CARROLS RESTAURANT GROUP, INC.
Form 10-K
March 03, 2014

UNITED STATES
SECURITIES AND EXCHANGE COMMISSION
WASHINGTON, DC 20549
FORM 10-K

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

For the fiscal year ended December 29, 2013
OR

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

Commission File Number: 001-33174
CARROLS RESTAURANT GROUP, INC.
(Exact name of Registrant as specified in its charter)

Delaware	16-1287774
(State or other jurisdiction of incorporation or organization)	(I.R.S. Employer Identification No.)
968 James Street, Syracuse, New York	13203
(Address of principal executive office)	(Zip Code)

Registrant's telephone number, including area code: (315) 424-0513
Securities registered pursuant to Section 12(b) of the Act:

Title of each class:	Name on each exchange on which registered:
Common Stock, par value $.01 per share	The NASDAQ Global Market

Securities registered pursuant to Section 12(g) of the Act: None
Indicate by check mark if the registrant is a well-known seasoned issuer, as defined in Rule 405 of the Securities Act. Yes ¨ No x
Indicate by check mark if the registrant is not required to file reports pursuant to Section 13 or 15(d) of the Exchange Act. Yes ¨ No x
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 ý No ¨
Indicate by check mark whether the registrant has submitted electronically and posted on its corporate Web site, if any, every Interactive Data File required to be submitted and posted pursuant to Rule 405 of Regulation S-T during the preceding 12 months (or for such shorter period that the registrant was required to submit and post such files). Yes ý No ¨
Indicate by check mark if disclosure of delinquent filers pursuant to Item 405 of Regulation S-K is not contained herein, and will not be contained, to the best of the registrant's knowledge, in definitive proxy or information statements incorporated by reference in Part III of this Form 10-K or any amendment to this Form 10-K. ý
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. (Check one):

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

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

As of February 27, 2014 Carrols Restaurant Group, Inc. had 23,711,096 shares of its common stock, $.01 par value, outstanding. The aggregate market value of the common stock held by non-affiliates as of June 30, 2013 of Carrols Restaurant Group, Inc. was $142,651,309.

DOCUMENTS INCORPORATED BY REFERENCE

Portions of the registrant's definitive Proxy Statement for Carrols Restaurant Group, Inc's 2014 Annual Meeting of Stockholders, which is expected to be filed pursuant to Regulation 14A no later than 120 days after the conclusion of Carrols Restaurant Group, Inc.'s fiscal year ended December 29, 2013 are incorporated by reference into Part III of this annual report.

