15”)

In May 2014, the IASB issued IFRS 15, which covers principles for reporting about the nature, amount, timing and uncertainty of revenue and cash flows arising from contracts with customers. The standard contains a single model that applies to contracts with customers and two approaches to recognizing revenue: at a point in time or over time. The model features a contract-based five-step analysis of transactions to determine whether, how much and when revenue is recognized. New estimates and judgmental thresholds have been introduced, which may affect the amount and/or timing of revenue recognized. IFRS 15 becomes effective for annual periods beginning on or after January 1, 2018. The new revenue standards may be applied retrospectively to each prior period presented or retrospectively with the cumulative effect recognized as of the date of adoption. PPL is in the process of reviewing the standard to determine the impact on the consolidated financial statements.

### IFRS 16, Leases (“IFRS 16”)

In January 2016, the IASB has issued IFRS 16, Leases, its new leases standard that requires lessees to recognize assets and liabilities for most leases on their balance sheets. Lessees applying IFRS 16 will have a single accounting model for all leases, with certain exemptions. Lessor accounting is substantially unchanged. The new standard will be effective from January 1, 2019 with limited early application permitted. PPL has not yet begun the process of evaluating the impact of this standard on its consolidated financial statements.

#### d) Basis of consolidation

These consolidated financial statements incorporate the assets and liabilities of PPL and its subsidiaries as at January 1, 2017 and January 3, 2016 and the results of these entities for the 52-week and 53-week periods ended January 1, 2017 and January 3, 2016, respectively.

PPL consolidates the results of its investments over which it exercises control. Specifically, an investor controls an investee when it has power over the investee, it is exposed, or has rights, to variable returns from its involvement with the investee and has the ability to affect those returns through its power over the investee. Subsidiaries are fully consolidated from the date on which control is transferred to PPL and deconsolidated from the date that control ceases. Inter-entity transactions, balances and unrealized gains/losses on transactions between entities are eliminated.

#### *Investment in associate*

An associate is an entity over which the Company has significant influence. Significant influence is the power to participate in the financial and operating policy decisions of the investee, but is not control or joint control over those policies.

PPL accounts for its 21.1% (January 3, 2016 – 20.4%) share interest in the Pizza Pizza Royalty Limited Partnership (the “Partnership”) as an investment in an associate and applies equity accounting whereby PPL’s investment is increased by its 21.1% share of income for the period of the Partnership and reduced for distributions received during the Partnership’s fiscal period. The Partnership’s financial and fiscal periods differ from PPL’s, as the Partnership operates on a calendar year-end.

PPL assesses at each period-end whether there is any objective evidence that its interest in the Partnership is impaired. If impaired, the carrying value of PPL’s share of the underlying assets of the Partnership is written down to its estimated recoverable amount, being the higher of fair value less cost to sell and value in use, and the write-down is charged to the consolidated statements of income.

#### *Investments in joint ventures*

A joint venture is a type of joint arrangement whereby the parties that have joint control of the arrangement have rights to the net assets of the joint venture. Joint control is the contractually agreed sharing of control of an arrangement, which exists only when decisions about the relevant activities require unanimous consent of the parties sharing control.



# Pizza Pizza Limited

## Notes to the Consolidated Financial Statements

For the 52-week period ended January 1, 2017 and 53-week period ended January 3, 2016

(In thousands of Canadian dollars except common shares, special voting shares and number of shares)

PPL accounts for its 50% (January 3, 2016 – 50%) share interest in the 75 jointly-controlled companies as an investment in a joint venture and applies equity accounting whereby PPL's investment is increased by its 50% share of income for the period of the joint ventures and reduced for distributions received during the joint ventures' fiscal period. The jointly-controlled companies' financial and fiscal periods differ from PPL's, as the joint ventures have a floating year-end of the Saturday immediately preceding July 31.

PPL assesses at each period-end whether there is any objective evidence that its interest in the joint ventures is impaired. If impaired, the carrying value of PPL's share of the underlying assets of the joint ventures is written down to its estimated recoverable amount, being the higher of fair value less cost to sell and value in use, and the write-down is charged to the consolidated statements of income.

e) Functional and presentation currency

Items included in the consolidated financial statements are measured using the currency of the primary economic environment in which PPL operates (the functional currency). These consolidated financial statements are presented in Canadian dollars, which is PPL's functional and presentation currency.

f) Financial assets and liabilities

A financial asset or liability is recognized if PPL becomes a party to the contractual provisions of the asset or liability. A financial asset or liability is recognized initially (at the trade date) at its fair value plus, in the case of a financial asset or liability not at fair value through profit or loss, transaction costs that are directly attributable to the acquisition or issue of the instrument. Financial assets and liabilities carried at fair value through profit or loss are initially recognized at fair value and transaction costs are expensed in the consolidated statements of income.

After initial recognition, financial assets are measured at their fair values, except for loans and receivables and held to maturity financial assets, which are measured at amortized cost. After initial recognition, financial liabilities are measured at amortized cost except for financial liabilities at fair value through profit or loss, which are measured at fair value.

PPL classifies its financial assets and liabilities according to their characteristics and management's intentions related thereto for the purposes of ongoing measurement.

Classification choices for financial assets include:

- i. Fair value through profit or loss - measured at fair value with changes in fair value recorded in the consolidated statements of income;
- ii. Held to maturity - recorded at amortized cost with gains and losses recognized in the consolidated statements of income in the period in which the financial asset is no longer recognized or impaired;
- iii. Available for sale - measured at fair value with changes in fair value recognized in other comprehensive Income (loss) for the current period until realized through disposal or impairment; and
- iv. Loans and receivables - recorded at amortized cost with gains and losses recognized in profit in the period in which the financial asset is no longer recognized or impaired.

Classification choices for financial liabilities include:

- i. Fair value through profit or loss - measured at fair value with changes in fair value recorded in the consolidated statements of income; and
- ii. Other financial liabilities - measured at amortized cost with gains and losses recognized in the consolidated statements of income in the period in which the financial liability is no longer recognized.

# Pizza Pizza Limited

## Notes to the Consolidated Financial Statements

For the 52-week period ended January 1, 2017 and 53-week period ended January 3, 2016

(In thousands of Canadian dollars except common shares, special voting shares and number of shares)

PPL's financial assets and liabilities are classified and measured as follows:

<b>Assets/liabilities</b>	<b>Category</b>	<b>Measurement</b>
Cash and cash equivalents	Loans and receivables	Amortized cost
Short-term-investment	Loans and receivables	Amortized cost
Trade and other receivables	Loans and receivables	Amortized cost
Receivables from jointly-controlled companies	Loans and receivables	Amortized cost
Recoverable franchisee expenses	Loans and receivables	Amortized cost
Notes receivable	Loans and receivables	Amortized cost
Renovation funds	Loans and receivables	Amortized cost
Trade and other payables	Other financial liabilities	Amortized cost
Deposits from franchisees	Other financial liabilities	Amortized cost
Borrowings	Other financial liabilities	Amortized cost
Advances from related party	Other financial liabilities	Amortized cost

Financial assets are derecognized if PPL's contractual rights to the cash flows from the financial assets expire or if PPL transfers the financial asset to another party without retaining control or substantially all risks and rewards of the asset. Financial liabilities are derecognized if PPL's obligations specified in the contract expire or are discharged or cancelled.

### g) Impairment of financial assets

PPL assesses at the end of each reporting period whether there is objective evidence that a financial asset or group of financial assets is impaired. A financial asset or group of financial assets is impaired and impairment losses are incurred only if there is objective evidence of impairment as a result of one or more events that occurred after the initial recognition of the asset (a loss event) and that loss event has an impact on the estimated future cash flows of the financial asset or group of financial assets that can be reliably estimated.

In the case of financial assets measured at amortized cost, the amount of the loss is measured as the difference between the asset's carrying amount and the present value of estimated future cash flows discounted at the financial asset's original effective interest rate. The asset's carrying amount is reduced and the amount of the loss is recognized in the consolidated statements of income. If, in a subsequent period, the amount of the impairment loss decreases and the decrease can be related objectively to an event occurring after the impairment was recognized, the reversal of the previously recognized impairment is recognized in the consolidated statements of income.

