Core-Mark Holding Company, Inc.
Form 10-Q
November 05, 2015


UNITED STATES
SECURITIES AND EXCHANGE COMMISSION
WASHINGTON, D.C. 20549
FORM 10-Q
(MARK ONE)

x QUARTERLY REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934

For the quarterly period ended September 30, 2015

o 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: 000-51515

Core-Mark Holding Company, Inc.
(Exact name of registrant as specified in its charter)

| | |
|---|---|
| Delaware<br>(State or other jurisdiction of incorporation or organization) | 20-1489747<br>(IRS Employer Identification No.) |
| 395 Oyster Point Boulevard, Suite 415<br>South San Francisco, CA | 94080 |
| (Address of principal executive offices) | (Zip Code) |

(650) 589-9445
(Registrant’s telephone number, including area code)

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

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

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

| | |
|---|---|
| Large accelerated filer x | Accelerated filer o |
| Non-accelerated filer o (Do not check if a smaller reporting company) | Smaller reporting company o |

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

As of October 30, 2015, 23,052,867 shares of the registrant’s common stock, $0.01 par value per share, were outstanding.

FORM 10-Q
FOR THE QUARTER ENDED SEPTEMBER 30, 2015
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PART I. FINANCIAL INFORMATION
ITEM 1. FINANCIAL STATEMENTS

CORE-MARK HOLDING COMPANY, INC. AND SUBSIDIARIES
CONDENSED CONSOLIDATED BALANCE SHEETS
(In millions, except share and per share data)
(Unaudited)

| | September 30, 2015 | December 31, 2014 |
|---|---|---|
| Assets | | |
| Current assets: | | |
| Cash and cash equivalents | $9.4 | $14.4 |
| Restricted cash | 9.7 | 13.0 |
| Accounts receivable, net of allowance for doubtful accounts of $10.9 and $10.8 as of September 30, 2015 and December 31, 2014, respectively | 278.6 | 245.3 |
| Other receivables, net | 63.9 | 61.5 |
| Inventories, net (Note 4) | 350.1 | 417.8 |
| Deposits and prepayments | 58.0 | 43.7 |
| Deferred income taxes | 9.1 | 8.4 |
| Total current assets | 778.8 | 804.1 |
| Property and equipment, net | 157.1 | 148.9 |
| Goodwill | 22.9 | 22.9 |
| Other intangible assets, net | 28.4 | 22.6 |
| Other non-current assets, net | 29.6 | 31.1 |
| Total assets | $1,016.8 | $1,029.6 |
| Liabilities and Stockholders' Equity | | |
| Current liabilities: | | |
| Accounts payable | $148.1 | $128.4 |
| Book overdrafts | 28.0 | 29.1 |
| Cigarette and tobacco taxes payable | 170.9 | 187.3 |
| Accrued liabilities | 108.1 | 93.4 |
| Deferred income taxes | 0.2 | 0.3 |
| Total current liabilities | 455.3 | 438.5 |
| Long-term debt (Note 5) | 19.4 | 68.2 |
| Deferred income taxes | 16.6 | 16.2 |
| Other long-term liabilities | 11.5 | 11.9 |
| Claims liabilities | 27.7 | 27.5 |
| Pension liabilities | 8.2 | 6.0 |
| Total liabilities | 538.7 | 568.3 |
| Contingencies (Note 6) | | |
| Stockholders' equity: | | |
| Common stock, $0.01 par value (100,000,000 shares authorized, 25,970,413 and 25,847,269 shares issued; 23,054,835 and 23,080,110 shares outstanding at September 30, 2015 and December 31, 2014, respectively) | 0.3 | 0.3 |
| Additional paid-in capital | 269.7 | 263.8 |
| Treasury stock at cost (2,915,578 and 2,767,159 shares of common stock at September 30, 2015 and December 31, 2014, respectively) | (61.6) | (52.6) |
| Retained earnings | 286.1 | 261.4 |
| Accumulated other comprehensive loss | (16.4) | (11.6) |

| | | |
|---|---|---|
| Total stockholders’ equity | 478.1 | 461.3 |
| Total liabilities and stockholders’ equity | $1,016.8 | $1,029.6 |

See accompanying notes to condensed consolidated financial statements.

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CORE-MARK HOLDING COMPANY, INC. AND SUBSIDIARIES
CONDENSED CONSOLIDATED STATEMENTS OF OPERATIONS
(In millions, except per share data)
(Unaudited)

| | Three Months Ended September 30, | | Nine Months Ended September 30, | |
|---|---|---|---|---|
| | 2015 | 2014 | 2015 | 2014 |
| Net sales | $2,991.6 | $2,747.4 | $8,254.3 | $7,671.5 |
| Cost of goods sold | 2,820.0 | 2,596.0 | 7,786.5 | 7,252.4 |
| Gross profit | 171.6 | 151.4 | 467.8 | 419.1 |
| Warehousing and distribution expenses | 92.8 | 83.5 | 260.9 | 236.9 |
| Selling, general and administrative expenses | 52.8 | 47.0 | 147.6 | 134.9 |
| Amortization of intangible assets | 0.6 | 0.7 | 1.8 | 2.0 |
| Total operating expenses | 146.2 | 131.2 | 410.3 | 373.8 |
| Income from operations | 25.4 | 20.2 | 57.5 | 45.3 |
| Interest expense | (0.6) | (0.5) | (1.9) | (1.8) |
| Interest income | 0.1 | 0.1 | 0.4 | 0.4 |
| Foreign currency transaction gains (losses), net | (0.7) | 0.2 | (1.3) | — |
| Income before income taxes | 24.2 | 20.0 | 54.7 | 43.9 |
| Provision for income taxes (Note 7) | (9.1) | (6.3) | (20.9) | (15.8) |
| Net income | $15.1 | $13.7 | $33.8 | $28.1 |
| | | | | |
| Basic net income per common share (Note 9) | $0.65 | $0.59 | $1.46 | $1.22 |
| Diluted net income per common share (Note 9) | $0.65 | $0.59 | $1.45 | $1.21 |
| | | | | |
| Basic weighted-average shares (Note 9) | 23.1 | 23.1 | 23.1 | 23.1 |
| Diluted weighted-average shares (Note 9) | 23.3 | 23.3 | 23.3 | 23.2 |
| | | | | |
| Dividends declared and paid per common share (Note 11) | $0.13 | $0.11 | $0.39 | $0.33 |

See accompanying notes to condensed consolidated financial statements.

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CORE-MARK HOLDING COMPANY, INC. AND SUBSIDIARIES
CONDENSED CONSOLIDATED STATEMENTS OF COMPREHENSIVE INCOME
(In millions)
(Unaudited)

| | Three Months Ended September 30, | | Nine Months Ended September 30, | |
|---|---|---|---|---|
| | 2015 | 2014 | 2015 | 2014 |
| Net income | $15.1 | $13.7 | $33.8 | $28.1 |
| Other comprehensive income (loss), net of tax: | | | | |
| Defined benefit plan adjustments | (0.8) | 0.1 | (0.7) | 0.2 |
| Foreign currency translation loss | (1.9) | (1.7) | (4.1) | (1.8) |
| Other comprehensive loss, net of tax | (2.7) | (1.6) | (4.8) | (1.6) |
| Comprehensive income | $12.4 | $12.1 | $29.0 | $26.5 |

See accompanying notes to condensed consolidated financial statements.

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CORE-MARK HOLDING COMPANY, INC. AND SUBSIDIARIES
CONDENSED CONSOLIDATED STATEMENTS OF CASH FLOWS
(In millions)
(Unaudited)

| | Nine Months Ended September 30, 2015 | 2014 |
|---|---|---|
| Cash flows from operating activities: | | |
| Net income | $33.8 | $28.1 |
| Adjustments to reconcile net income to net cash provided by operating activities: | | |
| LIFO and inventory provisions | 9.2 | 13.4 |
| Amortization of debt issuance costs | 0.2 | 0.2 |
| Stock-based compensation expense | 6.7 | 4.3 |
| Bad debt expense, net | 1.1 | 1.3 |
| Depreciation and amortization | 28.3 | 23.4 |
| Foreign currency transaction losses, net | 1.3 | — |
| Deferred income taxes | (0.3) | 1.5 |
| Changes in operating assets and liabilities: | | |
| Accounts receivable, net | (33.3) | (32.5) |
| Other receivables, net | (3.3) | (2.5) |
| Inventories, net | 53.9 | 34.6 |
| Deposits, prepayments and other non-current assets | (18.0) | (10.4) |
| Excess tax deductions associated with stock-based compensation | (2.0) | (2.4) |
| Accounts payable | 22.3 | 23.6 |
| Cigarette and tobacco taxes payable | (10.2) | (18.0) |
| Pension, claims, accrued and other long-term liabilities | 16.2 | 4.9 |
| Net cash provided by operating activities | 105.9 | 69.5 |
| Cash flows from investing activities: | | |
| Acquisition of business, net of cash acquired | (8.0) | — |
| Change in restricted cash | 3.3 | 0.4 |
| Additions to property and equipment, net | (24.7) | (24.1) |
| Capitalization of software and related development costs | (7.5) | (3.2) |
| Proceeds from sale of fixed assets | 0.3 | — |
| Net cash used in investing activities | (36.6) | (26.9) |
| Cash flows from financing activities: | | |
| Repayments under revolving credit facility, net | (50.6) | (17.7) |
| Dividends paid | (9.1) | (7.7) |
| Payments on capital leases | (1.6) | (1.3) |
| Repurchases of common stock | (9.0) | (5.3) |
| Proceeds from exercise of common stock options | 0.3 | 1.9 |
| Tax withholdings related to net share settlements of restricted stock units | (3.2) | (1.4) |
| Excess tax deductions associated with stock-based compensation | 2.0 | 2.4 |
| Increase (decrease) in book overdrafts | (1.1) | 0.5 |
| Net cash used in financing activities | (72.3) | (28.6) |
| Effects of changes in foreign exchange rates | (2.0) | (0.8) |
| Change in cash and cash equivalents | (5.0) | 13.2 |
| Cash and cash equivalents, beginning of period | 14.4 | 11.0 |
| Cash and cash equivalents, end of period | $9.4 | $24.2 |
| Supplemental disclosures: | | |

| | | |
|---|---|---|
| Cash paid during the period for: | | |
| Income taxes, net | $21.1 | $15.4 |
| Interest | $1.0 | $0.7 |
| Non-cash capital lease obligations incurred | $5.2 | $4.7 |
| Unpaid property and equipment purchases included in accrued liabilities | $1.5 | $7.8 |

See accompanying notes to condensed consolidated financial statements.

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CORE-MARK HOLDING COMPANY, INC. AND SUBSIDIARIES
NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS
(Unaudited)

1. Summary of Company Information

Business

Core-Mark Holding Company, Inc., together with its subsidiaries (referred to herein as “the Company” or “Core-Mark”), is one of the largest marketers of fresh and broad-line supply solutions to the convenience retail industry in North America. The Company offers a full range of products, marketing programs and technology solutions to approximately 37,500 customer locations in the United States (“U.S.”) and Canada. The Company’s customers include traditional convenience stores, drug stores, grocery stores, liquor stores and other specialty and small format stores that carry convenience products. The Company’s product offering includes cigarettes, other tobacco products, candy, snacks, fast food, groceries, fresh products, dairy, bread, beverages, general merchandise and health and beauty care products. The Company operates a network of 29 distribution centers in the U.S. and Canada (excluding two distribution facilities it operates as a third party logistics provider). Twenty-five of the Company’s distribution centers are located in the U.S. and four are located in Canada.