CARROLS RESTAURANT GROUP, INC.
FORM 10-K
YEAR ENDED DECEMBER 29, 2013

PART I—FINANCIAL INFORMATION
PART I
Throughout this Annual Report on Form 10-K, we refer to Carrols Restaurant Group, Inc. as “Carrols Restaurant Group” and, together with its consolidated subsidiaries, as “we”, “our” and “us” unless otherwise indicated or the context otherwise requires. Any reference to “Carrols” refers to our wholly-owned subsidiary, Carrols Corporation, a Delaware corporation, and its consolidated subsidiaries, unless otherwise indicated or the context otherwise requires. Any reference to “Carrols LLC” refers to Carrols' direct subsidiary, Carrols LLC, a Delaware limited liability company, unless otherwise indicated or the context otherwise requires. Any reference to “Fiesta Restaurant Group” or “Fiesta” refers to our former indirect wholly-owned subsidiary, Fiesta Restaurant Group, Inc., a Delaware corporation, and its consolidated subsidiaries unless otherwise indicated or the context otherwise requires.
We use a 52 or 53 week fiscal year ending on the Sunday closest to December 31. Our fiscal years ended January 2, 2011, January 1, 2012, December 30, 2012 and December 29, 2013 each contained 52 weeks. Our fiscal year ended January 3, 2010 contained 53 weeks.
In this Annual Report on Form 10-K, we refer to information, forecasts and statistics regarding the restaurant industry and to information, forecasts and statistics from Nation's Restaurant News, the U.S. Census Bureau and the U.S. Department of Agriculture. Any reference to BKC in this Annual Report on Form 10-K refers to Burger King Worldwide, Inc. and its wholly-owned subsidiaries, including Burger King Corporation. Unless otherwise indicated, information regarding BKC in this Annual Report on Form 10-K has been made publicly available by BKC.
Forward-Looking Statements
This 2013 Annual Report on Form 10-K contains statements which constitute forward-looking statements within the meaning of Section 27A of the Securities Act of 1933, as amended (the “Securities Act”), and Section 21E of the Securities Exchange Act of 1934, as amended (the “Exchange Act”). Statements that are predictive in nature or that depend upon or refer to future events or conditions are forward-looking statements. These statements are often identified by the words “may”, “might”, “will”, “should”, “anticipate”, “believe”, “expect”, “intend”, “estimate”, “hope”, “plan
expressions. In addition, expressions of our strategies, intentions or plans are also forward-looking statements. These statements reflect management's current views with respect to future events and are subject to risks and uncertainties, both known and unknown. You are cautioned not to place undue reliance on these forward-looking statements, which speak only as of their date. There are important factors that could cause actual results to differ materially from those in forward-looking statements, many of which are beyond our control. Investors are cautioned that any such forward-looking statements are not guarantees of future performance and involve risks and uncertainties, and that actual results may differ materially from those projected or implied in the forward-looking statements. We have identified significant factors that could cause actual results to differ materially from those stated or implied in the forward-looking statements. For more information, please see Item 1A-Risk Factors. We believe important factors that could cause actual results to differ materially from our expectations include the following, in addition to other risks and uncertainties discussed herein:
- The effect of our tax-free spin-off of Fiesta, including any potential tax liability that may arise;
- Effectiveness of the Burger King® advertising programs and the overall success of the Burger King brand;
- Increases in food costs and other commodity costs;
- Competitive conditions;
- Our ability to integrate any restaurants we acquire;
- Regulatory factors;
- Environmental conditions and regulations;
- General economic conditions, particularly in the retail sector;
- Weather conditions;
- Fuel prices;
- Significant disruptions in service or supply by any of our suppliers or distributors;
- Changes in consumer perception of dietary health and food safety;
- Labor and employment benefit costs, including the effects of healthcare reform;
- The outcome of pending or future legal claims or proceedings;

• Our ability to manage our growth and successfully implement our business strategy;

- Our inability to service our indebtedness;
- Our borrowing costs and credit ratings, which may be influenced by the credit ratings of our competitors;
- The availability and terms of necessary or desirable financing or refinancing and other related risks and uncertainties;
- Factors that affect the restaurant industry generally, including recalls if products become adulterated or misbranded, liability if our products cause injury, ingredient disclosure and labeling laws and regulations, reports of cases of food borne illnesses such as “mad cow” disease and avian flu, and the possibility that consumers could lose confidence in the safety and quality of certain food products, as well as negative publicity regarding food quality, illness, injury or other health concerns; and
- Other factors discussed under Item 1A - "Risk Factors" and elsewhere herein.

ITEM 1. BUSINESS

Overview

Our Company

We are the largest Burger King® franchisee in the world, based on number of restaurants, and have operated Burger King restaurants since 1976. As of December 29, 2013, we owned and operated 564 Burger King restaurants located in 13 Northeastern, Midwestern and Southeastern states. Burger King restaurants feature the popular flame-broiled Whopper® sandwich, as well as a variety of hamburgers, chicken and other specialty sandwiches, french fries, salads, breakfast items, snacks, smoothies, frappes and other offerings. We believe that our size, seasoned management team, extensive operating infrastructure, experience and proven operating disciplines differentiate us from many of our competitors as well as many other Burger King operators.