### h) Cash and cash equivalents

Cash and cash equivalents consist of cash and short-term deposits with a maturity at acquisition of less than 90 days.

### i) Short-term investment

The short-term investment includes amounts invested in a Guaranteed Investment Certificate with a maturity at acquisition between 90 and 365 days.

### j) Trade and other receivables

Trade and other receivables are amounts due for the sale of goods to franchises and jointly-controlled entities, prepayments, and customer rebate from non-franchisees. If collection is expected in one year or less, they are classified as current assets. If not, they are presented as non-current assets. Trade and other receivables are initially recognized at fair value and subsequently measured at amortized cost using the effective interest method, less provision for impairment.

### k) Inventories

Inventories consist of food, supplies, and construction materials available to be sold to restaurants. Inventories are valued at the lower of cost and net realizable value. Cost is determined on the first-in, first-out basis.

# Pizza Pizza Limited

## Notes to the Consolidated Financial Statements

For the 52-week period ended January 1, 2017 and 53-week period ended January 3, 2016

(In thousands of Canadian dollars except common shares, special voting shares and number of shares)

l) Notes receivable

Notes receivable are amounts due from franchisees bearing interest at agreed interest rates. Notes are classified as non-current taking into consideration their nature and management's intention with respect to timing of recovery of these balances.

Notes receivable are initially recognized at fair value and subsequently measured at amortized cost using the effective interest method, less provision for impairment.

m) Recoverable franchisee expenses

PPL provides advertising and order processing services to Pizza Pizza and Pizza 73 restaurants. Expenses related to the provision of these services are paid by PPL. PPL recovers advertising expenses based on a percentage of individual restaurant sales and order processing service expenses based on the number of orders directed to the restaurant. Recoveries from franchisees are recorded as a reduction of the related expenses. To the extent that expenses recovered exceed or are less than expenses paid by PPL, the difference is recorded as a payable or a receivable.

In addition to providing advertising and order processing services to Pizza 73 restaurants, PPL also operates two Pizza 73 commissaries. A consulting agreement controls the markup on food sales, which is designed to cover the expenses of the commissary operations. Recoveries are recorded as a reduction of the related expenses. To the extent that expenses recovered exceed or are less than expenses paid by PPL, the difference can be allocated annually to individual restaurants based on a percentage of individual restaurant sales.

n) Property, plant and equipment

*Owned assets*

Property, plant and equipment are stated at historical cost less accumulated depreciation and impairment losses, if any. Historical cost includes expenditures that are directly attributable to the acquisition or construction of items. Subsequent costs are included in the asset's carrying amount or recognized as a separate asset, as appropriate, only when it is probable that future economic benefits associated with the asset will flow to PPL and the cost can be measured reliably. The carrying amount of any replaced part is derecognized. All other repairs and maintenance are charged to the consolidated statements of income during the period in which they are incurred.

*Leased assets*

Operating lease payments are recognized as an expense on a straight-line basis over the period of the lease.

*Depreciation*

Depreciation is calculated on a straight-line or declining balance basis to allocate the cost of the asset, less any residual value, over its estimated useful life. The depreciation method and range of estimated useful lives for each class of property, plant and equipment are as follows:

On the declining balance method -

Equipment	20%
Furniture and fixtures	20%
Vehicles	30%

On the straight-line method -

Leasehold improvements	5 years
Computer - software	3 years
- hardware	4 years
Company-owned restaurant assets	5 years

PPL allocates the amount initially recognized in respect of an item of property, plant and equipment to its significant components and depreciates separately each such component. Residual values, method of depreciation and useful lives of items of property, plant and equipment are reviewed annually and adjusted if appropriate.

# Pizza Pizza Limited

## Notes to the Consolidated Financial Statements

For the 52-week period ended January 1, 2017 and 53-week period ended January 3, 2016

(In thousands of Canadian dollars except common shares, special voting shares and number of shares)

Gains and losses on disposals of property, plant and equipment are determined by comparing the proceeds with the carrying amount of the asset and are included as part of general and administrative expenses in the consolidated statements of income.

o) Intangible assets

Intangible assets are assets acquired that lack physical substance and that meet the specified criteria for recognition. Intangible assets with a finite life are recorded at cost and are amortized over the period of expected future benefit on the straight-line method:

Lease agreements	10 years
Computer software	3 years

p) Impairment of non-financial assets

The Company assesses at each reporting date whether there is an indication that an asset may be impaired. If any indication exists, or when annual impairment testing for an asset is required, the Company estimates the asset's recoverable amount. The recoverable amount is the higher of an asset's fair value less costs to sell and its value in use. For the purposes of assessing impairment, assets are grouped at the lowest levels for which there are separately identifiable cash flows. Specifically, assets are grouped at the cash-generating unit ("CGU") level, namely Pizza Pizza restaurants and Pizza 73 restaurants. In determining fair value less costs to sell, recent market transactions are taken into account, if available. In assessing value in use, the estimated further cash flows are discounted to their present value using a pre-tax discount rate that reflects current market assessments of the time value of money and the risks specific to the asset. An impairment loss is recognized for the amount by which the asset's carrying amount exceeds its recoverable amount. Impairment losses are recognized in the consolidated statements of income.

The Company bases its impairment calculation on detailed budgets that are prepared for each of the CGUs and generally cover a period of one year. For longer periods, a long-term growth rate is calculated and applied to project future cash flows after the one-year period.

An assessment is made at each reporting date whether there is any indication that previously recognized impairment losses may no longer exist or may have decreased. If such indication exists, the Company estimates the asset's recoverable amount. A previously recognized impairment loss is reversed only if there has been a change in the assumptions used to determine the asset's recoverable amount since the last impairment loss was recognized. The reversal is limited so that the carrying amount of the asset does not exceed its recoverable amount, nor exceed the carrying amount that would have been determined, net of depreciation, had no impairment loss been recognized for the asset in prior years. Such reversal is recognized in the consolidated statements of income.

q) Renovation funds

PPL maintains a long-term renovation program whereby franchisees contribute towards future restaurant renovations and upgrades. The franchise owner acknowledges that the renovation fund contribution may be used by PPL, without interest or other compensation to the franchise owner, to fund the renovation, expansion or relocation of other Pizza Pizza outlets until such time as the funds are required by the franchise owner for renovation, expansion or relocation of the franchised outlet.

r) Deferred franchise costs

Certain costs related to the construction of new franchised locations are deferred and amortized over the term of the franchise agreement, generally being five years.

s) Income taxes

Income tax expense for the period is comprised of current and deferred tax. Income taxes are recognized in the consolidated statements of income except to the extent it relates to items recognized directly in equity.

*Current income taxes*

Current income tax expense is based on the income for the period as adjusted for items that are not taxable or not deductible. Current income taxes are calculated using tax rates and tax laws that were substantively enacted

# Pizza Pizza Limited

## Notes to the Consolidated Financial Statements

For the 52-week period ended January 1, 2017 and 53-week period ended January 3, 2016

(In thousands of Canadian dollars except common shares, special voting shares and number of shares)

at the end of the reporting periods. Management periodically evaluates positions taken in tax returns with respect to situations in which applicable tax regulation is subject to interpretation. Provisions are established, where appropriate, on the basis of amounts expected to be paid to the tax authorities.

### *Deferred taxes*

Deferred taxes are recognized, using the liability method, on temporary differences arising between the tax bases of assets and liabilities and their carrying amounts in the consolidated financial statements. Deferred taxes are determined using tax rates (and tax laws) that have been enacted or substantively enacted by the consolidated statement of financial position dates and are expected to apply when the related deferred tax asset is realized or the deferred tax liability is settled. The measurement of deferred tax assets and liabilities reflect the tax consequences that would follow from the manner in which PPL expects, at the end of the reporting period, to recover or settle the carrying amount of its assets and liabilities.

Deferred tax assets are recognized only to the extent that it is probable that future taxable income will be available against which the temporary differences can be utilized.