2. Basis of Presentation and Principles of Consolidation

The accompanying unaudited condensed consolidated balance sheet as of September 30, 2015, the unaudited condensed consolidated statements of operations and comprehensive income for the three and nine months ended September 30, 2015 and 2014, and the unaudited condensed consolidated statements of cash flows for the nine months ended September 30, 2015 and 2014, have been prepared on the same basis as the Company’s audited consolidated financial statements and include all adjustments necessary for the fair presentation of its consolidated results of operations, financial position, comprehensive income and cash flows. Results for the interim periods are not necessarily indicative of results to be expected for the full year or any other future periods. The condensed consolidated balance sheet as of December 31, 2014 has been derived from the Company’s audited financial statements, which are included in its 2014 Annual Report on Form 10-K, filed with the Securities and Exchange Commission (“SEC”) on March 2, 2015.

The significant accounting policies and certain financial information that are normally included in financial statements prepared in accordance with accounting principles generally accepted in the U.S. (“GAAP”), but which are not required for interim reporting purposes, have been omitted. The unaudited condensed consolidated interim financial statements should be read in conjunction with the Company’s audited consolidated financial statements in its Annual Report on Form 10-K, for the year ended December 31, 2014.

The unaudited condensed consolidated financial statements include Core-Mark and its wholly-owned subsidiaries. All intercompany balances and transactions have been eliminated in the unaudited condensed consolidated financial statements.

Concentration of Credit Risks

Financial instruments, which potentially subject the Company to concentrations of credit risk, consist principally of cash investments, accounts receivable and other receivables. The Company places its cash and cash equivalents in short-term instruments with high quality financial institutions and limits the amount of credit exposure in any one financial instrument. The Company pursues amounts and incentives due from vendors in the normal course of business and is often allowed to deduct these amounts and incentives from payments made to vendors.

A credit review is completed for new customers and ongoing credit evaluations of each customer’s financial condition are performed periodically, with reserves maintained for potential credit losses. Credit limits given to customers are based on a risk assessment of their ability to pay and other factors. Accounts receivable are typically not collateralized, but the Company may require prepayments or other guarantees whenever deemed necessary.

Alimentation Couche-Tard, Inc. (“Couche-Tard”), the Company’s largest customer, accounted for approximately 13.8% and 14.3% of the Company’s total net sales in the three and nine months ended September 30, 2015, respectively, and accounted for approximately 14.6% of the Company's net sales for both the three and nine months ended September 30, 2014. No single customer accounted for 10% or more of the Company’s accounts receivables as of September 30, 2015 or December 31, 2014.

Recent Accounting Standards or Updates Not Yet Effective

On May 28, 2014, the Financial Accounting Standards Board ("FASB") issued Accounting Standards Update ("ASU") No. 2014-09, Revenue from Contracts with Customers: Topic 606 ("ASU 2014-09"), to supersede nearly all existing revenue recognition guidance under U.S. GAAP. The core principle of ASU 2014-09 is to recognize revenues when promised goods or services are

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transferred to customers in an amount that reflects the consideration that is expected to be received for those goods or services. On August 12, 2015, the FASB issued ASU 2015-14 to defer the effective date of the new revenue recognition standard for annual reports on fiscal years beginning after December 15, 2017. The Company is currently evaluating the impact of the adoption of ASU 2014-09 on its financial statements.

On May 7, 2015, the FASB issued ASU No. 2015-07, Disclosures for Investments in Certain Entities That Calculate Net Asset Value per Share (or Its Equivalent): Topic 820 ("ASU 2015-07"). The standard removes the requirement to categorize within the fair value hierarchy all investments for which fair value is measured using the net asset value per share practical expedient. The Company does not hold any such investments on its condensed consolidated balance sheet, however, the assets held in a group trust for the Company's defined benefit pension plan include such investments. ASU 2015-07 requires retrospective adoption and is effective for the Company beginning in 2016, although early adoption is permitted. The Company is currently evaluating the impact ASU 2015-07 will have on its financial statements.

On August 18, 2015, the FASB issued ASU No. 2015-15, Imputation of Interest: Presentation and Subsequent Measurement of Debt Issuance Costs Associated with Line-of -Credit Arrangements: Subtopic 835-30 ("ASU 2015-15"). The guidance states that the SEC staff would not object to an entity deferring and presenting debt issuance costs as an asset and subsequently amortizing the deferred debt issuance costs ratably over the term of the line-of-credit arrangement, regardless of whether there are any outstanding borrowings on the line-of-credit arrangement. ASU 2015-15 requires retrospective application and is effective for annual periods beginning after December 15, 2015. The Company has determined the adoption of ASU 2015-15 will not have a material impact on its financial statements.

On September 25, 2015, the FASB issued ASU 2015-16, Business Combinations (Topic 805): Simplifying the Accounting for Measurement-Period Adjustments ("ASU 2015-16"). The new guidance eliminates the requirement that an acquiring entity in a business combination account for measurement-period adjustments retrospectively. Under ASU 2015-16, acquirers must recognize measurement-period adjustments in the period in which they determine the amounts, including the effect on earnings of any amounts they would have recorded in previous periods, if the accounting had been completed at the acquisition date. The amendments in this update are to be applied prospectively, for fiscal years beginning after December 15, 2015. The Company has determined the adoption of ASU 2015-16 will not have a material impact on its financial statements.

## 3. Acquisition

### Asset Acquisition of Karrys Bros., Limited

On February 23, 2015, the Company acquired substantially all of the assets of Karrys Bros., Limited ("Karrys Bros."), a regional convenience wholesaler servicing customers in Ontario, Canada, and the surrounding provinces, for cash consideration of approximately $8.0 million, or $10.0 million Canadian. The Karrys Bros. operations have been integrated into the Company's existing distribution center in Toronto and have provided the Company with the opportunity to increase its market share in eastern Canada. The purchase price allocation of the acquired assets and liabilities assumed was as follows (in millions):

| | February 23, 2015 |
|---|---|
| Accounts receivable | $3.9 |
| Inventory | 3.9 |
| Property and equipment | 2.3 |
| Liabilities | (2.1) |
| Total consideration | $8.0 |

Transaction and integration costs in connection with the acquisition of Karrys Bros. were approximately $0.4 million and $1.5 million for the three and nine months ended September 30, 2015, respectively. The results of operations of Karrys Bros. have been included in the Company's consolidated statements of operations and comprehensive income since the acquisition date. The Company does not consider the Karrys Bros. acquisition to be a material business combination and therefore has not disclosed pro-forma results of operations for the acquired business.

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4. Inventories

Inventories consist of the following (in millions):

| | September 30, 2015 | December 31, 2014 |
|---|---|---|
| Inventories at FIFO, net of reserves | $474.6 | $533.1 |
| Less: LIFO reserve | (124.5) | (115.3) |
| Total inventories at LIFO, net of reserves | $350.1 | $417.8 |

Cost of goods sold reflects the application of the last-in, first-out (“LIFO”) method of valuing inventories in the U.S. based upon estimated annual producer price indices. Inventories in Canada are valued on a first-in, first-out (“FIFO”) basis, as LIFO is not a permitted inventory valuation method in Canada. During periods of rising prices, the LIFO method of costing inventories generally results in higher current costs being charged against income while lower costs are retained in inventories. Conversely, during periods of decreasing prices, the LIFO method of costing inventories generally results in lower current costs being charged against income and higher stated inventories. The Company recorded LIFO expense of $3.3 million and $6.5 million for the three months ended September 30, 2015 and 2014, respectively, and $9.2 million and $13.6 million for the nine months ended September 30, 2015 and 2014, respectively.

5. Long-term Debt

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

| | September 30, 2015 | December 31, 2014 |
|---|---|---|
| Amounts borrowed (Credit Facility) | $5.7 | $55.9 |
| Obligations under capital leases | 13.7 | 12.3 |
| Total long-term debt | $19.4 | $68.2 |

The Company has a revolving credit facility (“Credit Facility”) with a capacity of $200 million, which can be increased up to an additional $100 million, limited by a borrowing base primarily consisting of eligible accounts receivable and inventories. All obligations under the Credit Facility are secured by first priority liens on substantially all of the Company’s present and future assets. The terms of the Credit Facility permit prepayment without penalty at any time (subject to customary breakage costs with respect to LIBOR or CDOR based loans prepaid prior to the end of an interest period).

On May 21, 2015, the Company entered into a sixth amendment to the Credit Facility (the "Sixth Amendment"), which extended the term of the Credit Facility from May 2018 to May 2020. The Sixth Amendment fixed the unused facility fee at 25 basis points and provided for quarterly borrowing base reporting. The margin added to the LIBOR or CDOR rate remains at a range of 125 to 175 basis points. In addition, the Sixth Amendment raised and reset the baskets for stock repurchases in aggregate of $75.0 million, not to exceed $20.0 million in any year, an aggregate of $100.0 million for dividends and up to $150.0 million for permitted acquisitions. As of September 30, 2015, the remaining balances under the Credit Facility for stock repurchases, dividends, and permitted acquisitions were $72.0 million, $94.0 million, and $150.0 million, respectively. The Company incurred fees of approximately $0.4 million in connection with the Sixth Amendment, which are being amortized over the remaining term of the amendment.

Amounts borrowed, outstanding letters of credit and amounts available to borrow, net of certain reserves required under the Credit Facility, were as follows (in millions):

| | September 30, 2015 | December 31, 2014 |
|---|---|---|
| Amounts borrowed | $5.7 | $55.9 |
| Outstanding letters of credit | $18.5 | $17.4 |
| Amounts available to borrow[1] | $166.3 | $114.8 |

(1) Excluding $100 million expansion feature.

Average borrowings during the three and nine months ended September 30, 2015 were $48.1 million and $38.6 million, respectively, with amounts borrowed, at any one time outstanding, ranging from zero to $120.9 million. For the three and nine months ended September 30, 2014, average borrowings were $1.9 million and $7.4 million, respectively, with amounts borrowed, at any one time outstanding, ranging from zero to $46.3 million.

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The weighted-average interest rate on the revolving credit facility for the three and nine months ended September 30, 2015 was 1.5% and 1.6%, respectively, compared to 1.8% and 1.6% for the same periods in 2014. The weighted-average interest rate is calculated based on the daily cost of borrowing, reflecting a blend of prime and LIBOR rates. The Company paid fees for unused facility and letter of credit participation, which are included in interest expense, of $0.2 million and $0.5 million during the three and nine months ended September 30, 2015, respectively, and $0.2 million and $0.6 million during the three and nine months ended September 30, 2014, respectively. The Company recorded charges related to amortization of debt issuance costs, which are included in interest expense, of less than $0.1 million for each of the three months ended September 30, 2015 and 2014. For each of the nine months ended September 30, 2015 and 2014, the Company recorded charges related to amortization of debt issuance costs of $0.2 million. Unamortized debt issuance costs were $1.3 million and $1.1 million as of September 30, 2015 and December 31, 2014, respectively.