According to BKC, as of December 31, 2013 there were a total of 13,667 Burger King restaurants, of which 13,615 were franchised and 7,436 were located in the United States and Canada. Burger King is the second largest hamburger restaurant chain in the world (as measured by number of restaurants) and we believe that the Burger King brand is one of the world's most recognized consumer brands. Burger King restaurants have a distinctive image and are generally located in high-traffic areas throughout the United States. Burger King restaurants are designed to appeal to a broad spectrum of consumers, with multiple day-part meal segments targeted to different groups of consumers. We believe that the competitive attributes of Burger King restaurants include significant brand recognition, convenience of location, quality, speed of service and price.

Our Burger King restaurants are typically open seven days per week and generally have operating hours ranging from 6:00 am to midnight on Sunday to Wednesday and to 2:00 am on Thursday to Saturday.

Our existing restaurants consist of one of several building types with various seating capacities. Our typical freestanding restaurant contains approximately 2,800 to 3,200 square feet with seating capacity for 90 to 100 customers, has drive-thru service windows and has adjacent parking areas. The building types for recently constructed or remodeled Burger King restaurants utilize 2,600 square feet and typically have seating capacity for 60 to 70 customers. As of December 29, 2013, almost all of our restaurants were freestanding. We operate our restaurants under franchise agreements with BKC.

On May 7, 2012, we completed the spin-off of Fiesta Restaurant Group, which included the Pollo Tropical and Taco Cabana restaurant businesses which we refer to as the "spin-off".

On May 30, 2012, we completed the acquisition of 278 Burger King restaurants from BKC, which we refer to as the "2012 acquisition" including BKC's assignment of its right of first refusal on franchise restaurant transfers in 20 states as follows: Connecticut (except Hartford county), Delaware, Indiana, Kentucky, Maine, Maryland, Massachusetts (except for Middlesex, Norfolk and Suffolk counties), Michigan, New Hampshire, New Jersey, New York (except for Bronx, Kings, Nassau, New York, Queens, Richmond, Suffolk and Westchester counties), North Carolina, Ohio, Pennsylvania, Rhode Island, South Carolina, Vermont, Virginia, Washington DC and West Virginia, (the "ROFR") pursuant to an operating agreement with BKC, which we refer to as the "operating agreement", dated as of May 30, 2012. In addition, pursuant to the operating agreement, BKC granted us, on a non-exclusive basis, franchise pre-approval to acquire restaurants from Burger King franchisees in the 20 states covered by the ROFR until we operate 1,000 Burger King restaurants. Newly constructed or acquired restaurants beyond 1,000, or acquisitions in states not subject to the ROFR would be subject to BKC's customary approval process. We also agreed to remodel 455

Burger King restaurants to BKC's "20/20" restaurant image.
We refer to the restaurants acquired from BKC in the 2012 transaction as our "acquired BKC restaurants" and all of our other restaurants are referred to as our "legacy restaurants". For the fiscal year ended December 29, 2013, our restaurants generated revenues of $663.5 million in total and our comparable restaurant sales increased 1.0%. Our average annual restaurant sales for all restaurants were approximately $1,177,000 per restaurant.

Our Competitive Strengths

We believe we have the following competitive strengths:

Largest Burger King Franchisee. We are BKC's largest franchisee in the world based on number of restaurants, and are well positioned to leverage the scale and marketing of one of the most recognized brands in the restaurant industry. We believe the geographic dispersion of our restaurants provides us with stability and enhanced growth opportunities in many of the markets in which we operate. We also believe that our large number of restaurants increases our ability to effectively manage the awareness of the Burger King brand in certain markets through our ability to influence local advertising and promotional activities.

Operational Expertise. We have been operating Burger King restaurants since 1976 and have developed sophisticated information and operating systems that enable us to measure and monitor key metrics for operational performance, sales and profitability that may not be available to other restaurant operators. Our focus on leveraging our operational expertise, infrastructure and systems allows us to optimize the performance of our restaurants and any restaurants that we may acquire. Our size and history with the Burger King brand enable us to effectively track operating metrics and leverage best practices across our organization. We believe that our experienced management team, operating culture, effective operating systems and infrastructure enable us to operate more efficiently than many other Burger King operators, resulting in higher restaurant margins and overall performance.