Deferred tax assets and liabilities are offset when there is a legally enforceable right to offset current taxes and when the deferred tax assets and liabilities relate to income taxes levied by the same taxation authority where there is an intention to settle the balances on a net basis.

### t) Trade and other payables

Trade and other payables are obligations to pay for goods or services that have been acquired in the ordinary course of business from suppliers. Trade and other payables are classified as current liabilities if payment is due within one year or less.

### u) Borrowings

Borrowings are initially recognized at fair value net of any financing fees. Borrowings are classified as current liabilities unless PPL has an unconditional right to defer settlement of the liability for more than 12 months. After initial recognition, borrowings are carried at amortized cost with any difference between the proceeds (net of financing fees) and the redemption value recognized in the consolidated statements of income over the period of the borrowing using the effective interest method.

### v) Provisions

Provisions represent liabilities to PPL for which the amount or timing is uncertain. Provisions are recognized when PPL has a present legal or constructive obligation as a result of past events, it is probable that an outflow of resources will be required to settle the obligation, and the amount has been reliably estimated. Provisions are not recognized for future operating losses.

Provisions are measured at the present value of the expenditures expected to be required to settle the obligation using a discount rate that reflects current market assessments of the time value of money and the risks specific to the obligation. The increase in the provision due to the passage of time is recognized in the consolidated statements of income.

### w) Unearned vendor allowances

Unearned vendor allowances relate to an allowance received from a supplier in consideration of the achievement of certain volume commitments. The unearned vendor allowances are being amortized based on the proportion of volume commitments met during each period.

### x) Common shares and special voting shares

Common shares and special voting shares are classified as equity. Incremental costs directly attributable to the issuance of new shares are shown in equity as a deduction, net of income taxes, from the proceeds.

# Pizza Pizza Limited

## Notes to the Consolidated Financial Statements

For the 52-week period ended January 1, 2017 and 53-week period ended January 3, 2016

(In thousands of Canadian dollars except common shares, special voting shares and number of shares)

y) Revenue recognition

PPL recognizes revenue on the following basis:

- Food sales are recognized when the products are delivered to the franchised and jointly-controlled restaurants. Pizza Pizza franchisees and joint ventures are required to purchase from Pizza Pizza, at an agreed markup on cost, all of the raw materials and supplies used and sold in their Pizza Pizza restaurants. Payment for materials and supplies are due within seven days.
- Company-owned and managed restaurant retail sales are recognized when the services are rendered and the products are sold to the public. Payment by the public is immediate.
- Franchise royalties and administration and accounting fees are recognized as earned and are based on a percentage of the franchisees' sales as provided for in individual franchise agreements. Royalties are due within seven days.
- Initial and renewal franchise fees are recognized at the commencement of the initial term of the franchise agreement and upon the renewal of such an agreement. The initial franchise fee is payable, in full, at the commencement of the agreement and is non-refundable. The renewal fee is charged to franchisees upon renewal of their franchise agreement, which is typically five years from the initial agreement.
- Construction fees are recognized when the costs are incurred. Fees are generated by PPL acting as general contractor as per the franchise agreement.
- Interest and other income is recognized and accrued when earned. Interest income is derived from notes receivable with franchisees and investments in cash equivalents that have maturity dates less than 90 days.

z) Critical accounting estimates and assumptions

PPL makes estimates and assumptions concerning the future. The resulting accounting estimates will, by definition, seldom equal the related actual results. The estimates and assumptions that have a significant risk of causing a material adjustment to the carrying amounts of assets and liabilities within the next financial period are addressed below:

*Impairment of investment in Pizza Pizza Royalty Limited Partnership*

PPL, at each period-end, identifies impairment indicators and assesses whether there is any objective evidence that its interest in the Partnership is impaired. If impaired, the carrying value of PPL's share of the underlying assets of the Partnership is written down to its estimated recoverable amount, being the higher of fair value less cost to sell and value in use, and the write-down is charged to the consolidated statements of income.

The value-in-use calculation requires the Company to estimate the future cash flows expected to arise from the Partnership and a suitable discount rate in order to calculate present value. In measuring future cash flows, PPL makes assumptions about future sales and terminal growth rates that are based on historical experience and expected future performance. Determining the applicable discount rate also involves estimating appropriate adjustments to market risk and PPL specific risk factors. The two most sensitive assumptions are pre-tax discount rates and terminal growth rates.

*Impairment of investment in jointly-controlled companies*

PPL, at each period-end, identifies impairment indicators and assesses whether there is any objective evidence that its interest in the joint ventures is impaired. If impaired, the carrying value of PPL's share of the underlying assets of the joint ventures is written down to its estimated recoverable amount, being the higher of fair value less cost to sell and value in use, and charged to the consolidated statements of income.

The value-in-use calculation requires the Company to estimate the future cash flows expected to arise from the CGU and a suitable discount rate in order to calculate present value. In measuring future cash flows, PPL makes

# Pizza Pizza Limited

## Notes to the Consolidated Financial Statements

For the 52-week period ended January 1, 2017 and 53-week period ended January 3, 2016

(In thousands of Canadian dollars except common shares, special voting shares and number of shares)

assumptions about future sales, tax rates, and terminal growth rates that were based on historical experience and expected future performance. Determining the applicable discount rate also involves estimating appropriate adjustments to market risk and PPL specific risk factors. The two most sensitive assumptions used are pre-tax discount rates and terminal growth rates.

### *Impairment of non-trade assets*

PPL, at each period-end, identifies impairment indicators and assesses whether there is any objective evidence that its non-trade assets are impaired. If impaired, the carrying value of these assets is written down to its estimated recoverable amount, and charged to the consolidated statements of income.

### aa) Critical judgments

#### *Consolidation*

Determining which entities are to be consolidated by PPL requires judgment on the definition of control. The definition of control under IFRS 10, Consolidated Financial Statements ("IFRS 10"), states that an investor controls an investee when it has power over the investee, is exposed, or has rights, to variable returns from its involvement with the investee and has the ability to affect those returns through its power over the investee. Based on an assessment of the activities of the Partnership and the franchisees, it was concluded that PPL does not control these entities, and therefore shall not consolidate their operations. The Partnership is consolidated by Pizza Pizza Royalty Corp ("PPRC"), formerly Pizza Pizza Royalty Income Fund (the "Fund").

#### *Identification of CGUs*

For the purposes of identifying CGUs, assets are grouped at the lowest levels for which there are separately identifiable cash flows. PPL concludes there are interdependencies of cash flows between Pizza 73 restaurants and PPL and therefore, the investment in jointly-controlled Pizza 73 restaurants is considered a single CGU. PPL's assets pertaining to Pizza Pizza operations are classified as a separate CGU.

#### *Sale of Rights and Marks and annual vend-ins*

PPL has applied judgment in assessing the application of the revenue recognition accounting policy for the initial sale of Rights and Marks, described in note 14, and the annual vend-ins of restaurants in the Royalty Pool (note 8). In making its assessment, management considered the substance of these transactions and whether the risks and rewards of ownership have been transferred. Based on this assessment, management has determined that revenue relating to the sale will be deferred and amortized as earned and that the subsequent vend-ins will have no impact on PPL. Cash in lieu of vend-ins is considered as proceeds of disposition of the contractual right to an increase in the Exchange Multiplier and is taken to income when due.

### 3. Trade and Other Receivables

	As at January 1, 2017	As at January 3, 2016
Trade receivables	12,709	9,498
Less: provision for impairment of trade receivables	(427)	(1,136)
Trade receivables less provision for impairment	12,282	8,362
Prepayments and other receivables	5,625	4,326
<b>Total trade and other receivables</b>	<b>17,907</b>	<b>12,688</b>

# Pizza Pizza Limited

## Notes to the Consolidated Financial Statements

For the 52-week period ended January 1, 2017 and 53-week period ended January 3, 2016

(In thousands of Canadian dollars except common shares, special voting shares and number of shares)

	For the 52-week period ended January 1, 2017	For the 53-week period ended January 3, 2016
<b>Movements in the provision for impairment of trade receivables</b>		
Opening balance	1,136	1,305
Provisions made during the period	-	1,069
Utilization of the impairment provision	(709)	(1,238)
<b>Closing balance</b>	<b>427</b>	<b>1,136</b>

The establishment and release of the provision for impaired trade receivables have been included within general and administrative expenses in the consolidated statements of income. Amounts charged to the provision are generally written off when there is no expectation of recovering additional cash. The other classes within trade and other receivables do not contain impaired assets and accordingly, no amounts were written off during the period.