## 6. Contingencies

### Litigation

The Company and its insurers are plaintiffs in a lawsuit against Sonitrol Corporation. The case arose from the December 21, 2002 arson fire at the Denver warehouse, in which Sonitrol failed to detect and respond to a four-hour burglary and subsequent arson. In 2010, a jury found in favor of the Company and its insurers. Sonitrol appealed the judgment to the Colorado Appellate Court and on July 19, 2012, the Appellate Court upheld the trial court’s ruling on two of the three issues being appealed but set aside the judgment and remanded the case back to the District Court for trial on the sole issue of damages. On April 29, 2013, the Colorado Supreme Court denied Sonitrol’s appeal and the case was returned to the District Court to resolve the sole issue of damages. On April 11, 2014, the damages trial concluded with a jury award of $2.75 million in favor of the Company and its insurers, finding that Sonitrol was liable for damages related only to the burglary and not the subsequent arson. The District Court denied the Company’s motion for post-judgment relief on June 26, 2014. The Company and its insurers have appealed the District Court’s decision. The Company and Sonitrol have filed their briefs and replies in the appeal and await the next step in the process, which is oral argument. The Company is unable to predict when this litigation will be resolved and its ultimate outcome. Any monetary recovery from this lawsuit will be recognized only if and when it is finally paid to the Company.

The Company is subject to certain legal proceedings, claims, investigations and administrative proceedings in the ordinary course of its business. The Company records a provision for a liability when it is both probable that the liability has been incurred and the amount of the liability can be reasonably estimated. These provisions, if any, are reviewed at least quarterly and adjusted to reflect the impacts of negotiations, settlements, rulings, advice of legal counsel and other information and events pertaining to a particular case. In the opinion of management, the outcome of pending litigation is not expected to have a material effect on the Company’s results of operations or financial condition.

## 7. Income Taxes

The Company’s effective tax rates were 37.6% and 38.2% for the three and nine months ended September 30, 2015, respectively, compared to 31.5% and 36.0% for the same periods in 2014. The provision for income taxes for the three and nine months ended September 30, 2015 included a net benefit of $0.4 million, compared to a net benefit of $1.6 million for the same periods in 2014, related primarily to adjustments of prior year’s estimates and the expiration of statute of limitations for uncertain tax positions, which reduced the Company’s effective tax rates.

The total gross amount of unrecognized tax benefits related to federal, state and foreign taxes was approximately $0.4 million at both September 30, 2015 and December 31, 2014, all of which would impact the Company’s effective tax rate, if recognized. The expiration of the statute of limitations for certain tax positions in future years could impact the total gross amount of unrecognized tax benefits by $0.2 million through September 30, 2016.

The Company files U.S. federal, state and foreign income tax returns in jurisdictions with varying statutes of limitations. The 2012 to 2014 tax years remain subject to examination by federal authorities. The 2012 to 2014 tax years remain subject to examination by state authorities with the 2010 and 2011 tax years still open for certain state tax authorities. The 2008 to 2014 tax years remain subject to examination by the tax authorities in Canada.

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8. Employee Benefit Plans

The Company sponsored a qualified defined-benefit pension plan and a post-retirement benefit plan (collectively, "the Pension Plans"). The plans were frozen as of September 30, 1986, and since then there have been no new entrants to the Pension Plans.

The following table provides the components of the net periodic benefit cost (income) of the qualified defined-benefit pension plan (in millions):

| | Three Months Ended September 30, | | Nine Months Ended September 30, | |
|---|---|---|---|---|
| | 2015 | 2014 | 2015 | 2014 |
| PENSION BENEFITS | | | | |
| Interest cost | $0.5 | $0.5 | $1.3 | $1.3 |
| Expected return on plan assets | (0.5) | (0.7) | (1.5) | (1.9) |
| Amortization of net actuarial loss | 0.2 | 0.1 | 0.5 | 0.3 |
| Settlement charge | 0.9 | — | 0.9 | — |
| Net periodic benefit cost (income) | $1.1 | $(0.1) | $1.2 | $(0.3) |

The net periodic benefit costs incurred related to the post-retirement benefit plan were zero and $0.1 million for the three and nine months ended September 30, 2015 and 2014.

The Company made no contributions to the Pension Plans during the three and nine months ended September 30, 2015, compared to contributions of $1.9 million and $3.5 million for the three and nine months ended September 30, 2014, respectively. No minimum contribution to the defined-benefit pension plan is required in 2015. During the remainder of 2015, the Company expects to contribute a total of $0.2 million to the post-retirement benefit plan.

The Company offers certain plan participants the option to receive a lump sum payment in lieu of future annuity pension benefits. For the nine months ended September 30, 2015 the Company had settled accumulated benefits of $1.9 million (pre-tax) for participants who accepted lump sum payments. The Company re-measured its plan obligation as of September 30, 2015 and recorded a settlement charge of $0.9 million, as the lump sum payments exceeded thresholds calculated under GAAP. In addition, the Company recognized a $2.5 million deferred actuarial loss in accumulated other comprehensive loss, increasing the pension liability by the same amount. The Company expects to recognize additional settlement charges between $0.7 million and $1.0 million in the fourth quarter of 2015 related to lump sum payments and other pension settlement activities.

9. Earnings Per Share

The following tables set forth the computation of basic and diluted net income per common share (dollars and shares in millions, except per share amounts):

| | Three Months Ended September 30, 2015 | | | 2014 | | |
|---|---|---|---|---|---|---|
| | Net Income | Weighted-Average Shares Outstanding | Net Income Per Common Share | Net Income | Weighted-Average Shares Outstanding | Net Income Per Common Share |
| Basic EPS | $15.1 | 23.1 | $0.65 | $13.7 | 23.1 | $0.59 |
| Effect of dilutive common share equivalents: | | | | | | |
| Restricted stock units | | 0.1 | — | | 0.1 | — |
| Stock options | | — | — | | 0.1 | — |
| Performance shares | | 0.1 | — | | — | — |
| Diluted EPS | $15.1 | 23.3 | 1,233,856 | 1,854,889 | | |
| | 1,298 | 2,148 | 1,256 | 2,354 | | |

| | | | | |
|---|---|---|---|---|
| Dilutive effect of stock awards | | | | |
| Weighted average common and incremental shares | 1,227,277 | 1,850,427 | 1,235,112 | 1,857,243 |
| | | | | |
| Number of share-based awards excluded from the calculation | - | - | - | - |

The Company’s common stock is $0.50 stated value. The following table presents shares authorized, issued and outstanding.

| | June 30, 2016 | December 31, 2015 |
|---|---|---|
| Common stock authorized | 2,500,000 | 2,500,000 |
| | | |
| Common stock issued | 2,142,202 | 2,142,202 |
| Treasury stock held by the Company | (75,338 ) | (75,511 ) |
| Outstanding shares | 2,066,864 | 2,066,691 |
| Proportional ownership of the Company's common stock in investment partnerships | (850,839 ) | (807,069 ) |
| Net outstanding shares for financial reporting purposes | 1,216,025 | 1,259,622 |

Note 4. Investments

Investments consisted of the following.

| | June 30, 2016 | December 31, 2015 |
|---|---|---|
| Cost | $21,450 | $24,842 |
| Gross unrealized gains | 36 | 10 |
| Gross unrealized losses | (225 ) | (1,102 ) |
| Fair value | $21,261 | $23,750 |

Investment gains/losses are recognized when investments are sold (as determined on a specific identification basis) or as otherwise required by GAAP. The timing of realized gains and losses from sales can have a material effect on periodic earnings. However, such realized gains or losses usually have little, if any, impact on total shareholders’ equity because the investments are carried at fair value with any unrealized gains/losses included as a component of accumulated other comprehensive income in shareholders’ equity. We believe that realized investment gains/losses are often meaningless in terms of understanding reported results. Short-term investment gains/losses have caused and may continue to cause volatility in our results.

Investments in equity securities and a related put option of $4,464 are included in other assets and recorded at fair value.

Note 5. Investment Partnerships

The Company reports on the limited partnership interests in investment partnerships under the equity method of accounting. We record our proportional share of equity in the investment partnerships but exclude Company common stock held by said partnerships. The Company's pro-rata share of its common stock held by the investment partnerships is recorded as treasury stock even though they are legally outstanding. The Company records gains/losses from investment partnerships (inclusive of the investment partnerships' unrealized gains and losses on their securities) in the consolidated statements of earnings based on our carrying value of these partnerships. The fair value is calculated net of the general partner's accrued incentive fees. Gains and losses on Company common stock included in the earnings of these partnerships are eliminated because they are recorded as treasury stock.

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Note 5. Investment Partnerships (continued)

The fair value and adjustment for Company common stock held by the investment partnerships to determine carrying value of our partnership interest is presented below.

| | Fair Value | Company Common Stock | Carrying Value |
|---|---|---|---|
| Partnership interest at December 31, 2015 | $734,668 | $262,979 | $471,689 |
| Investment partnership gains | 189,857 | 59,335 | 130,522 |
| Contributions (net of distributions) to investment partnerships | 5,894 | | 5,894 |
| Increase in proportionate share of Company stock held | | 16,221 | (16,221) |
| Partnership interest at June 30, 2016 | $930,419 | $338,535 | $591,884 |

| | Fair Value | Company Common Stock | Carrying Value |
|---|---|---|---|
| Partnership interest at December 31, 2014 | $776,899 | $78,917 | $697,982 |
| Investment partnership gains | 20,155 | 2,747 | 17,408 |
| Contributions (net of distributions) to investment partnerships | 63,000 | | 63,000 |
| Increase in proportionate share of Company stock held | | 8,810 | (8,810) |
| Partnership interest at June 30, 2015 | $860,054 | $90,474 | $769,580 |

The fair value of the investment partnerships net of deferred taxes is presented below.

| | June 30, 2016 | December 31, 2015 |
|---|---|---|
| Fair value of investment partnerships | $930,419 | $734,668 |
| Deferred tax liability related to investment partnerships | (162,097) | (115,952) |
| Fair value of investment partnerships net of deferred taxes | $768,322 | $618,716 |

The Company's proportionate share of Company stock held by investment partnerships at cost is $349,048 and $332,827 at June 30, 2016 and December 31, 2015, respectively, and is recorded as treasury stock.

The carrying value of the partnership interest approximates fair value adjusted by changes in the value of held Company stock. Fair value is according to our proportional ownership interest of the fair value of investments held by the investment partnerships. The fair value measurement is classified as level 3 within the fair value hierarchy.

Gains from investment partnerships recorded in the Company's consolidated statements of earnings are presented below.

| | Second Quarter | | First Six Months | |
|---|---|---|---|---|
| | 2016 | 2015 | 2016 | 2015 |
| Investment partnership gains (losses) | $51,549 | $(5,557) | $130,522 | $17,408 |
| Loss on contribution of securities to investment partnership | (306) | - | (306) | - |
| Investment partnership gains (losses) | 51,243 | (5,557) | 130,216 | 17,408 |
| Tax expense (benefit) | 18,171 | (3,002) | 46,756 | 4,851 |
| Contribution to net earnings | $33,072 | $(2,555) | $83,460 | $12,557 |

Non-cash investments were $1,219 (net of non-cash distributions) for the first six months of 2016.

As the general partner of the investment partnerships, Biglari Capital Corp. ("Biglari Capital") on December 31 of each year will earn an incentive reallocation fee for the Company's investments equal to 25% of the net profits over an annual hurdle rate of 6% above the previous high-water mark. Our policy is to accrue an estimated incentive fee throughout the year; however, no fees are reallocated until the end of the calendar year. As of June 30, 2016 and 2015, the Company accrued incentive fees for Biglari Capital of $17,857 and $526, respectively. Our investments in these partnerships are committed on a rolling 5-year basis.