Consistent Operating History and Financial Strength. We believe that the quality and sophistication of our restaurant operations have driven our strong restaurant level performance. Our restaurants have generally outperformed the Burger King system from a comparable sales perspective over time. Our strong restaurant level operations coupled with our financial management capabilities have resulted in consistent and stable cash flows. We have demonstrated our ability to prudently manage financial leverage through a variety of economic cycles. We believe that our cash flow from operations and availability of revolving credit borrowings under our senior credit facility will be used to fund our ongoing operations and strategic capital expenditure needs.

Distinct Brand with Global Recognition, Innovative Marketing and New Product Development. As a Burger King franchisee, we benefit from, and rely on, BKC's extensive marketing, advertising and product development capabilities to drive sales and generate increased restaurant traffic. Over the years, BKC has launched innovative and creative multimedia advertising campaigns that highlight the popular relevance of the Burger King brand. In 2012, BKC launched an extensive campaign of new product introductions and innovative marketing that drove system-wide sales growth. We believe these campaigns continue to positively impact the brand today as BKC focuses on a well-balanced promotional mix and remains committed to focusing on fewer but more impactful new product launches and limited time offers, both of which continue to show positive trends. BKC is also aggressively working with franchisees throughout the system to encourage the renovation and remodeling of restaurants to BKC's 20/20 image, which we believe will increase customer traffic and restaurant sales.

Strategic Relationship with Burger King Corporation. We believe that the structure of the 2012 acquisition strengthens our well-established relationship with BKC and further aligns our common interests to grow our business. We intend to expand by making acquisitions, including acquisitions resulting from the exercise of the ROFR obtained in the 2012 acquisition. The consideration to BKC included a 28.9% equity interest in Carrols Restaurant Group. BKC's Chief Executive Officer, Daniel Schwartz, joined our board of directors upon the closing of the 2012 acquisition on May 30, 2012 and Alexandre Macedo, BKC's President of North America, also currently serves on our board of directors. Our restaurants represent approximately 7.6% of the Burger King locations in North America as of December 29, 2013. We believe that the combination of our rights under the operating agreement, BKC's shared equity interest and its board level representation have reinforced the alignment of our common interests with BKC for the long term.

Multiple Growth Levers. We believe our historical track record of acquiring and integrating restaurants and our commitment to remodel our restaurants provides multiple avenues to grow our business. With more than 50 years of restaurant operating experience, we have successfully grown our business through acquisitions, including the most recent acquisition in May 2012 of 278 restaurants from BKC. Since this acquisition, we have experienced increases in comparable restaurant sales, increased restaurant-level profitability and improved operating metrics at these acquired restaurants. In addition, we have remodeled a total of 201 restaurants over the past two years to BKC's 20/20 restaurant image which we believe has improved the guests' overall experience and increased customer traffic.

Experienced Management Team with a Proven Track Record. We believe that our senior management team's extensive experience in the restaurant industry and its long and successful history of developing, acquiring, integrating and operating quick-service restaurants provide us with a competitive advantage. Our management team has a successful history of integrating acquired restaurants, and over the past 20 years, we have significantly increased the number of Burger King restaurants we own and operate, largely through acquisitions. In addition, we successfully acquired, integrated and expanded the Pollo Tropical and Taco Cabana brands during 1998 to 2012 prior to our spin-off of Fiesta. Our operations are overseen by our Chief Executive Officer, Dan Accordino, who has over 40 years of Burger King and quick-service restaurant experience and eight Regional Directors that have an average of 27 years of Burger King restaurant experience. Seventy-three district managers support the Regional Directors of which 51 have over 15 years of restaurant management experience in the Burger King system. Our operations management is further supported by our infrastructure of financial, information systems, real estate and human resources professionals.