#### 4. Recoverable Franchisee Expenses

	For the 52-week period ended January 1, 2017	For the 53-week period ended January 3, 2016
<b>Movements in recoverable franchisee expenses</b>		
Opening balance	9,662	10,762
Receipts and contributions	(84,115)	(88,804)
Provision for impairment of recoverable franchisee expenses	(9,850)	(3,500)
Disbursements	88,179	91,204
<b>Closing balance</b>	<b>3,876</b>	<b>9,662</b>

#### 5. Property, Plant and Equipment

	Equipment	Furniture and fixtures	Vehicles	Leasehold improvements	Computer hardware and software	Company- owned restaurant assets	Total
<b>52-week period ended January 1, 2017</b>							
Opening net book value	1,742	55	28	754	511	5,384	8,474
Additions	270	-	-	213	792	6,056	7,331
Disposals	(10)	-	(5)	-	-	(1,078)	(1,093)
Depreciation charge	(360)	(11)	(7)	(288)	(360)	(1,826)	(2,852)
<b>Closing net book value</b>	<b>1,642</b>	<b>44</b>	<b>16</b>	<b>679</b>	<b>943</b>	<b>8,536</b>	<b>11,860</b>
Cost	14,979	1,124	491	9,862	14,562	22,841	63,859
Accumulated depreciation	(13,337)	(1,080)	(475)	(9,183)	(13,619)	(14,305)	(51,999)
<b>Net book value</b>	<b>1,642</b>	<b>44</b>	<b>16</b>	<b>679</b>	<b>943</b>	<b>8,536</b>	<b>11,860</b>



# Pizza Pizza Limited

## Notes to the Consolidated Financial Statements

For the 52-week period ended January 1, 2017 and 53-week period ended January 3, 2016

(In thousands of Canadian dollars except common shares, special voting shares and number of shares)

	Equipment	Furniture and fixtures	Vehicles	Leasehold improvements	Computer hardware and software	Company-owned restaurant assets	Total
<b>52-week period ended January 3, 2016</b>							
Opening net book value	1,813	70	40	842	885	3,906	7,556
Additions	302	-	-	165	135	4,102	4,704
Disposals	-	-	(6)	-	-	(1,321)	(1,327)
Depreciation charge	(373)	(15)	(6)	(253)	(509)	(1,303)	(2,459)
<b>Closing net book value</b>	<b>1,742</b>	<b>55</b>	<b>28</b>	<b>754</b>	<b>511</b>	<b>5,384</b>	<b>8,474</b>
<b>As at January 3, 2016</b>							
Cost	14,761	1,124	540	9,649	13,770	18,481	58,325
Accumulated depreciation	(13,019)	(1,069)	(512)	(8,895)	(13,259)	(13,097)	(49,851)
<b>Net book value</b>	<b>1,742</b>	<b>55</b>	<b>28</b>	<b>754</b>	<b>511</b>	<b>5,384</b>	<b>8,474</b>

Depreciation in the amount of \$388 (53-week period ended January 3, 2016 - \$558) for the 52-week period ended January 1, 2017 has been recovered from franchisees. Accumulated depreciation of \$704 on disposals (January 3, 2016 - \$387) has been removed from accumulated depreciation on property plant and equipment as at January 1, 2017.

## 6. Notes Receivable

	As at January 1, 2017	As at January 3, 2016
From franchisees, bearing interest from 5% to 9% (January 3, 2016 – 5% to 9%)	8,859	9,180
From franchisees, non-interest bearing	6,995	4,280
Less: provision for impairment of notes receivable	(1,013)	(1,156)
<b>Total notes receivable</b>	<b>14,841</b>	<b>12,304</b>

The notes receivable from franchisees are unsecured and are repayable in varying monthly principal amounts. The effective interest rate on the notes receivable as at January 1, 2017 is 6.4% (January 3, 2016 – 6.5%).

	For the 52-week period ended January 1, 2017	For the 53-week period ended January 3, 2016
<b>Movements in the provision for impairment of notes receivable</b>		
Opening balance	1,156	1,622
Provisions made during the period	431	275
Utilization of the impairment provision	(574)	(741)
<b>Closing balance</b>	<b>1,013</b>	<b>1,156</b>

## 7. Renovation Funds

The renovation funds are non-interest bearing and are collected from franchisees on a monthly basis at amounts based on a percentage of sales.

# Pizza Pizza Limited

## Notes to the Consolidated Financial Statements

For the 52-week period ended January 1, 2017 and 53-week period ended January 3, 2016

(In thousands of Canadian dollars except common shares, special voting shares and number of shares)

### 8. Investment in Pizza Pizza Royalty Limited Partnership

- a) PPL owns Class B and Class D Partnership Units that are exchangeable for PPRC shares based on the Exchange Multiplier applicable at the exchange date and represent an effective 21.1% interest in the Partnership as at January 1, 2017 (January 3, 2016 – 20.4%).

The table below reconciles the balance of PPL's investment in the Partnership, which is accounted for using equity accounting.

	For the 52-week period ended January 1, 2017	For the 53-week period ended January 3, 2016
Balance – beginning of period	23,562	34,874
Equity income of the Partnership	6,531	6,483
Distributions received from Partnership	(6,585)	(6,764)
Share of Partnership other comprehensive income (loss)	140	(88)
Disposal of Class B Partnership Units	-	(10,943)
<b>Balance – end of period</b>	<b>23,648</b>	<b>23,562</b>

The business of the Partnership is the ownership and licensing of the Pizza Pizza and Pizza 73 Rights and Marks through two separate Licence and Royalty Agreements with PPL. Additionally, the Partnership will collect the royalty payable under each Licence and Royalty Agreement as well as perform the administration of PPRC pursuant to the Administration Agreement.

A breakdown of the Partnership's aggregated assets, liabilities, revenue and profit is as follows:

	As at December 31, 2016	As at December 31, 2015
Total assets	345,045	341,357
Total liabilities	80,133	81,282

	For the 52-week period ended December 31, 2016	For the 52-week period ended December 31, 2015
Revenue	35,333	34,808
Profit for the period	33,790	31,792

- b) 2015 Royalty Pool Adjustment – Class B Exchange Multiplier

In early January 2016, adjustments to royalty payments and PPL's Class B Exchange Multiplier were made based on the actual performance of the 23 new restaurants added to the Royalty Pool on January 1, 2015. As a result of the adjustments, the new Class B Exchange Multiplier is 1.796297 and Class B Units can be exchanged for 4,505,541 shares, which is an increase of 17,641 shares, effective January 1, 2015.

# Pizza Pizza Limited

## Notes to the Consolidated Financial Statements

For the 52-week period ended January 1, 2017 and 53-week period ended January 3, 2016

(In thousands of Canadian dollars except common shares, special voting shares and number of shares)

c) 2015 Royalty Pool Adjustment – Class D Exchange Multiplier

In early January 2016, adjustments to royalty payments and PPL's Class D Exchange Multiplier were made based on the actual performance of the eight Pizza 73 restaurants added to the Royalty Pool on January 1, 2015. As a result of the adjustments, the new Class D Exchange Multiplier is 17.07332 and Class D Units can be exchanged for 1,707,332 shares, which is an increase of 71,099 shares, effective January 1, 2015.

d) Sale of Class B Partnership Units

On March 23, 2015, PPL entered into an underwriting agreement for the sale of 2,800,000 shares of the PPRC at a price of \$15.00 per share for gross proceeds of \$42,000. In order to provide the 2,800,000 shares of PPRC to the underwriters, PPL exchanged 1,564,889 of its Class B Units of the Partnership, applying the Class B Exchange Multiplier of 1.789264. PPL's ownership of the PPRC's fully diluted shares decreased from 29.0% to 19.9% as a result of this transaction.