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Note 5. Investment Partnerships (continued)

Summarized financial information for The Lion Fund, L.P. and The Lion Fund II, L.P. is presented below.

| | Equity in Investment Partnerships | |
|---|---|---|
| | Lion Fund | Lion Fund II |
| Total assets as of June 30, 2016 | $198,210 | $1,088,067 |
| Total liabilities as of June 30, 2016 | $8,563 | $199,518 |
| Revenue for the first six months ending June 30, 2016 | $9,655 | $223,759 |
| Earnings for the first six months ending June 30, 2016 | $9,563 | $221,154 |
| Biglari Holdings' Ownership Interest | 64.5 % | 93.5% |
| | | |
| Total assets as of December 31, 2015 | $165,996 | $819,323 |
| Total liabilities as of December 31, 2015 | $409 | $141,274 |
| Revenue for the first six months ending June 30, 2015 | $5,112 | $20,171 |
| Earnings for the first six months ending June 30, 2015 | $5,054 | $18,888 |
| Biglari Holdings' Ownership Interest | 59.8 % | 93.3% |

Revenue in the above summarized financial information of the investment partnerships includes investment income and unrealized gains and losses on investments. The investments held by the investment partnerships are largely concentrated in the common stock of one investee, Cracker Barrel Old Country Store, Inc.

Note 6. Property and Equipment

Property and equipment is composed of the following.

| | June 30, 2016 | December 31, 2015 |
|---|---|---|
| Land | $161,886 | $160,697 |
| Buildings | 157,169 | 156,909 |
| Land and leasehold improvements | 164,514 | 165,042 |
| Equipment | 200,419 | 199,934 |
| Construction in progress | 2,974 | 3,478 |
| | 686,962 | 686,060 |
| Less accumulated depreciation and amortization | (362,750 ) | (353,736 ) |
| Property and equipment, net | $324,212 | $332,324 |

Note 7. Goodwill and Other Intangibles

Goodwill

Goodwill consists of the excess of the purchase price over the fair value of the net assets acquired in connection with business acquisitions.

A reconciliation of the change in the carrying value of goodwill is as follows.

| | Restaurants | Other | Total |
|---|---|---|---|
| Goodwill at December 31, 2015 | $28,109 | $11,913 | $40,022 |

| | | | |
|---|---|---|---|
| Change in foreign exchange rates during first six months 2016 | 11 | - | 11 |
| Goodwill at June 30, 2016 | $28,120 | $11,913 | $40,033 |

We are required to assess goodwill and any indefinite-lived intangible assets for impairment annually, or more frequently if circumstances indicate impairment may have occurred. The analysis of potential impairment of goodwill requires a two-step approach. The first is the estimation of fair value of each reporting unit. If step one indicates that impairment potentially exists, the second step is performed to measure the amount of impairment, if any. Goodwill impairment occurs when the estimated fair value of goodwill is less than its carrying value.

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Note 7. Goodwill and Other Intangibles (continued)

The valuation methodology and underlying financial information included in our determination of fair value require significant management judgments. We use both market and income approaches to derive fair value. The judgments in these two approaches include, but are not limited to, comparable market multiples, long-term projections of future financial performance, and the selection of appropriate discount rates used to determine the present value of future cash flows. Changes in such estimates or the application of alternative assumptions could produce significantly different results. No impairment charges for goodwill were recorded in the first six months of 2016 or 2015.

Other Intangibles

Other intangibles are composed of the following.

| | June 30, 2016 | | | December 31, 2015 | | |
|---|---|---|---|---|---|---|
| | Gross carrying amount | Accumulated amortization | Total | Gross carrying amount | Accumulated amortization | Total |
| Franchise agreement | $ 5,310 | $ (3,319 ) | $ 1,991 | $ 5,310 | $ (3,054 ) | $ 2,256 |
| Other | 810 | (687 ) | 123 | 810 | (667 ) | 143 |
| Total | 6,120 | (4,006 ) | 2,114 | 6,120 | (3,721 ) | 2,399 |
| Intangible assets with indefinite lives: | | | | | | |
| Trade names | 15,876 | - | 15,876 | 15,876 | - | 15,876 |
| Other assets with indefinite lives | 3,474 | - | 3,474 | 3,398 | - | 3,398 |
| Total intangible assets | $ 25,470 | $ (4,006 ) | $ 21,464 | $ 25,394 | $ (3,721 ) | $ 21,673 |

Intangible assets subject to amortization consist of franchise agreements connected with the purchase of Western as well as rights to favorable leases related to prior acquisitions. These intangible assets are being amortized over their estimated weighted average of useful lives ranging from eight to twelve years.

Amortization expense for the first six months of 2016 and 2015 was $285 and $286, respectively. Total annual amortization expense for years 2017 through 2019 will approximate $560 per year. The Company's intangible assets with definite lives will fully amortize in 2020.

Intangible assets with indefinite lives consist of trade names, franchise rights as well as lease rights.

Note 8. Restaurant Operations Revenues

Restaurant operations revenues were as follows.

| | Second Quarter | | First Six Months | |
|---|---|---|---|---|
| | 2016 | 2015 | 2016 | 2015 |
| Net sales | $205,082 | $206,278 | $400,149 | $398,448 |
| Franchise royalties and fees | 4,784 | 4,420 | 9,134 | 8,076 |
| Other | 843 | 933 | 1,721 | 1,843 |
| | $210,709 | $211,631 | $411,004 | $408,367 |

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Note 9. Borrowings

Notes payable and other borrowings include the following.

| Current portion of notes payable and other borrowings | June 30, 2016 | December 31, 2015 |
|---|---|---|
| Notes payable | $2,200 | $2,200 |
| Unamortized original issue discount | (302) | (296) |
| Unamortized debt issuance costs | (700) | (688) |
| Obligations under leases | 5,575 | 5,787 |
| Western revolver | 530 | 786 |
| Total current portion of notes payable and other borrowings | $7,303 | $7,789 |
| | | |
| Long-term notes payable and other borrowings | | |
| Notes payable | $201,998 | $210,175 |
| Unamortized original issue discount | (1,250) | (1,403) |
| Unamortized debt issuance costs | (2,533) | (2,888) |
| Obligations under leases | 88,116 | 90,178 |
| Total long-term notes payable and other borrowings | $286,331 | $296,062 |

ASU 2015-03 requires debt issuance costs to be presented in the balance sheet as a direct deduction from the carrying amount of the debt liability. As of December 31, 2015, the Company reclassified unamortized debt issuance costs from other assets to notes payable and other borrowings.

Steak n Shake Credit Facility
On March 19, 2014, Steak n Shake and its subsidiaries entered into a new credit agreement. This credit agreement provides for a senior secured term loan facility in an aggregate principal amount of $220,000 and a senior secured revolving credit facility in an aggregate principal amount of up to $30,000.

The term loan is scheduled to mature on March 19, 2021. It amortizes at an annual rate of 1.0% in equal quarterly installments, beginning June 30, 2014, at 0.25% of the original principal amount of the term loan, subject to mandatory prepayments from excess cash flow, asset sales and other events described in the credit agreement. The balance will be due at maturity. The revolver will be available on a revolving basis until March 19, 2019.

Steak n Shake has the right to request an incremental term loan facility from participating lenders and/or eligible assignees at any time, up to an aggregate total principal amount not to exceed $70,000 if certain customary conditions within the credit agreement are met.

Borrowings bear interest at a rate per annum equal to a base rate or a Eurodollar rate (minimum of 1%) plus an applicable margin. Interest on the term loan is based on a Eurodollar rate plus an applicable margin of 3.75% or on the prime rate plus an applicable margin of 2.75%. Interest on loans under the revolver is based on a Eurodollar rate plus an applicable margin ranging from 2.75% to 4.25% or on the prime rate plus an applicable margin ranging from 1.75% to 3.25%. The applicable margins on revolver loans are contingent on Steak n Shake's total leverage ratio. The revolver also carries a commitment fee ranging from 0.40% to 0.50% per annum, depending on Steak n Shake's total leverage ratio, on the unused portion of the revolver.

The interest rate on the term loan was 4.75% as of June 30, 2016.

The credit agreement includes customary affirmative and negative covenants and events of default, as well as a financial maintenance covenant, solely with respect to the revolver, relating to the maximum total leverage ratio. Steak n Shake's credit facility contains restrictions on its ability to pay dividends to Biglari Holdings.

Both the term loan and the revolver have been secured by first priority security interests in substantially all the assets of Steak n Shake. Biglari Holdings is not a guarantor under the credit facility. As of June 30, 2016, $204,198 was outstanding under the term loan, and no amount was outstanding under the revolver.

Steak n Shake had $10,188 in standby letters of credit outstanding as of June 30, 2016 and December 31, 2015.

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Note 9. Borrowings (continued)

Western Revolver
As of June 30, 2016, Western has $530 due December 13, 2016.

Fair Value of Debt
The carrying amounts for debt reported in the consolidated balance sheet did not differ materially from their fair values at June 30, 2016 and December 31, 2015. The fair value was determined to be a Level 3 fair value measurement.

Note 10. Accumulated Other Comprehensive Income

During the first six months of 2016 and 2015, the changes in the balances of each component of accumulated other comprehensive income, net of tax, were as follows.

| | Six months ended June 30, 2016 | | | Six months ended June 30, 2015 | | |
|---|---|---|---|---|---|---|
| | Foreign Currency Translation Adjustments | Investment Gain (Loss) | Accumulated Other Comprehensive Income (Loss) | Foreign Currency Translation Adjustments | Investment Gain (Loss) | Accumulated Other Comprehensive Income (Loss) |
| Beginning Balance | $(2,992) | $(687) | $ (3,679) | $(620) | $(163) | $ (783) |
| Other comprehensive income (loss) before reclassifications | 121 | 368 | 489 | 128 | (343) | (215) |
| Reclassification to (earnings) loss | - | 193 | 193 | - | 36 | 36 |
| Ending Balance | $(2,871) | $(126) | $ (2,997) | $(492) | $(470) | $ (962) |

Reclassifications made from accumulated other comprehensive income to the consolidated statement of earnings during the first six months of 2016 and 2015 were as follows.

| Reclassifications from Accumulated Other Comprehensive Income | 2016 | 2015 | Affected Line Item in the Consolidated Statement of Earnings |
|---|---|---|---|
| Investment gain | $- | $(55) | Insurance premiums and other |
| | (306) | - | Investment partnership gains (losses) |
| | (113) | (19) | Income tax expense (benefit) |
| | $(193) | $(36) | Net of tax |

During the second quarters of 2016 and 2015, the changes in the balances of each component of accumulated other comprehensive income, net of tax, were as follows.

| | Second Quarter 2016 | | | Second Quarter 2015 | | |
|---|---|---|---|---|---|---|
| | Foreign Currency Translation Adjustments | Investment Gain (Loss) | Accumulated Other Comprehensive Income (Loss) | Foreign Currency Translation Adjustments | Investment Gain (Loss) | Accumulated Other Comprehensive Income (Loss) |
| Beginning Balance | $(2,661) | $(943) | $ (3,604) | $(557) | $(426) | $ (983) |
| Other comprehensive income (loss) before reclassifications | (210) | 624 | 414 | 65 | (80) | (15) |

| | | | | | | |
|---|---|---|---|---|---|---|
| Reclassification to (earnings) loss | - | 193 | 193 | - | 36 | 36 |
| Ending Balance | $(2,871 ) | $(126 ) | $ (2,997 ) | $(492 ) | $(470 ) | $ (962 ) |

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Note 10. Accumulated Other Comprehensive Income (continued)

Reclassifications made from accumulated other comprehensive income to the consolidated statement of earnings during the second quarters of 2016 and 2015 were as follows.

| Reclassifications from Accumulated Other Comprehensive Income | Second Quarter 2016 | Second Quarter 2015 | Affected Line Item in the Consolidated Statement of Earnings |
|---|---|---|---|
| Investment gain | $- | $(55) | Insurance premiums and other |
| | (306) | - | Investment partnership gains (losses) |
| | (113) | (19) | Income tax expense (benefit) |
| | $(193) | $(36) | Net of tax |

Note 11. Income Taxes

In determining the quarterly provision for income taxes, the Company uses an estimated annual effective tax rate based on expected annual income, statutory tax rates, and available tax planning opportunities in the various jurisdictions in which the Company operates. Unusual or infrequently occurring items are separately recognized during the quarter in which they occur.