Our Business Strategies

Our primary business strategies are as follows:

Increase Restaurant Sales and Customer Traffic. BKC has identified and implemented a number of strategies to increase brand awareness, increase market share, improve overall operations and drive future growth. These strategies are central to our strategic objectives to deliver profitable growth.

- Products. The strength of the BKC menu has been built on a distinct flame-grilled cooking platform to make better tasting hamburgers. We believe that BKC intends to continue to optimize the menu by focusing on core products, such as the flagship Whopper® sandwich, while maintaining a balance between value promotions and premium limited time offerings to drive sales and traffic. In April 2012, BKC launched one of the broadest expansions of food offerings in its 58-year history, including the introduction of Garden Fresh Salads, Wraps, Real Fruit Smoothies and Frappes. Product innovation continued in 2013 with a multi-tier balanced approach to value and premium offerings, pairing value promotions, such as the $1 Fry Burger, with premium limited time offerings such as the Angry Whopper® sandwich. In the third quarter of 2013, BKC introduced Satisfries™, a first of its kind reduced calorie french fry. There have also been a number of enhancements to food preparation procedures to improve the quality of BKC's existing products. These new menu platforms and quality improvements form the backbone of BKC's strategy to appeal to a broader consumer base and to increase restaurant sales.
- Image. We believe that reimaged restaurants increase curb appeal and result in increased restaurant sales. We agreed to remodel 455 restaurants beginning in 2012 to BKC's 20/20 restaurant image which features a fresh, sleek, eye-catching design. The restaurant redesign incorporates easy-to-navigate digital menu boards in the dining room, streamlined merchandising at the drive-thru, flat screen televisions in the dining area and new employee uniforms. We believe the restaurant remodeling plan will improve our guests' dining experience and increase customer traffic. As of December 29, 2013, we have completed remodeling a total of 201 restaurants to the 20/20 restaurant image.
- Advertising and Promotion. We believe that we will continue to benefit from BKC's advertising support of its new menu additions, product enhancement and reimaging initiatives. BKC has established a data driven marketing process which is focused on driving restaurant sales and traffic, while targeting a broader consumer base with more inclusive messaging. This strategy uses multiple touch points to advertise our products, including digital advertising, social media and on-line video in addition to traditional television advertising. In 2012, BKC launched a food-centric marketing strategy with the tagline Taste is King® which focuses consumers on the food offerings, the core asset, and balances value promotions and premium limited time offerings to drive profitable restaurant sales and traffic. In 2013, BKC initiated a 2 for $5 premium sandwich promotion which features different premium sandwiches from time to time and also serves as a platform for the promotion of new premium sandwiches as they are introduced.
- Operations. We believe that improving restaurant operations and enhancing the customer experience are key components to increasing the profitability of our restaurants. We believe we will benefit from BKC's initiatives to improve food quality, simplify restaurant level execution and monitor operational performance, all of which are designed to improve the customer experience and increase customer traffic.

Strategically Remodel to Elevate Brand Profile and Increase Profit Potential. As of December 29, 2013 we have completed remodeling a total of 201 restaurants to BKC's 20/20 restaurant image which we believe will improve the customer experience, increase traffic and potentially lead to a higher average check size. Over the next two to three years, we plan to strategically remodel an additional 250 or more locations to conform to BKC's 20/20 image. Based on our recent experience, our restaurants remodeled to BKC's 20/20 image have generated an average sales lift of approximately 10% and have resulted in an attractive return on investment. We believe there are opportunities to increase profitability by remodeling additional restaurants including restaurants that we may acquire in the future.