e) 2016 Royalty Pool Adjustment – Class B Exchange Multiplier

On January 1, 2016, six net Pizza Pizza restaurants were added to the Royalty Pool as a result of 24 new restaurants opening and 18 closing from January 1, 2015 to December 31, 2015. The additional system sales from the 24 new restaurants are estimated at \$4,887 annually less sales of \$3,630 from 18 permanently closed Pizza Pizza restaurants resulting in net estimated Pizza Pizza sales of \$1,257 added to the Royalty Pool. The total number of Pizza Pizza restaurants in the Royalty Pool has increased to 636. The yield of the shares was determined to be 5.89% calculated using \$13.85 as a weighted average share price. Weighted average share price is calculated based on the market price of the shares traded on the Toronto Stock Exchange during the period of twenty consecutive days ending on the fifth trading day before January 1, 2016. As a result of the contribution of the additional net sales to the Royalty Pool, the Class B Exchange Multiplier increased fractionally by 80% of the total adjustment or 0.021529; the new Class B Exchange Multiplier is 1.817826. This adjustment will also increase the entitlement of the holders of the Class B Units to distributions of cash and allocations of income from the Partnership. The second adjustment to the Class B Exchange Multiplier will be adjusted to be effective January 1, 2016, once the actual performance of the new restaurants is determined in early 2017.

In early January 2017, adjustments to royalty payments and PPL's Class B Exchange Multiplier were made based on the actual performance of the 24 new restaurants added to the Royalty Pool on January 1, 2016. As a result of the adjustments, the new Class B Exchange Multiplier is 1.819988 and Class B Units can be exchanged for 4,564,964 shares, which is an increase of 5,422 shares, effective January 1, 2016.

f) 2016 Royalty Pool Adjustment – Class D Exchange Multiplier

On January 1, 2016, the Pizza 73 Royalty Pool remained unchanged as a result of two new restaurants opening between September 2, 2014 and September 1, 2015 and two restaurants closing between January 1, 2015 and December 31, 2015. The forecasted additional system sales from the two new restaurants are estimated at \$1,070 annually less \$512 in system sales attributable to the two closed restaurants. The total number of Pizza 73 restaurants in the Royalty Pool remains at 100 for 2016. The yield of and the weighted average share price used in the calculation of the Class D Exchange Multiplier is determined in the same manner as that of the Class B Exchange Multiplier calculation at 5.89% and \$13.85, respectively. As a result of the contribution of the additional net sales to the Royalty Pool, the Class D Exchange Multiplier increased fractionally by 80% of the total adjustment or 0.35975; the new Class D Exchange Multiplier is 17.43307. This adjustment will also increase the entitlement of the holders of the Class D units to distributions of cash and allocations of income from the Partnership. The second adjustment to the Class D Exchange Multiplier will be adjusted to be effective January 1, 2016, once the actual performance of the new restaurants is determined in early 2017.

In early January 2017, adjustments to royalty payments and PPL's Class D Exchange Multiplier were made based on the actual performance of the two Pizza 73 restaurants added to the Royalty Pool on January 1, 2016. As a result of the adjustments, the new Class D Exchange Multiplier is 17.52620 and Class D Units can be exchanged for

# Pizza Pizza Limited

## Notes to the Consolidated Financial Statements

For the 52-week period ended January 1, 2017 and 53-week period ended January 3, 2016

(In thousands of Canadian dollars except common shares, special voting shares and number of shares)

1,752,620 shares, which is an increase of 9,313 shares, effective January 1, 2016.

g) 2017 Royalty Pool Adjustment – Class B Exchange Multiplier

On January 1, 2017, 15 net Pizza Pizza restaurants were added to the Royalty Pool as a result of 23 new restaurants opening and eight closing from January 1, 2016 to December 31, 2016. The additional system sales from the 23 new restaurants are estimated at \$7,674 annually less sales of \$873 from eight permanently closed Pizza Pizza restaurants resulting in net estimated Pizza Pizza sales of \$6,801 added to the Royalty Pool. The total number of Pizza Pizza restaurants in the Royalty Pool has increased to 651. The yield of the shares was determined to be 5.16% calculated using \$16.43 as a weighted average share price. Weighted average share price is calculated based on the market price of the shares traded on the Toronto Stock Exchange during the period of twenty consecutive days ending on the fifth trading day before January 1, 2017. As a result of the contribution of the additional net sales to the Royalty Pool, the Class B Exchange Multiplier increased fractionally by 80% of the total adjustment or 0.110643; the new Class B Exchange Multiplier is 1.930631. This adjustment will also increase the entitlement of the holders of the Class B Units to distributions of cash and allocations of income from the Partnership. The second adjustment to the Class B Exchange Multiplier will be adjusted to be effective January 1, 2017, once the actual performance of the new restaurants is determined in early 2018.

h) 2017 Royalty Pool Adjustment – Class D Exchange Multiplier

On January 1, 2017, the Pizza 73 Royalty Pool remained unchanged as a result of four new restaurants opening between September 2, 2015 and September 1, 2016 and four restaurants closing between January 1, 2016 and December 31, 2016. The forecasted additional system sales from the four new restaurants are estimated at \$1,226 annually less \$179 in system sales attributable to the four closed Pizza 73 restaurants resulting in net estimated Pizza 73 sales of \$1,047 added to the Royalty Pool. The net estimated sales were further reduced by \$2,086 in system sales attributable to certain restaurants previously added to the Royalty Pool whose territory adjusted a previously existing restaurant, resulting in a negative Pizza 73 Estimated Determined Amount. As per the Pizza Pizza Royalty Limited Partnership agreement, whenever the Estimated Determined Amount is negative it shall be deemed to be zero. Accordingly, the Class D Exchange Multiplier remained unchanged at 17.52620. Once the actual performance of the new restaurants is determined in early 2018, the Class D Exchange Multiplier may be adjusted to be effective January 1, 2017. The total number of Pizza 73 restaurants in the Royalty Pool remains at 100 for 2017.

i) PPRC Outstanding Shares

In exchange for adding the forecasted Pizza Pizza system sales to the Royalty Pool, PPL has received 277,519 additional equivalent shares (through the change to the Class B Exchange Multiplier). These represent 80% of the forecasted equivalent shares entitlement to be received (346,899 equivalent shares represent 100%), with the final equivalent shares entitlement to be determined when the new restaurants' 2017 actual sales performance is known with certainty in early 2018.

PPL's Class D equivalent share entitlement is unchanged for 2017. In any year that the forecasted system sales (less closed restaurants sales and other adjustments) is negative, as was the case with the Class D equivalent share entitlement calculation for 2017, no increase or decrease in the Exchange Multiplier is made. PPL will only have a Class D equivalent share entitlement for 2017 if the actual sales performance of the four new Pizza 73 restaurants, less the sales of adjustment restaurants, significantly exceeds forecasted system sales and yields net, positive sales when the actual sales performance is known with certainty in early 2018.

After giving effect to PPL's entitlement to additional equivalent shares as at January 1, 2017, PPL owns equivalent shares representing 21.1% of the Partnership's fully diluted shares.

# Pizza Pizza Limited

## Notes to the Consolidated Financial Statements

For the 52-week period ended January 1, 2017 and 53-week period ended January 3, 2016

(In thousands of Canadian dollars except common shares, special voting shares and number of shares)

The chart below shows the shares that would be outstanding if all of PPL's Class B and D Units of the Partnership were converted to shares after accounting for their respective multipliers.

### Shares outstanding and issuable on January 1, 2017

Shares outstanding		24,618,392
Class B equivalent Shares held by PPL as at December 31, 2016	4,559,542	
PPL additional Class B equivalent shares - True-up Holdback as at December 31, 2016	5,422	
Additional PPL Class B equivalent shares as at January 1, 2017	<u>277,519</u>	4,842,483
Class D equivalent Shares held by PPL as at December 31, 2016	1,743,307	
PPL additional Class D equivalent shares - True-up Holdback as at December 31, 2016	9,313	
Additional PPL Class D equivalent shares as at January 1, 2017	<u>-</u>	1,752,620
Number of fully diluted shares		<u>31,213,495</u>
PPL's proportion of all shares outstanding and available for exchange		21.1%

## 9. Investment in Jointly-controlled Companies

Jointly-controlled companies are joint ventures, consisting of PPL's 50% interest in 75 Pizza 73 restaurants (January 3, 2016 – 74 Pizza 73 restaurants). Jointly-controlled restaurants are companies, owned and operated as an independent business, equally owned by PPL and an Owner/Operator. Licensing, consulting and other agreements govern the relationship of PPL and the Owner/Operator as shareholders of these jointly-controlled restaurants, and establish a framework under which each restaurant is operated.