Income tax expense for the second quarter of 2016 was $19,562 compared to a tax benefit of $2,203 for the second quarter of 2015. Income tax expense for the first six months of 2016 was $49,140 compared to $4,987 for the first six months of 2015. The variance in income tax expense between 2016 and 2015 is primarily attributable to tax expense on income from investment partnerships. The tax expense for investment partnership gains was $18,171 during the second quarter of 2016 compared to a tax benefit for investment partnership losses of $3,002 during the second quarter of 2015, and the tax expense for investment partnership gains was $46,756 during the first six months of 2016 compared to $4,851 during the first six months of 2015.

As of June 30, 2016 and December 31, 2015, we had approximately $476 and $413, respectively, of unrecognized tax benefits, which are included in other liabilities in the consolidated balance sheets.

Note 12. Commitments and Contingencies

We are involved in various legal proceedings and have certain unresolved claims pending. We believe, based on examination of these matters and experiences to date, that the ultimate liability, if any, in excess of amounts already provided in our consolidated financial statements is not likely to have a material effect on our results of operations, financial position or cash flows.

In 2013 two shareholders of the Company filed derivative actions putatively on behalf of the Company against the members of our Board of Directors in the United States District Courts for the Southern District of Indiana and the Western District of Texas. The actions were consolidated in the Southern District of Indiana in 2014. On March 18, 2015, the United States District Court for the Southern District of Indiana granted a motion to dismiss the derivative actions in favor of the Company. In addition, the Court issued judgment on all counts in favor of the Company and its directors.

The two shareholders appealed the Southern District of Indiana Court's March 18, 2015 decision. On February 17, 2016, the United States Court of Appeals for the Seventh Circuit affirmed the decision of the District Court dismissing, in their entirety, all claims made against the Company and its Board of Directors.

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Note 13. Fair Value of Financial Assets and Liabilities

The fair values of substantially all of our financial instruments were measured using market or income approaches. Considerable judgment may be required in interpreting market data used to develop the estimates of fair value. Accordingly, the fair values presented are not necessarily indicative of the amounts that could be realized in an actual current market exchange. The use of alternative market assumptions and/or estimation methodologies may have a material effect on the estimated fair value. The hierarchy for measuring fair value consists of Levels 1 through 3, which are described below.

- Level 1 – Inputs represent unadjusted quoted prices for identical assets or liabilities exchanged in active markets.

- Level 2 – Inputs include directly or indirectly observable inputs (other than Level 1 inputs) such as quoted prices for similar assets or liabilities exchanged in active or inactive markets; quoted prices for identical assets or liabilities exchanged in inactive markets; other inputs that may be considered in fair value determinations of the assets or liabilities, such as interest rates and yield curves, volatilities, prepayment speeds, loss severities, credit risks and default rates; and inputs that are derived principally from or corroborated by observable market data by correlation or other means. Pricing evaluations generally reflect discounted expected future cash flows, which incorporate yield curves for instruments with similar characteristics, such as credit ratings, estimated durations and yields for other instruments of the issuer or entities in the same industry sector.

- Level 3 – Inputs include unobservable inputs used in the measurement of assets and liabilities. Management is required to use its own assumptions regarding unobservable inputs because there is little, if any, market activity in the assets or liabilities and we may be unable to corroborate the related observable inputs. Unobservable inputs require management to make certain projections and assumptions about the information that would be used by market participants in pricing assets or liabilities.

The following methods and assumptions were used to determine the fair value of each class of the following assets and liabilities recorded at fair value in the consolidated balance sheet:

Cash equivalents: Cash equivalents primarily consist of money market funds which are classified within Level 1 of the fair value hierarchy.

Equity securities: The Company’s investments in equity securities are classified within Level 1 of the fair value hierarchy.

Bonds: The Company’s investments in bonds are classified within Level 2 of the fair value hierarchy.

Non-qualified deferred compensation plan investments: The assets of the non-qualified plan are set up in a rabbi trust. They represent mutual funds and are classified within Level 1 of the fair value hierarchy.

Derivative instruments: Options related to equity securities and interest rate swaps are marked to market each reporting period and are classified within Level 2 of the fair value hierarchy.

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Note 13. Fair Value of Financial Assets and Liabilities (continued)

As of June 30, 2016 and December 31, 2015, the fair values of financial assets and liabilities were as follows.

| | June 30, 2016 | | | | December 31, 2015 | | | |
|---|---|---|---|---|---|---|---|---|
| | Level 1 | Level 2 | Level 3 | Total | Level 1 | Level 2 | Level 3 | Total |
| Assets | | | | | | | | |
| Cash equivalents | $504 | $- | $- | $504 | $700 | $- | $- | $700 |
| Equity securities: | | | | | | | | |
| Insurance | - | - | - | - | 5,046 | - | - | 5,046 |
| Consumer goods | 2,531 | - | - | 2,531 | - | - | - | - |
| Bonds | - | 23,893 | - | 23,893 | - | 21,304 | - | 21,304 |
| Options on equity securities | - | 1,933 | - | 1,933 | - | - | - | - |
| Non-qualified deferred compensation plan investments | 2,498 | - | - | 2,498 | 2,203 | - | - | 2,203 |
| Total assets at fair value | $5,533 | $25,826 | $- | $31,359 | $7,949 | $21,304 | $- | $29,253 |
| | | | | | | | | |
| Liabilities | | | | | | | | |
| Interest rate swaps | $- | $- | $- | $- | $- | $2 | $- | $2 |
| Total liabilities at fair value | $- | $- | $- | $- | $- | $2 | $- | $2 |

There were no changes in our valuation techniques used to measure fair values on a recurring basis.

Note 14. Related Party Transactions

In 2013 Biglari Holdings entered into the following agreements with Mr. Biglari, its Chairman and Chief Executive Officer: (i) a Stock Purchase Agreement for the sale of Biglari Capital to Mr. Biglari (the "Biglari Capital Transaction"); (ii) a Shared Services Agreement with Biglari Capital, and (iii) a First Amendment to the Amended and Restated Incentive Bonus Agreement with Mr. Biglari (the "Incentive Agreement Amendment"). The transactions contemplated thereby were unanimously approved by the independent Governance, Compensation and Nominating Committee of the Board of Directors of the Company (the "Committee"), which retained separate counsel, tax/accounting advisors, an independent compensation consultant, and a financial advisor to assist the Committee in the structuring, evaluation, and negotiation of such transactions.

Shared Services Agreement

Connected with the Biglari Capital Transaction, Biglari Holdings and Biglari Capital entered into the Shared Services Agreement pursuant to which Biglari Holdings provides certain services to Biglari Capital in exchange for a 6% hurdle rate for Biglari Holdings and its subsidiaries (as compared to a 5% hurdle rate for all other limited partners) in order to determine the incentive reallocation to Biglari Capital, as general partner of The Lion Fund, L.P. and The Lion Fund II, L.P., under their respective partnership agreements. The incentive reallocation to Biglari Capital is equal to 25% of the net profits allocated to the limited partners in excess of their applicable hurdle rate above the previous high-water mark. The Shared Services Agreement runs for an initial five-year term, and automatically renews for successive five-year periods, unless terminated by either party effective at the end of the initial or the renewed term, as applicable. The term of the Shared Services Agreement coincides with the lock-up period for the Company's investments in The Lion Fund, L.P. and The Lion Fund II, L.P. under their respective partnership agreements. The Company provided services for Biglari Capital under the Shared Services Agreement costing an aggregate of $351 and $3,706 for the second quarters of 2016 and 2015, respectively, and $652 and $3,791 for the first six months of 2016 and 2015, respectively.

Investments in The Lion Fund, L.P. and The Lion Fund II, L.P.
As of June 30, 2016, the Company's investments in The Lion Fund, L.P. and The Lion Fund II, L.P. had a fair value of $930,419.

As the general partner of the investment partnerships, Biglari Capital on December 31 of each year will earn an incentive reallocation fee for the Company's investments equal to 25% of the net profits over an annual hurdle rate of 6% above the previous high-water mark. Our policy is to accrue an estimated incentive fee throughout the year; however, no fees are reallocated until the end of the calendar year. The Company accrued $17,857 and $526 in incentive fees for Biglari Capital during the first six months of 2016 and 2015, respectively.

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Note 14. Related Party Transactions (continued)

Incentive Agreement Amendment
Also in connection with the Biglari Capital Transaction, Biglari Holdings and Mr. Biglari entered into the Incentive Agreement Amendment which amends the Amended and Restated Incentive Bonus Agreement with Mr. Biglari to reflect and give effect to the Biglari Capital Transaction, which excludes earnings by the investment partnerships from the calculation of Mr. Biglari's incentive bonus.

License Agreement
In 2013 the Company entered into a Trademark License Agreement (the "License Agreement") with Mr. Biglari. The License Agreement was unanimously approved by the Committee. In addition, the license under the License Agreement is provided on a royalty-free basis in the absence of specified extraordinary events described below. Accordingly, the Company and its subsidiaries have paid no royalties to Mr. Biglari under the License Agreement since its inception.

Under the License Agreement, Mr. Biglari granted to the Company an exclusive license to use the Biglari and Biglari Holdings names (the "Licensed Marks") in association with various products and services (collectively the "Products and Services"). Upon (a) the expiration of twenty years from the date of the License Agreement (subject to extension as provided in the License Agreement), (b) Mr. Biglari's death, (c) the termination of Mr. Biglari's employment by the Company for Cause (as defined in the License Agreement), or (d) Mr. Biglari's resignation from his employment with the Company absent an Involuntary Termination Event (as defined in the License Agreement), the Licensed Marks for the Products and Services will transfer from Mr. Biglari to the Company, without any compensation, if the Company is continuing to use the Licensed Marks in the ordinary course of its business. Otherwise, the rights will revert to Mr. Biglari.

If (i) a Change of Control (as defined in the License Agreement) of the Company; (ii) the termination of Mr. Biglari's employment by the Company without Cause; or (iii) Mr. Biglari's resignation from his employment with the Company due to an Involuntary Termination Event (each, a "Triggering Event") were to occur, Mr. Biglari would be entitled to receive a 2.5% royalty on "Revenues" with respect to the "Royalty Period." The royalty payment to Mr. Biglari would not apply to all revenues received by Biglari Holdings and its subsidiaries nor would it apply retrospectively (i.e., to revenues received with respect to the period prior to the Triggering Event). The royalty would apply to revenues recorded by the Company on an accrual basis under GAAP, solely with respect to the defined period of time after the Triggering Event equal to the Royalty Period, from a covered Product, Service or business that (1) has used the Biglari Holdings or Biglari name at any time during the term of the License Agreement, whether prior to or after a Triggering Event, or (2) the Company has specifically identified, prior to a Triggering Event, will use the name Biglari or Biglari Holdings.