Selectively Acquire and Develop Additional Burger King Restaurants. As of December 29, 2013, we operated 564 Burger King restaurants, making us the largest Burger King franchisee in the world. In addition, as a part of the 2012 acquisition, we received the ROFR and certain pre-approval rights to acquire additional franchised restaurants and to develop new restaurants. Due to the number of restaurants and franchisees in the Burger King franchise system and our historical success in acquiring and integrating restaurants, we believe that there is considerable opportunity for future growth. There are more than 2,000 Burger King restaurants we do not own in states in which we have the ROFR and pre-approval rights. Furthermore, we believe there are additional Burger King restaurants in states not subject to the ROFR that could be attractive acquisition candidates, subject to BKC's customary approval. While our primary focus recently has been on successfully integrating, remodeling and improving the profitability of the acquired BKC restaurants, we believe that the assignment of the ROFR and the pre-approval to acquire and develop additional restaurants provide us with the opportunity to significantly expand our ownership of Burger King restaurants in the future. While we may evaluate and discuss potential acquisitions of additional restaurants from time to time, we currently have no understandings, commitments or agreements with respect to any material acquisitions. We may be required to obtain additional financing to fund future acquisitions. There can be no assurance that we will be able to obtain additional financing, if necessary, on acceptable terms or at all.

Improve Profitability of Restaurants We Acquire by Leveraging Our Existing Infrastructure and Best-Practices. For future acquisitions of restaurants, we believe we can realize benefits from economies of scale, including leveraging our existing infrastructure across a larger number of restaurants. Additionally, we believe that our skilled management team, sophisticated information technology, operating systems and training and development programs support our ability to enhance operating efficiencies at any restaurants we may acquire. We have demonstrated our ability to increase the profitability of acquired restaurants and we believe, over time, we will improve profitability and operational efficiency at the restaurants we acquire.

Restaurant Economics

Selected restaurant operating data for our restaurants is as follows:

	Year Ended					
	January 1, 2012		December 30, 2012		December 29, 2013	
Average annual sales per restaurant (1)	$1,153,778		$1,180,761		$1,176,806	
Average sales transaction	$5.80		$6.00		$6.11	
Drive-through sales as a percentage of total sales	64.9	%	64.9	%	65.0	%
Day-part sales percentages:						
Breakfast	13.1	%	14.3	%	14.8	%
Lunch	32.1	%	31.5	%	31.3	%
Dinner	27.1	%	26.6	%	26.6	%
Afternoon and late night	27.7	%	27.6	%	27.3	%

(1) Average annual sales per restaurant are derived by dividing restaurant sales by the average number of restaurants operating during the period.

Restaurant Capital Costs

The initial cost of the franchise fee, equipment, seating, signage and other interior costs of a standard new Burger King restaurant currently is approximately $350,000 (excluding the cost of the land, building and site improvements). In the markets in which we primarily operate, the cost of land generally ranges from $600,000 to $800,000 and the cost of building and site improvements generally ranges from $650,000 to $700,000.

With respect to development of freestanding restaurants, we generally seek to acquire the land to construct the building, and thereafter enter into an arrangement to sell and leaseback the land and building under a long-term lease. Historically, we have been able to acquire and finance many of our locations under such leasing arrangements. Where we are unable to purchase the underlying land, we enter into a long-term lease for the land and fund the construction of the building from cash generated from our operations or with borrowings under our senior credit facility rather than through long-term leasing arrangements.

The cost of developing and equipping new restaurants can vary significantly and depends on a number of factors, including the local economic conditions and the characteristics of a particular site. Accordingly, the cost of opening new restaurants in the future may differ substantially from, and may be significantly higher than, both the historical cost of restaurants previously opened and the estimated costs above.

The cost of remodeling restaurants to BKC's 20/20 restaurant image ranges from $200,000 to $500,000 per restaurant with an average cost of approximately $300,000 per restaurant. BKC's 20/20 restaurant design draws inspiration from its signature flame-grilled cooking process and incorporates a variety of innovative elements to a backdrop that evokes the industrial look of corrugated metal, brick, wood and concrete. Pursuant to the operating agreement, we agreed to remodel 455 Burger King restaurants to BKC's 20/20 restaurant image. We have remodeled a total of 201 restaurants as of December 29, 2013 and we plan to remodel approximately 65 to 75 additional restaurants in 2014.