The financial statements of all jointly-controlled companies have a floating year-end of the Saturday immediately preceding July 31 and all operations are continuing.

The table below reconciles the balance of PPL's investment in the jointly-controlled companies, which is accounted for using equity accounting.

	For the 52-week period ended January 1, 2017	For the 53-week period ended January 3, 2016
Balance – beginning of period	18,937	18,818
Equity income from jointly-controlled companies	5,382	6,413
Dividends received from jointly-controlled companies	(5,084)	(6,294)
<b>Balance – end of period</b>	<b>19,235</b>	<b>18,937</b>

A breakdown of PPL's share in jointly-controlled companies' comprehensive income is as follows:

	For the 52-week period ended January 1, 2017	For the 53-week period ended January 3, 2016
Revenue	41,103	44,710
Expenses	(35,721)	(38,297)
<b>Income for the period after income taxes</b>	<b>5,382</b>	<b>6,413</b>

# Pizza Pizza Limited

## Notes to the Consolidated Financial Statements

For the 52-week period ended January 1, 2017 and 53-week period ended January 3, 2016

(In thousands of Canadian dollars except common shares, special voting shares and number of shares)

### 10. Intangible Assets

	Lease agreements	Computer software	Total
<b>52-week period ended January 1, 2017</b>			
Opening net book value	248	205	453
Additions	-	-	-
Amortization charge	(159)	(164)	(323)
<b>Closing net book value</b>	<b>89</b>	<b>41</b>	<b>130</b>
<b>As at January 1, 2017</b>			
Cost	1,600	1,982	3,582
Accumulated amortization	(1,511)	(1,941)	(3,452)
<b>Net book value</b>	<b>89</b>	<b>41</b>	<b>130</b>
<b>52-week period ended January 3, 2016</b>			
Opening net book value	410	342	752
Additions	-	77	77
Amortization charge	(162)	(214)	(376)
<b>Closing net book value</b>	<b>248</b>	<b>205</b>	<b>453</b>
<b>As at January 3, 2016</b>			
Cost	1,600	1,982	3,582
Accumulated amortization	(1,352)	(1,777)	(3,129)
<b>Net book value</b>	<b>248</b>	<b>205</b>	<b>453</b>

Amortization in the amount of \$164 (53-week period ended January 3, 2016 - \$204) for the 52-week period ended January 1, 2017 has been recovered from franchisees.

### 11. Trade and Other Payables

	As at January 1, 2017	As at January 3, 2016
Trade payables	24,542	24,824
Accruals	6,206	5,509
Sales tax payable	8,790	9,123
Other payables	4,020	4,034
<b>Total trade and other payables</b>	<b>43,558</b>	<b>43,490</b>

#### Sales Tax Payable

PPL collects provincial sales tax and federal goods and services tax on behalf of certain franchised restaurants in addition to the collection of tax on its own account. These accounts are included in trade and other payables above as follows:

	As at January 1, 2017	As at January 3, 2016
Sales tax disbursed in PPL's operations	237	466
Sales tax collected on behalf of certain franchised restaurants	8,553	8,657
<b>Total sales tax payable</b>	<b>8,790</b>	<b>9,123</b>

# Pizza Pizza Limited

## Notes to the Consolidated Financial Statements

For the 52-week period ended January 1, 2017 and 53-week period ended January 3, 2016

(In thousands of Canadian dollars except common shares, special voting shares and number of shares)

### 12. Borrowings

	As at January 1, 2017	As at January 3, 2016
Notes payable, bearing interest from 5.4% to 8%, repayable in varying monthly principal amounts, maturing between 2016 and 2019. These notes were secured by specific company-owned restaurant assets. The effective interest rate as at January 1, 2017 was 6.5% (January 3, 2016 – 6.9%).	1,317	421
	<b>1,317</b>	<b>421</b>
Less: current portion	(570)	(64)
<b>Total non-current borrowings</b>	<b>747</b>	<b>357</b>

### 13. Provisions

The provision for onerous leases represents the liability for the leased premises that are either vacant or subleased at a lower rate. The provision is made for the losses to be incurred over the remaining term period of the lease.

Future outflows may differ if the Company is able to franchise, sublease or terminate the lease before the expiry of the agreement.

	For the 52-week period ended January 1, 2017	For the 53-week period ended January 3, 2016
<b>Movements in the provision for onerous leases</b>		
Opening balance	934	475
Arising during the period	118	647
Reversals	(97)	-
Utilized during the period	(541)	(245)
Imputed interest	75	57
<b>Closing balance</b>	<b>489</b>	<b>934</b>

Reversals in the period relate to leases that were franchised, subleased or terminated during the period.

### 14. Deferred Gain

The deferred gain arose following the sale of the Pizza Pizza Rights and Marks to the Partnership following the initial public offering of the Fund. Concurrent with the sale, PPL entered into a 99-year License and Royalty Agreement with the Partnership, whereby PPL has the right to use the Rights and Marks and pays a royalty equal to 6% of the total system sales of restaurants in the Royalty Pool. The deferred gain is being amortized on a straight-line basis over the term of the License and Royalty Agreement.

# Pizza Pizza Limited

## Notes to the Consolidated Financial Statements

For the 52-week period ended January 1, 2017 and 53-week period ended January 3, 2016

(In thousands of Canadian dollars except common shares, special voting shares and number of shares)

The movement in the deferred gain balance during each period is as follows:

	For the 52-week period ended January 1, 2017	For the 53-week period ended January 3, 2016
Balance – beginning of period	206,209	208,539
Amortization for the period	(2,330)	(2,330)
<b>Balance – end of period</b>	<b>203,879</b>	<b>206,209</b>

A summary of the deferred gain and accumulated amortization at the end of each period is as follows:

	As at January 1, 2017	As at January 3, 2016
Deferred gain	230,675	230,675
Accumulated amortization	(26,796)	(24,466)
<b>Balance – end of period</b>	<b>203,879</b>	<b>206,209</b>

## 15. Income Taxes

The components of the income tax (expense) recovery are as follows:

	For the 52-week period ended January 1, 2017	For the 53-week period ended January 3, 2016
Current income tax recovery (expense)	5,290	(7,651)
Deferred tax recovery (expense)	(981)	2,848
<b>Income tax recovery (expense)</b>	<b>4,309</b>	<b>(4,803)</b>

The reconciliation to the statutory tax rate is as follows:

	For the 52-week period ended January 1, 2017	For the 53-week period ended January 3, 2016
Income (loss) for the period before income taxes	(1,053)	32,604
Combined Canadian federal and provincial rates	26.59%	26.5%
<b>Computed expected income tax recovery (expense)</b>	<b>280</b>	<b>(8,640)</b>
Non-taxable portion of capital gain	20	5,223
Effect of income taxable at lower rates	200	256
Equity income from jointly-controlled companies	1,431	1,700
Prior year dividend refund booked in current year	333	-
Rate differential	2,090	(3,260)
Permanent adjustments	(44)	(25)
Other	(1)	(57)
<b>Income tax recovery (expense)</b>	<b>4,309</b>	<b>(4,803)</b>



# Pizza Pizza Limited

## Notes to the Consolidated Financial Statements

For the 52-week period ended January 1, 2017 and 53-week period ended January 3, 2016

(In thousands of Canadian dollars except common shares, special voting shares and number of shares)

The deferred tax asset arises as a result of the temporary difference between the accounting and tax basis on the Rights and Marks, deferred financing fees and cash flow hedge as shown below.