"Revenues" means all revenues received, on an accrual basis under GAAP, by the Company, its subsidiaries and affiliates from the following: (1) all Products and Services covered by the License Agreement bearing or associated with the names Biglari and Biglari Holdings at any time (whether prior to or after a Triggering Event). This category would include, without limitation, the use of Biglari or Biglari Holdings in the public name of a business providing any covered Product or Service; and (2) all covered Products, Services and businesses that the Company has specifically identified, prior to a Triggering Event, will bear, use or be associated with the name Biglari or Biglari Holdings.

The Committee unanimously approved the association of the Biglari name and mark with all of Steak n Shake's restaurants (including Company operated and franchised locations), products and brands. On May 14, 2013, the Company, Steak n Shake, LLC and Steak n Shake Enterprises, Inc. entered into a Trademark Sublicense Agreement in connection therewith. Accordingly, revenues received by the Company, its subsidiaries and affiliates from Steak n

Shake’s restaurants, products and brands would come within the definition of Revenues for purposes of the License Agreement.

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Note 14. Related Party Transactions (continued)

The “Royalty Period” is a defined period of time, after the Triggering Event, calculated as follows: (i) if, following three months after a Triggering Event, the Company or any of its subsidiaries or affiliates continues to use the Biglari or Biglari Holdings name in connection with any covered product or service, or continues to use Biglari as part of its corporate or public company name, then the “Royalty Period” will equal (a) the period of time during which the Company or any of its subsidiaries or affiliates continues any such use, plus (b) a period of time after the Company, its subsidiaries and affiliates have ceased all uses of the names Biglari and Biglari Holdings equal to the length of the term of the License Agreement prior to the Triggering Event, plus three years. As an example, if a Triggering Event occurs five years after the date of the License Agreement, and the Company ceases all uses of the Biglari and Biglari Holdings names two years after the Triggering Event, the Royalty Period will equal a total of ten years (the sum of two years after the Triggering Event during which the Biglari and Biglari Holdings names are being used, plus a period of time equal to the five years prior to the Triggering Event, plus three years); or (ii) if the Company, its subsidiaries and affiliates cease all uses of the Biglari and Biglari Holdings names within three months after a Triggering Event, then the “Royalty Period” will equal the length of the term of the License Agreement prior to the Triggering Event, plus three years. As an example, if a Triggering Event occurs five years after the date of the License Agreement, and the Company ceases all uses of the Biglari and Biglari Holdings names two months after the Triggering Event, the Royalty Period will equal a total of eight years (the sum of the period of time equal to the five years prior to the Triggering Event, plus three years). Notwithstanding the above methods of determining the Royalty Period, the minimum Royalty Period is five years after a Triggering Event.

Note 15. Business Segment Reporting

Our reportable business segments are organized in a manner that reflects how management views those business activities. Certain businesses have been grouped together for segment reporting based upon operations.

Our restaurant operations includes Steak n Shake and Western. As a result of the acquisitions of Maxim and First Guard, the Company reports segment information for these businesses. Prior to the fourth quarter of 2015, other business activities not specifically identified with reportable business segments were presented in corporate. Such other business activities are now presented in “other” within total operating businesses. Prior periods have been reclassified to conform to the current presentation. We report our earnings from investment partnerships separate from corporate.

We assess and measure segment operating results based on segment earnings as disclosed below. Segment earnings from operations are neither necessarily indicative of cash available to fund cash requirements, nor synonymous with cash flow from operations.

The tabular information that follows shows data of our reportable segments reconciled to amounts reflected in the consolidated financial statements.

Revenue by segment for the second quarters and first six months of 2016 and 2015 were as follows.

| | Second Quarter | | First Six Months | |
|---|---|---|---|---|
| | 2016 | 2015 | 2016 | 2015 |
| Operating Businesses: | | | | |
| Restaurant Operations: | | | | |
| Steak n Shake | $206,828 | $207,848 | $403,726 | $401,301 |
| Western | 3,881 | 3,783 | 7,278 | 7,066 |
| Total Restaurant Operations | 210,709 | 211,631 | 411,004 | 408,367 |

| | | | | |
|---|---|---|---|---|
| First Guard | 5,731 | 3,717 | 11,230 | 7,371 |
| Maxim | 2,673 | 6,608 | 5,121 | 12,046 |
| | $219,113 | $221,956 | $427,355 | $427,784 |

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Note 15. Business Segment Reporting (continued)

Earnings (losses) before income taxes by segment for the second quarters and first six months of 2016 and 2015 were as follows.

| | Second Quarter | | First Six Months | |
|---|---|---|---|---|
| | 2016 | 2015 | 2016 | 2015 |
| Operating Businesses: | | | | |
| Restaurant Operations: | | | | |
| Steak n Shake | $12,144 | $13,815 | $20,506 | $20,050 |
| Western | 837 | 688 | 1,423 | 1,098 |
| Total Restaurant Operations | 12,981 | 14,503 | 21,929 | 21,148 |
| First Guard | 2,098 | 1,139 | 3,425 | 1,799 |
| Maxim | (3,321) | (4,173) | (6,836) | (10,059) |
| Other | 140 | 90 | 265 | 147 |
| Total Operating Businesses | 11,898 | 11,559 | 18,783 | 13,035 |
| Corporate and Investments: | | | | |
| Corporate | (3,189) | (5,182) | (5,384) | (9,444) |
| Investment partnership gains (losses) | 51,243 | (5,557) | 130,216 | 17,408 |
| Total Corporate and Investments | 48,054 | (10,739) | 124,832 | 7,964 |
| Interest expense on notes payable and other borrowings | (2,873) | (2,997) | (5,795) | (6,003) |
| | $57,079 | $(2,177) | $137,820 | $14,996 |

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

(dollars in thousands except per share data)

Overview

Biglari Holdings Inc. ("Biglari Holdings" or the "Company") is a holding company owning subsidiaries engaged in a number of diverse business activities, including media, property and casualty insurance, and restaurants. The Company's largest operating subsidiaries are involved in the franchising and operating of restaurants. Biglari Holdings is founded and led by Sardar Biglari, Chairman and Chief Executive Officer of Biglari Holdings and its major operating subsidiaries. The Company's long-term objective is to maximize per-share intrinsic value. All major operating, investment, and capital allocation decisions are made for the Company and its subsidiaries by Mr. Biglari.

The Lion Fund II, L.P., a private investment partnership of which Mr. Biglari controls the general partner, purchased 24,000 shares of Biglari Holdings common stock from January 4, 2016 through February 3, 2016 and 13,095 shares from May 24, 2016 through June 30, 2016 pursuant to Rule 10b5-1 Trading Plans. As of June 30, 2016, Mr. Biglari's beneficial ownership of the Company's outstanding common stock was approximately 51.3%.

Net earnings attributable to Biglari Holdings shareholders for the second quarters and first six months of 2016 and 2015 are disaggregated in the table that follows. Amounts are recorded after deducting income taxes.

| | Second Quarter | | First Six Months | |
|---|---|---|---|---|
| | 2016 | 2015 | 2016 | 2015 |
| Operating businesses: | | | | |
| Restaurant | $8,660 | $9,320 | $14,138 | $12,968 |
| Insurance | 1,372 | 742 | 2,248 | 1,178 |
| Media | (2,099) | (2,692) | (4,336) | (6,592) |
| Other | 73 | 23 | 132 | 3 |
| Total operating businesses | 8,006 | 7,393 | 12,182 | 7,557 |
| Corporate | (1,780) | (2,954) | (3,369) | (6,383) |
| Investment partnership gains (losses) | 33,072 | (2,555) | 83,460 | 12,557 |
| Interest expense on notes payable and other borrowings | (1,781) | (1,858) | (3,593) | (3,722) |
| | $37,517 | $26 | $88,680 | $10,009 |

Our restaurant businesses include Steak n Shake Inc. ("Steak n Shake") and Western Sizzlin Corporation ("Western"). As of June 30, 2016, Steak n Shake comprised 417 company-operated restaurants and 154 franchised units. Western comprised 4 company-operated restaurants and 65 franchised units.

Our insurance business is composed of First Guard Insurance Company and its agency, 1st Guard Corporation (collectively "First Guard"), which we acquired on March 19, 2014. First Guard is a direct underwriter of commercial trucking insurance, selling physical damage and nontrucking liability insurance to truckers.

Our media business is composed of Maxim Inc. ("Maxim"). We acquired certain assets and liabilities of Maxim on February 27, 2014. Maxim's business lies principally in media and licensing.

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

Restaurants

Steak n Shake and Western comprise 640 company-operated and franchised restaurants as of June 30, 2016.

| | Steak n Shake | | Western Sizzlin | | |
|---|---|---|---|---|---|
| | Company-operated | Franchised | Company-operated | Franchised | Total |
| Total stores as of December 31, 2014 | 417 | 128 | 4 | 68 | 617 |
| Net restaurants opened (closed) | - | 8 | - | (2) | 6 |
| Total stores as of June 30, 2015 | 417 | 136 | 4 | 66 | 623 |
| | | | | | |
| Total stores as of December 31, 2015 | 417 | 144 | 4 | 66 | 631 |
| Net restaurants opened (closed) | - | 10 | - | (1) | 9 |
| Total stores as of June 30, 2016 | 417 | 154 | 4 | 65 | 640 |

Earnings of our restaurant operations are summarized below.

| | Second Quarter | | | | First Six Months | | | |
|---|---|---|---|---|---|---|---|---|
| | 2016 | | 2015 | | 2016 | | 2015 | |
| Revenue | | | | | | | | |
| Net sales | $ 205,082 | | $ 206,278 | | $ 400,149 | | $ 398,448 | |
| Franchise royalties and fees | 4,784 | | 4,420 | | 9,134 | | 8,076 | |
| Other revenue | 843 | | 933 | | 1,721 | | 1,843 | |
| Total revenue | 210,709 | | 211,631 | | 411,004 | | 408,367 | |
| | | | | | | | | |
| Restaurant cost of sales | | | | | | | | |
| Cost of food (1) | 56,567 | 27.6 % | 59,743 | 29.0 % | 110,559 | 27.6 % | 116,854 | 29.3 % |
| Restaurant operating costs (1) | 99,714 | 48.6 % | 94,885 | 46.0 % | 196,946 | 49.2 % | 188,212 | 47.2 % |
| Rent (1) | 4,520 | 2.2 % | 4,377 | 2.1 % | 9,033 | 2.3 % | 8,700 | 2.2 % |
| Total cost of sales | 160,801 | | 159,005 | | 316,538 | | 313,766 | |
| | | | | | | | | |
| Selling, general and administrative | | | | | | | | |
| General and administrative (2) | 15,064 | 7.1 % | 16,444 | 7.8 % | 29,044 | 7.1 % | 32,852 | 8.0 % |
| Marketing (2) | 13,405 | 6.4 % | 13,455 | 6.4 % | 25,975 | 6.3 % | 23,385 | 5.7 % |
| Other expenses (2) | 597 | 0.3 % | (196) | -0.1 % | 1,661 | 0.4 % | 164 | 0.0 % |
| Total selling, general and administrative | 29,066 | 13.8 % | 29,703 | 14.0 % | 56,680 | 13.8 % | 56,401 | 13.8 % |
| | | | | | | | | |
| Depreciation and amortization (2) | 5,112 | 2.4 % | 6,010 | 2.8 % | 10,827 | 2.6 % | 12,167 | 3.0 % |
| | | | | | | | | |
| | 2,749 | | 2,410 | | 5,030 | | 4,885 | |

| | | | | |
|---|---|---|---|---|
| Interest on obligations under leases | | | | |
| Earnings before income taxes | 12,981 | 14,503 | 21,929 | 21,148 |
| Income tax expense | 4,321 | 5,183 | 7,791 | 8,180 |
| Contribution to net earnings | $ 8,660 | $ 9,320 | $ 14,138 | $ 12,968 |

(1) Cost of food, restaurant operating costs and rent expense are expressed as a percentage of net sales.
(2) General and administrative, marketing, other expenses and depreciation and amortization are expressed as a percentage of total revenue.

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

Net sales during the second quarter and the first six months of 2016 were $205,082 and $400,149, respectively, representing a decrease of $1,196 over the second quarter and an increase of $1,701 over the first six months of 2015. The changes in performance of our restaurant operations were largely driven by Steak n Shake's same-store sales. Steak n Shake's same-store sales decreased 0.7% and customer traffic decreased 2.1% during the second quarter. Steak n Shake's same store sales increased 0.5% whereas customer traffic decreased 1.1% during the first six months. The term "same-store sales" refers to the sales of company-operated units open at least 18 months at the beginning of the current period and have remained open through the end of the period.

Franchise royalties and fees during the second quarter and first six months of 2016 increased 8.2% and 13.1%, respectively, compared to those in 2015. Steak n Shake opened seven franchise units during the second quarter of 2016. The increase in sales during 2016 is primarily attributable to the revenue from Steak n Shake units opened during 2016 and 2015.

Cost of food in the second quarter and first six months of 2016 was $56,567 or 27.6% of net sales and $110,559 or 27.6% of net sales, respectively, compared to the second quarter and first six months in 2015 of $59,743 or 29.0% of net sales and $116,854 or 29.3% of net sales, respectively. The decrease as a percent of net sales during 2016 was primarily attributable to lower beef costs.

Restaurant operating costs during the second quarter of 2016 were $99,714 or 48.6% of net sales compared to $94,885 or 46.0% of net sales in 2015. Restaurant operating costs during the first six months of 2016 were $196,946 or 49.2% of net sales compared to $188,212 or 47.2% of net sales in 2015. Costs as a percent of net sales during the second quarter and the first six months of 2016 increased principally due to higher wages and benefits.

Selling, general and administrative expenses during the second quarter and first six months of 2016 were $29,066 or 13.8% of total revenues and $56,680 or 13.8% of total revenues, respectively. The expenses in the second quarter and first six months of 2015 were $29,703 or 14.0% of total revenues and $56,401 or 13.8% of total revenues, respectively. General and administrative expenses decreased by $1,380 and $3,808 during the second quarter and first six months of 2016, respectively, compared to the same periods in 2015 primarily due to decreased personnel expenses. Marketing remained relatively flat during the second quarter of 2016 as compared to the same period during 2015. Marketing increased by $2,590 in the first six months of 2016 compared to the same period of 2015 primarily due to an increase in promotional advertising during the first quarter of 2016.

Insurance

First Guard is a direct underwriter of commercial trucking insurance, selling physical damage and nontrucking liability insurance to truckers. Earnings of our insurance business are summarized below.

| | Second Quarter | | First Six Months | |
|---|---|---|---|---|
| | 2016 | 2015 | 2016 | 2015 |
| Premiums written | $5,581 | $3,641 | $10,942 | $7,139 |
| | | | | |
| Insurance losses | 2,223 | 1,836 | 4,926 | 4,004 |
| Underwriting expenses | 1,396 | 724 | 2,851 | 1,519 |
| Pre-tax underwriting gain | 1,962 | 1,081 | 3,165 | 1,616 |
| | | | | |
| Other income | | | | |
| Commissions | 96 | 84 | 191 | 167 |

| | | | | |
|---|---|---|---|---|
| Investment income | 54 | 47 | 97 | 120 |
| Other income (expense) | (14) | (73) | (28) | (104) |
| Total other income | 136 | 58 | 260 | 183 |
| Earnings before income taxes | 2,098 | 1,139 | 3,425 | 1,799 |
| Income tax expense | 726 | 397 | 1,177 | 621 |
| Contribution to net earnings | $1,372 | $742 | $2,248 | $1,178 |

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

First Guard's insurance products are marketed primarily through direct response methods via the Internet or by telephone. First Guard's cost-efficient direct response marketing methods enable it to be a low-cost trucking insurer.

Underwriting results in the second quarter and first six months of 2016 of First Guard increased significantly from 2015. Pre-tax underwriting gain was $1,962 and $3,165 in the second quarter and first six months of 2016, respectively, compared to $1,081 and $1,616, respectively, for the same periods in 2015. The increase in pre-tax underwriting gain was mainly based on higher premiums written.

Media

Maxim's business lies principally in media and licensing. Earnings of our media operations are summarized below.

| | Second Quarter | | First Six Months | |
|---|---|---|---|---|
| | 2016 | 2015 | 2016 | 2015 |
| Revenue | $2,673 | $6,608 | $5,121 | $12,046 |
| | | | | |
| Media cost of sales | 5,048 | 9,183 | 10,067 | 18,601 |
| General and administrative expenses | 898 | 1,505 | 1,786 | 3,339 |
| Depreciation and amortization | 48 | 93 | 104 | 165 |
| Loss before income taxes | (3,321) | (4,173) | (6,836) | (10,059) |
| Income tax benefit | (1,222) | (1,481) | (2,500) | (3,467) |
| Contribution to net earnings | $(2,099) | $(2,692) | $(4,336) | $(6,592) |

We acquired Maxim with the idea of transforming the brand. We continue to make investments into the brand, many of which are reflected in the reported expenses. We have been rebuilding Maxim's media business, both in print and in digital, as well as developing a licensing business. We have been making adjustments in operations to reduce dramatically the high fixed costs inherent in the media business. The magazine developed the Maxim brand, a franchise we are utilizing to build cash-generating businesses, namely licensing royalties related to consumer products, services, and events.

We have taken the risk on the belief that the probability for gain in value more than justifies the risk of loss.

Investment Partnership Gains (Losses)

Earnings from our investments in partnerships are summarized below.

| | Second Quarter | | First Six Months | |
|---|---|---|---|---|
| | 2016 | 2015 | 2016 | 2015 |
| Investment partnership gains (losses) | $51,549 | $(5,557) | $130,522 | $17,408 |
| Loss on contribution of securities to investment partnership | (306) | - | (306) | - |
| Investment partnership gains (losses) | 51,243 | (5,557) | 130,216 | 17,408 |
| Tax expense (benefit) | 18,171 | (3,002) | 46,756 | 4,851 |
| Contribution to net earnings | $33,072 | $(2,555) | $83,460 | $12,557 |

The Company recorded after-tax gains from investment partnerships of $33,072 during the second quarter of 2016 and after-tax losses of $2,555 during the second quarter of 2015. During the first six months of 2016 the Company recorded after-tax earnings from investment partnerships of $83,460 compared to $12,557 for the first six months of

2015. The volatility of the gains and losses during the various periods is attributable to changes in market values of investments held by the investment partnerships.

Certain of the investment partnerships hold the Company's common stock as investments. The Company's pro-rata share of its common stock held by the investment partnerships is recorded as treasury stock even though these shares are legally outstanding. Gains and losses on Company common stock included in the earnings of these partnerships are eliminated.

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

Interest Expense

The Company's interest expense is summarized below.

| | Second Quarter | | First Six Months | |
|---|---|---|---|---|
| | 2016 | 2015 | 2016 | 2015 |
| Interest expense on notes payable and other borrowings | $2,873 | $2,997 | $5,795 | $6,003 |
| Tax benefit | 1,092 | 1,139 | 2,202 | 2,281 |
| Interest expense net of tax | $1,781 | $1,858 | $3,593 | $3,722 |

Interest expense during the second quarter and first six months of 2016 was $2,873 and $5,795, respectively. The expense in 2016 remained relatively flat compared to the second quarter and first six months of 2015 which were $2,997 and $6,003, respectively. The outstanding balance under Steak n Shake's credit facility on June 30, 2016 was $204,198 with a 4.75% interest rate.

Corporate

Corporate expenses exclude the activities in the restaurant, insurance, media and other companies. Corporate expenses, net of tax, during the second quarter and first six months of 2016 were $1,780 and $3,369, respectively, compared to $2,954 and $6,383 for the second quarter and first six months of 2015, respectively. The decrease in expenses during 2016 was primarily attributable to lower legal expenses.

Income Tax Expense

Income tax expense for the second quarter of 2016 was $19,562 compared to a tax benefit of $2,203 for the second quarter of 2015. Income tax expense for the first six months of 2016 was $49,140 compared to $4,987 for the first six months of 2015. The variance in income tax expense between 2016 and 2015 is primarily attributable to tax expense on income from investment partnerships. The tax expense for investment partnership gains was $18,171 during the second quarter of 2016 compared to a tax benefit for investment partnership losses of $3,002 during the second quarter of 2015, and the tax expense for investment partnership gains was $46,756 during the first six months of 2016 compared to $4,851 during the first six months of 2015.

Financial Condition

Our balance sheet continues to maintain significant liquidity. Our consolidated shareholders' equity on June 30, 2016 was $524,514 compared to $451,372 on December 31, 2015. Shareholders' equity increased during the quarter ended June 30, 2016 primarily because of net earnings of $88,680. The increase from net earnings was offset by an increase in treasury stock of $16,221 attributable primarily to purchases of Biglari Holdings common stock by The Lion Fund II, L.P.

Consolidated cash and investments are summarized below.

| | June 30, 2016 | December 31, 2015 |
|---|---|---|
| Cash and cash equivalents | $66,360 | $56,523 |
| Investments | 21,261 | 23,750 |

| | | |
|---|---|---|
| Investments in other assets | 4,464 | - |
| Fair value of interest in investment partnerships | 930,419 | 734,668 |
| Total cash and investments | 1,022,504 | 814,941 |
| Less portion of Company stock held by investment partnerships | (338,535 ) | (262,979 ) |
| Carrying value of cash and investments on balance sheet | $683,969 | $551,962 |

Liquidity

Cash provided by operating activities during the first six months of 2016 was $41,075 compared to cash provided by operating activities of $23,359 during 2015. The increase was primarily a result of $9,475 of distributions from the investment partnerships during 2016.

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

Net cash used in investing activities during the first six months of 2016 of $20,013 primarily consisted of investments in investment partnerships of $14,150 and capital expenditures of $4,341. Net cash used in investing activities during the first six months of 2015 of $80,293 was primarily because of investments in investment partnerships of $63,000, purchases of bonds (net of maturities) of $11,328 and capital expenditures of $6,102.

Net cash used in financing activities was $11,253 during the first six months of 2016 as compared to $4,725 during 2015. The increase in cash used in financing activities is primarily due to an additional $7,078 payment of long-term debt made during the first six months of 2016.

We intend to meet the working capital needs of our operating subsidiaries principally through anticipated cash flows generated from operations, cash on hand, existing credit facilities, and the sale of excess properties and investments. We continually review available financing alternatives.

Steak n Shake Credit Facility

On March 19, 2014, Steak n Shake and its subsidiaries entered into a new credit agreement. This credit agreement provides for a senior secured term loan facility in an aggregate principal amount of $220,000 and a senior secured revolving credit facility in an aggregate principal amount of up to $30,000.