	As at January 1, 2017	As at January 3, 2016
Property, plant and equipment	(933)	(622)
Intangible assets	(21)	(105)
Pizza Pizza Royalty Limited Partnership	(8,266)	(7,997)
Deferred gain	54,191	54,645
Donations	31	-
Provisions and other	130	248
Share of cash flow hedge of Partnership	47	79
Employee benefits	292	241
<b>Deferred tax asset</b>	<b>45,471</b>	<b>46,489</b>

## 16. Commitments and contingencies

### Commitments

Future minimum lease payments for premises, sponsorships and vehicles to related parties, which are companies under common control, and non-related entities, are as follows:

	Third parties	Related parties
Not later than 1 year	31,133	2,483
Later than 1 year and no later than 5 years	80,336	6,319
Later than 5 years	21,363	8,054

During the 52-week period ended January 1, 2017, lease payments of approximately \$24,882 (53-week period ended January 3, 2016 - \$20,965) were recovered under sublease agreements with various franchised restaurants. These recoveries are offset against rent expense.

The amounts receivable under future committed subleases are as follows:

	Third parties	Related parties
Not later than 1 year	27,715	-
Later than 1 year and no later than 5 years	73,001	-
Later than 5 years	19,663	-

### Contingencies

PPL is a party to various legal proceedings, mainly related to claims brought against it by former franchisees. It is not possible at this time to determine the outcome of these proceedings and, accordingly, no provisions have been made in these consolidated financial statements.

PPL has entered into an agreement with certain lenders to establish a line of credit of \$33,730 (January 3, 2016 – \$33,730) for the purpose of providing certain equipment and leasehold improvement loans to its franchisees. As security under these lines of credit facilities, PPL has provided certain guarantees as described in the agreement including a letter of credit in the amount of \$3,373 (January 3, 2016 – \$3,373). PPL has the right to increase the limit under these credit facilities by providing additional letters of credit.

As security for repayment of a borrowing facility held by the Partnership to the amount of \$47,000, PPL has granted a continuing, general security interest, subject to certain exceptions, in all present and acquired property of PPL, which may not be assigned without the prior consent of PPL. With respect to the Partnership's borrowing facility, PPL must

# Pizza Pizza Limited

## Notes to the Consolidated Financial Statements

For the 52-week period ended January 1, 2017 and 53-week period ended January 3, 2016

(In thousands of Canadian dollars except common shares, special voting shares and number of shares)

comply with certain financial covenants. As at January 1, 2017, PPL was in compliance with these financial covenants.

### 17. Common Shares and Special Voting Shares

	As at January 1, 2017	As at January 3, 2016
Authorized without limit as to number - Common shares (with no par value) Special voting shares, non-participating, entitling the holder to one vote per share (with no par value)		
Issued and paid -		
100 common shares	100	100
100,000 special voting shares	100	100
<b>Total common shares and special voting shares</b>	<b>200</b>	<b>200</b>

### 18. Capital Disclosures

PPL's objectives when managing capital are to safeguard PPL's ability to continue as a going concern so that it can continue to provide returns for the shareholder and benefits for other stakeholders and to provide an adequate return to shareholders by pricing products and services commensurately with the level of risk.

PPL evaluates its capital as all components of shareholders' deficiency, other than amounts in accumulated other comprehensive loss related to PPL's share of the Partnership's cash flow hedge.

PPL sets the amount of capital in proportion to risk. PPL manages the capital structure and makes adjustments to it in light of changes in economic conditions and the risk characteristics of the underlying assets. In order to maintain or adjust the capital structure, PPL may adjust the amount of dividends paid to shareholders, return capital to shareholders, issue new shares, or sell assets to reduce debt.

### 19. Food Sales

Food sales include the following:

	For the 52-week period ended January 1, 2017	For the 53-week period ended January 3, 2016
Food sales	173,343	171,583
Company-owned restaurant sales	15,879	18,464
<b>Total food sales</b>	<b>189,222</b>	<b>190,047</b>

# Pizza Pizza Limited

## Notes to the Consolidated Financial Statements

For the 52-week period ended January 1, 2017 and 53-week period ended January 3, 2016

(In thousands of Canadian dollars except common shares, special voting shares and number of shares)

### 20. Royalties, Franchise Fees and Other Revenue

Royalties, franchise fees and other revenue include the following:

	For the 52-week period ended January 1, 2017	For the 53-week period ended January 3, 2016
Royalties	24,475	24,351
Initial and renewal franchise fees	1,661	1,613
Construction fees	1,204	940
Administration and accounting fees	2,764	2,985
<b>Total royalties, franchise fees and other revenue</b>	<b>30,104</b>	<b>29,889</b>

### 21. Expenses by Nature

The following table summarizes significant general and administrative expenses:

	For the 52-week period ended January 1, 2017	For the 53-week period ended January 3, 2016
Depreciation of property, plant and equipment	2,464	1,901
Amortization of intangible assets	159	172
Operating lease payments	3,015	4,072
Employee benefit expense	16,996	17,655

### 22. Related Party Transactions

The following table summarizes PPL's transactions with related parties in the normal course of business:

	For the 52-week period ended January 1, 2017	For the 53-week period ended January 3, 2016
Rent expense <sup>(i)</sup>	2,601	2,904
Food purchases <sup>(i)</sup>	12,526	14,353
Recovery of expenses <sup>(i)</sup>	600	850
Administration and accounting fee revenue <sup>(ii)</sup>	2,764	2,985

<sup>(i)</sup> Transactions with commonly controlled companies

<sup>(ii)</sup> Transactions with jointly-controlled companies

As at January 1, 2017, PPL has trade payables of \$930 (as at January 3, 2016 - \$807) payable to a company under common management control.

As at January 1, 2017, PPL has included in trade and other payables amounts payable of \$3,498 (as at January 3, 2016 - \$4,047) to the Partnership, which were paid subsequent to the end of the period.

# Pizza Pizza Limited

## Notes to the Consolidated Financial Statements

For the 52-week period ended January 1, 2017 and 53-week period ended January 3, 2016

(In thousands of Canadian dollars except common shares, special voting shares and number of shares)

In addition, PPL has the following advances to and from related parties:

	As at January 1, 2017	As at January 3, 2016
Receivables from jointly-controlled companies	2,702	1,182
Advances from related party	(17,452)	(18,878)

Advances from related party are due to the parent company. Advances from related party and receivables from jointly-controlled companies are non-interest bearing, have no specified terms of repayment and are unsecured. The related party has waived the right to demand repayment prior to January 1, 2018. Accordingly, the advances from related party have been classified as long-term.

During the 53-week period ended January 3, 2016, PPL paid a dividend of \$39,000 to its shareholders, and subsequently this amount was advanced back to PPL

### Key management compensation

The compensation expense or amounts payable to management, including officers and directors, is shown below:

	For the 52-week period ended January 1, 2017	For the 53-week period ended January 3, 2016
Salaries and other short-term employee benefits	3,716	4,173
Other long-term benefits	188	212
<b>Total key management compensation</b>	<b>3,904</b>	<b>4,385</b>

## 23. Segmented Information

Operating segments are defined as components of an enterprise about which discrete separate financial information is available and which is evaluated regularly by the chief operating decision maker in deciding how to allocate resources and in assessing performance. The chief operating decision maker is the Chief Executive Officer and Director. The operations of Pizza Pizza consist of two reportable segments; Pizza Pizza and Pizza 73. While they both operate in the pizza QSR segment, they are in predominantly different geographic markets in Canada. Pizza Pizza operates mainly in the Ontario and Quebec (Eastern Canada) pizza QSR segment, whereas Pizza 73 operates mainly in the Alberta (Western Canada) pizza QSR segment. In addition, the return on Pizza Pizza's investment in the Partnership is included in the Pizza Pizza segment. The eliminations column represents adjustments required to reconcile PPL's segmented reporting, to the reporting on the consolidated statements of financial position and the consolidated statements of income. This column represents adjustments required to account for joint ventures under IFRS 11.