The term loan is scheduled to mature on March 19, 2021. It amortizes at an annual rate of 1.0% in equal quarterly installments, beginning June 30, 2014, at 0.25% of the original principal amount of the term loan, subject to mandatory prepayments from excess cash flow, asset sales and other events described in the credit agreement. The balance will be due at maturity. The revolver will be available on a revolving basis until March 19, 2019.

Steak n Shake has the right to request an incremental term loan facility from participating lenders and/or eligible assignees at any time, up to an aggregate total principal amount not to exceed $70,000 if certain customary conditions within the credit agreement are met.

Borrowings bear interest at a rate per annum equal to a base rate or a Eurodollar rate (minimum of 1%) plus an applicable margin. Interest on the term loan is based on a Eurodollar rate plus an applicable margin of 3.75% or on the prime rate plus an applicable margin of 2.75%. Interest on loans under the revolver is based on a Eurodollar rate plus an applicable margin ranging from 2.75% to 4.25% or on the prime rate plus an applicable margin ranging from 1.75% to 3.25%. The applicable margins on revolver loans are contingent on Steak n Shake's total leverage ratio. The revolver also carries a commitment fee ranging from 0.40% to 0.50% per annum, according to Steak n Shake's total leverage ratio, on the unused portion of the revolver.

As of June 30, 2016, the interest rate on the term loan was 4.75%.

The credit agreement includes customary affirmative and negative covenants and events of default, as well as a financial maintenance covenant, solely with respect to the revolver, relating to the maximum total leverage ratio. As of June 30, 2016, we were in compliance with all covenants. Steak n Shake's credit facility contains restrictions on its ability to pay dividends to Biglari Holdings.

Both the term loan and the revolver have been secured by first priority security interests on substantially all the assets of Steak n Shake. Biglari Holdings is not a guarantor under the credit facility. At June 30, 2016, $204,198 was outstanding under the term loan, and no amount is outstanding under the revolver.

Steak n Shake had $10,188 in standby letters of credit outstanding as of June 30, 2016 and December 31, 2015.

Western Revolver
As of June 30, 2016, Western has $530 due December 13, 2016.

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

Critical Accounting Policies
Management's discussion and analysis of financial condition and results of operations is based upon our consolidated financial statements, which have been prepared in accordance with accounting principles generally accepted in the United States. Certain accounting policies require management to make estimates and judgments concerning transactions that will be settled several years in the future. Amounts recognized in our consolidated financial statements from such estimates are necessarily based on numerous assumptions involving varying and potentially significant degrees of judgment and uncertainty. Accordingly, the amounts currently reflected in our consolidated financial statements will likely increase or decrease in the future as additional information becomes available. There have been no material changes to critical accounting policies previously disclosed in our annual report on Form 10-K for the year ended December 31, 2015.

Effects of Governmental Regulations and Inflation
Most Restaurant operations employees are paid hourly rates related to minimum wage laws. Any increase in the legal minimum wage would directly increase our operating costs. We are also subject to various laws related to zoning, land use, health and safety standards, working conditions, and accessibility standards. Any changes in these laws that require improvements to our restaurants would increase our operating costs.

Inflation in food, labor, fringe benefits, energy costs, transportation costs and other operating costs directly affect our operations.

The federal healthcare reform legislation that became law in March 2010 (known as the Patient Protection and Affordable Care Act ["PPACA"]) mandates menu labeling of certain nutritional aspects of restaurant menu items such as caloric, sugar, sodium, and fat content. Altering our recipes in response to such legislation could increase our costs and/or change the flavor profile of our menu offerings, which could have an adverse impact on our results of operations. Additionally, if our customers perceive our menu items to contain unhealthy caloric, sugar, sodium, or fat content, our results of operations could be further adversely affected.

Additionally, minimum employee health care coverage mandated by state or federal legislation, such as the PPACA, could significantly increase our employee health benefit costs or require us to alter the benefits we provide to our employees. While we are assessing the potential impact the PPACA will have on our business, certain of the mandates in the legislation are not yet effective. If our employee health benefit costs increase, we cannot provide assurance that we will be able to offset these costs through increased revenue or reductions in other costs, which could have an adverse effect on our results of operations and financial condition.

Recently Issued Accounting Pronouncements
For detailed information regarding recently issued accounting pronouncements and the expected impact on our consolidated financial statements, see Note 2, "New Accounting Standards" in the accompanying notes to consolidated financial statements included in Part I, Item 1 of this quarterly report on Form 10-Q.

Cautionary Note Regarding Forward-Looking Statements
This report includes forward-looking statements within the meaning of the Private Securities Litigation Reform Act of 1995. In general, forward-looking statements include estimates of future revenues, cash flows, capital expenditures, or other financial items, and assumptions underlying any of the foregoing. Forward-looking statements reflect management's current expectations regarding future events and use words such as "anticipate," "believe," "expect," "may," an other similar terminology. A forward-looking statement is neither a prediction nor a guarantee of future events or circumstances, and those future events or circumstances may not occur. Investors should not place undue reliance on the forward-looking statements, which speak only as of the date of this report. These forward-looking statements are

all based on currently available operating, financial, and competitive information and are subject to various risks and uncertainties. Our actual future results and trends may differ materially depending on a variety of factors, many beyond our control, including, but not limited to, the risks and uncertainties described in Item 1A, Risk Factors of our annual report on Form 10-K. We undertake no obligation to publicly update or revise them, except as may be required by law.

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ITEM 3. Quantitative and Qualitative Disclosures About Market Risk

The majority of our investments are conducted through investment partnerships which generally hold common stocks. We also hold marketable securities directly. Through investments in the investment partnerships we hold a concentrated position in the common stock of Cracker Barrel Old Country Store, Inc. A significant decline in the general stock market or in the prices of major investments may produce a large net loss and decrease in our consolidated shareholders' equity. Decreases in values of equity investments can have a materially adverse effect on our earnings and on consolidated shareholders' equity.

We prefer to hold equity investments for very long periods of time so we are not troubled by short-term price volatility with respect to our investments. Our interests in the investment partnerships are committed on a rolling 5-year basis, and any distributions upon our withdrawal of funds will be paid out over two years (and may be paid in kind rather than in cash). Market prices for equity securities are subject to fluctuation. Consequently the amount realized in the subsequent sale of an investment may significantly differ from the reported market value. A hypothetical 10% increase or decrease in the market price of our investments would result in a respective increase or decrease in the carrying value of our investments of $61,761 along with a corresponding change in shareholders' equity of approximately 7%.

Borrowings on Steak n Shake's credit facility bear interest at a rate per annum equal to a base rate or a Eurodollar rate (minimum of 1%) plus an applicable margin. Interest on the term loan is based on a Eurodollar rate plus an applicable margin of 3.75% or on the prime rate plus an applicable margin of 2.75%. Interest on loans under the revolver is based on a Eurodollar rate plus an applicable margin ranging from 2.75% to 4.25% or on the prime rate plus an applicable margin ranging from 1.75% to 3.25%. At June 30, 2016, a hypothetical 100 basis point increase in short-term interest rates would not have a significant impact on our net earnings.

We have had minimal exposure to foreign currency exchange rate fluctuations in the second quarter of 2016.

ITEM 4. Controls and Procedures

Based on an evaluation of our disclosure controls and procedures (as defined in Exchange Act Rules 13a-15(f) and 15d-15(f)), our Chief Executive Officer and Controller have concluded that our disclosure controls and procedures were effective as of June 30, 2016.

There have been no changes in our internal control over financial reporting that occurred during the quarter ended June 30, 2016 that have materially affected, or that are reasonably likely to materially affect, our internal control over financial reporting.

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## PART II OTHER INFORMATION

### ITEM 1. LEGAL PROCEEDINGS

Information in response to this Item is included in Note 12 to the Consolidated Financial Statements included in Part 1 Item 1 of this Form 10-Q and is incorporated herein by reference.

### ITEM 1A. RISK FACTORS

An investment in the common stock of any company involves a degree of risk. Investors should consider carefully the risks and uncertainties described in the Company’s annual report on Form 10−K filed with the SEC, as well as the risks subsequently disclosed in our reports filed with the SEC, before deciding whether to purchase our common stock. Additional risks and uncertainties not currently known to us or that we currently deem immaterial may also become important factors that may harm the Company’s business, financial condition, and results of operations. The occurrence of risk factors could harm the Company’s business, financial condition, and results of operations. The trading price of the Company’s common stock could decline due to any of these risks and uncertainties, and stockholders may lose part or all of their investment.

The following material changes in the risk factors previously disclosed in the Company’s Form 10-K for 2015.

We are a "controlled company" within the meaning of the NYSE rules and may rely on exemptions from certain corporate governance requirements.
Because Mr. Biglari beneficially owns more than 50% of the Company’s outstanding voting stock, we are considered a “controlled company” pursuant to New York Stock Exchange rules. As a result, we are not required to comply with certain director independence and board committee requirements.

### ITEM 2. UNREGISTERED SALES OF EQUITY SECURITIES AND USE OF PROCEEDS

The following table presents information on purchases of our common stock during the second quarter of 2016 by The Lion Fund II, L.P. and Sardar Biglari, each of whom may be deemed to be an “affiliated purchaser” as defined in Rule 10b-18(a)(3) under the Securities Exchange Act of 1934, as amended.  On May 10, 2016, The Lion Fund II, L.P. entered into a Rule 10b5-1 Trading Plan (the “Purchase Plan”) pursuant to Rule 10b5-1 under the Securities Exchange Act of 1934, as amended. Under the Purchase Plan, a broker dealer will make periodic purchases of up to an aggregate of 68,000 shares of the Company’s common stock on behalf of The Lion Fund II, L.P. at prevailing market prices, subject to the terms of the Purchase Plan.

| | (a) Total Number of Shares Purchased | (b) Average Price Paid per Share | (c) Total Number of Shares Purchased as Part of Publicly Announced Plans or Programs | (d) Maximum Number of Shares That May Yet Be Purchased Under Plans or Programs |
|---|---|---|---|---|

| | | | | |
|---|---|---|---|---|
| April 1, 2016 – April 30, 2016 | - | $- | - | - |
| May 1, 2016 – May 31, 2016 | 4,845 | $385.39 | 4,845 | 63,155 |
| June 1, 2016 – June 30, 2016 | 8,250 | $409.88 | 8,250 | 54,905 |
| Total | 13,095 | | 13,095 | |

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ITEM 3. DEFAULTS UPON SENIOR SECURITIES

None.

ITEM 4. MINE SAFETY DISCLOSURES

Not applicable.

ITEM 5. OTHER INFORMATION

None.

ITEM 6. EXHIBITS

| Exhibit Number | Description |
|---|---|
| 31.01 | Certification Pursuant to Rules 13a-14(a) and 15d-14(a) under the Securities Exchange Act of 1934, as Adopted Pursuant to Section 302 of the Sarbanes-Oxley Act of 2002. |
| 31.02 | Certification Pursuant to Rules 13a-14(a) and 15d-14(a) under the Securities Exchange Act of 1934, as Adopted Pursuant to Section 302 of the Sarbanes-Oxley Act of 2002. |
| 32.01* | Certification Pursuant to 18 U.S.C. Section 1350, as Adopted Pursuant to Section 906 of the Sarbanes-Oxley Act of 2002. |
| 101 | Interactive Data Files. |

* Furnished herewith.

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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.

Date: August 5, 2016

Biglari Holdings inc.

| | |
|---|---|
| By: | /s/ Bruce Lewis |
| | Bruce Lewis |
| | Controller |