For the 52-week period ended January 1, 2017	Eastern	Western	Eliminations	Total
Food sales	189,063	41,153	(40,994)	189,222
Royalties, franchise fees and other revenue	27,287	2,817	-	30,104
Interest and other income	1,120	367	(61)	1,426
Cost of food sales	152,134	15,039	(14,973)	152,200
General and administrative expenses	46,800	19,689	(17,699)	48,790
Equity income from jointly-controlled companies	-	-	5,382	5,382
Interest on borrowings	56	8	(8)	56
Income (loss) for the period before income taxes	259	4,890	(6,202)	(1,053)
Segment income (loss) for the period	4,567	4,071	(5,382)	3,256
Additions to property, plant and equipment	7,302	428	(399)	7,331

# Pizza Pizza Limited

## Notes to the Consolidated Financial Statements

For the 52-week period ended January 1, 2017 and 53-week period ended January 3, 2016

(In thousands of Canadian dollars except common shares, special voting shares and number of shares)

As at January 1, 2017	Eastern	Western	Eliminations	Total
Total assets	149,524	30,531	(3,108)	176,947
Intangible assets	41	89	-	130

For the 53-week period ended January 3, 2016	Eastern	Western	Eliminations	Total
Food sales	189,521	45,249	(44,723)	190,047
Royalties, franchise fees and other revenue	26,883	3,006	-	29,889
Interest and other income	1,381	324	(14)	1,691
Cost of food sales	151,332	16,651	(16,431)	151,552
General and administrative expenses	44,749	21,203	(19,102)	46,850
Equity income from jointly-controlled companies	-	-	6,413	6,413
Interest on borrowings	60	4	(4)	60
Income (loss) for the period before income taxes	32,987	7,033	(7,416)	32,604
Segment income (loss) for the period	28,183	6,043	(6,425)	27,801
Additions to property, plant and equipment	4,590	551	(437)	4,704

As at January 3, 2016	Eastern	Western	Eliminations	Total
Total assets	157,963	29,300	(3,035)	184,228
Intangible assets	205	248	-	453

## 24. Statements of Cash Flows Information

Changes in non-cash working capital are as follows:

	For the 52-week period ended January 1, 2017	For the 53-week period ended January 3, 2016
Trade and other receivables	(5,219)	(2,000)
Inventories	(120)	2,114
Income taxes recoverable	(5,017)	396
Recoverable franchisee expenses	5,786	1,100
Trade and other payables	68	5,864
Income taxes payable	(7,651)	7,651
Deposits from franchisees	116	734
Receivables from jointly-controlled companies	(1,520)	132
	(13,557)	15,991
	For the 52-week period ended January 1, 2017	For the 53-week period ended January 3, 2016
Interest paid	57	60
Income taxes paid	7,843	-

## 25. Financial Risk Management

PPL's objective is to minimize risk with respect to financial instruments by monitoring the performance of its franchisees and jointly-controlled companies, maintaining restaurants in different geographic regions and having the ability to assume the operations of franchisees for inadequate financial performance and/or default under the franchise agreement.

# Pizza Pizza Limited

## Notes to the Consolidated Financial Statements

For the 52-week period ended January 1, 2017 and 53-week period ended January 3, 2016

(In thousands of Canadian dollars except common shares, special voting shares and number of shares)

### Fair Values

The carrying amounts of cash and cash equivalents, trade and other receivables and trade and other payables approximate fair values given the short-term maturity of these instruments and are Level 3 instruments.

A reasonable estimate of fair value could not be made for receivables from jointly-controlled companies, advances from related party, recoverable franchisee expenses, renovation funds and deposits from franchisees as there are no fixed terms of repayment.

The fair value of the non-current notes receivable is based on the estimated future discounted cash flows using a comparable market rate of interest as at January 1, 2017 of 6.4% (January 3, 2016 – 6.5%).

The fair value of the borrowings is based on the estimated future discounted cash flows using a comparable market rate of interest as at January 1, 2017 of prime plus a spread varying by loan (January 3, 2016 - prime plus a spread varying by loan). The Company has no plans to prepay these instruments prior to maturity. The fair value of the borrowings was determined using Level 2 inputs, which are observable inputs or inputs that can be corroborated by observable market data for substantially the full term of the asset or liability.

The carrying value and fair value of PPL's financial instruments are as follows:

Category		As at January 1, 2017		As at January 3, 2016	
		Carrying value	Fair value	Carrying value	Fair value
Cash and cash equivalents	L&R	13,024	13,024	14,360	14,360
Trade and other receivables	L&R	17,907	17,907	12,688	12,688
Notes receivable	L&R	14,841	13,891	12,304	11,481
Trade and other payables	OFL	43,558	43,558	43,490	43,490
Borrowings	OFL	1,317	1,167	421	358

Financial instruments category guide:

- L&R Loans and receivables
- OFL Other financial liabilities

The different fair value hierarchy levels are as follows:

- Level 1: Quoted prices (unadjusted) in active markets for identical financial assets or financial liabilities;
- Level 2: Inputs other than quoted prices included within Level 1 that are observable for the financial asset or financial liability, either directly or indirectly; and
- Level 3: Inputs for the financial asset or financial liability that are not based on observable market data.

### Credit Risk

PPL is exposed to credit risk as all of the franchisees and jointly-controlled companies operate within the same segment: commercial food service. PPL is also exposed to credit risk in the event of non-payment by its franchisees and jointly-controlled companies of its trade receivables, recoverable franchisee expenses, notes receivable, receivables from jointly-controlled companies and renovation funds receivable. PPL's credit risk is mitigated by the large number of franchisees and jointly-controlled companies operating in different geographical markets and by PPL's ultimate ability to assume operations of the franchisees if there is inadequate financial performance and/or default under the franchisee agreement.

PPL writes off receivable accounts, including trade receivables, notes receivable and renovation funds, to expected realizable value as soon as the account is determined not to be fully collectible, with such write-offs charged to income (loss), unless the loss has been provided for in prior periods, in which case the write-off is applied to reduce

# Pizza Pizza Limited

## Notes to the Consolidated Financial Statements

For the 52-week period ended January 1, 2017 and 53-week period ended January 3, 2016

(In thousands of Canadian dollars except common shares, special voting shares and number of shares)

the provision for impairment of those receivables. PPL updates its estimate of the provision for impairment of receivables, based on a customer-by-customer evaluation of the collectability of receivable balances as at each consolidated statements of financial position reporting date, taking into account amounts that are past due, and any available information indicating that a customer could be experiencing liquidity or going concern problems. A reconciliation of the provision for impairment of trade and other receivables is shown in note 3 and a reconciliation of the provision for notes receivable is shown in note 6.

The aging of trade receivable balances that are past due, but not impaired are as follows:

	As at January 1, 2017	As at January 3, 2016
Past due 0-30 days	1,069	1,176
Past due 31-120 days	719	1,115
<b>Total trade receivables past due, but not impaired</b>	<b>1,788</b>	<b>2,291</b>

### Liquidity Risk

PPL is subject to liquidity risk with respect to the items outlined in the table below. The risk is mitigated as the majority of PPL's revenue is earned from franchisees and jointly-controlled companies, which have agreements with PPL and whose activities are closely monitored by PPL. In the case of franchisees, the majority of PPL's business, PPL is able to assume operations of the franchises if there is inadequate financial performance and/or default under the franchise agreement. Liquidity requirements are monitored by PPL's head office functions in order to guarantee effective access to financial resources.

Management believes that currently available funds and credit facilities, apart from those that will be generated by operating and financing activities, will allow PPL to satisfy its requirements for investment, working capital management, and borrowing repayment at maturity.

The following are the contractual undiscounted cash flows of financial liabilities as at January 1, 2017:

	Carrying amount	0 to 12 months	1 to 2 years	2 to 5 years	More than 5 years
Trade and other payables	43,558	43,558	-	-	-
Deposits from franchisees	2,486	2,486	-	-	-
Borrowings	1,317	570	389	358	-
Advances from related party	17,452	-	17,452	-	-

### Interest Rate Risk

PPL is exposed to interest rate risk from its borrowings. All borrowings are based on floating interest rates.

### 26. Seasonality

Historically, PPL's system sales experience a decrease in the first calendar quarter when compared to the fourth quarter, which has historically been the strongest quarter.