Site Selection

We believe that the location of our restaurants is a critical component of each restaurant's success. We evaluate potential new sites on many critical criteria including accessibility, visibility, costs, surrounding traffic patterns, competition and demographic characteristics. Our senior management determines the acceptability of all acquisition prospects and new sites, based upon analyses prepared by our real estate, financial and operations professionals.

Seasonality
Our business is moderately seasonal due to regional weather conditions. Due to the location of our restaurants, sales are generally higher during the summer months than during the winter months. The acquired BKC restaurants have somewhat moderated the seasonal impact on our business due to the increased concentration of acquired BKC restaurants in the Southeast.
Restaurant Locations
The following table details the locations of our 564 Burger King restaurants as of December 29, 2013:

State	Total Restaurants
Indiana	71
Kentucky	17
Maine	4
Massachusetts	1
Michigan	22
New Jersey	1
New York	118
North Carolina	138
Ohio	85
Pennsylvania	33
South Carolina	31
Vermont	1
Virginia	42
Total	564

Operations
Management Structure
We conduct substantially all of our executive management, finance, marketing and operations support functions from our corporate headquarters in Syracuse, New York. Carrols Restaurant Group is led by our Chief Executive Officer and President, Daniel T. Accordino, who has over 40 years of Burger King and quick-service restaurant experience at our company.
Our Burger King operations for our restaurants are overseen by eight Regional Directors that have an average of over 27 years of Burger King restaurant experience. Seventy-three district managers support the Regional Directors for our restaurants.
A district manager is responsible for the direct oversight of the day-to-day operations of an average of approximately seven to eight restaurants. Typically, district managers have previously served as restaurant managers at one of our restaurants. Regional directors, district managers and restaurant managers are compensated with a fixed salary plus an incentive bonus based upon the performance of the restaurants under their supervision, and for our regional directors and district managers, the combined performance of all of our restaurants. Typically, our restaurants are staffed with hourly employees who are typically supervised by a salaried manager and two or three salaried assistant managers.
Training
We maintain a comprehensive training and development program for all of our personnel and provide both classroom and in-restaurant training for our salaried and hourly personnel. The program emphasizes system-wide operating procedures, food preparation methods and customer service standards. BKC's training and development programs are also available to us as a franchisee.
Management Information Systems
Our sophisticated management information systems provide us with the ability to efficiently and effectively manage our restaurants and to ensure consistent application of operating controls at our restaurants. Our size affords us the ability to maintain an in-house staff of information technology and restaurant systems professionals dedicated to continuously enhancing our systems. In addition, these capabilities allow us to integrate newly developed restaurants

or restaurants that we acquire and achieve greater economies of scale and operating efficiencies.

We installed new point-of-sale (POS) systems at all of our legacy restaurants in 2011 and in the first half of 2012. Our restaurants employ touch-screen POS systems that are designed to facilitate accuracy and speed of order taking. These systems are user-friendly, require limited cashier training and improve speed-of-service through the use of conversational order-taking techniques. The POS systems are integrated with PC-based applications at the restaurant and hosted systems at our corporate office that are designed to facilitate financial and management control of our restaurant operations. We retained the existing POS systems used at the acquired BKC restaurants following the 2012 acquisition and implemented our labor and inventory management systems in 2012 and completed the rollout of our POS system software to all of the acquired BKC restaurants in 2013.

Our restaurant systems provide daily tracking and reporting of traffic counts, menu item sales, labor and food data including costs, and other key operating information for each restaurant. We communicate electronically with our restaurants on a continuous basis, which enables us to collect this information for use in our corporate management systems in near real-time. Our corporate headquarters manages systems that support all of our accounting, operating and reporting systems. We also operate a 24-hour, seven-day help desk at our corporate headquarters that enables us to provide systems and operational support to our restaurant operations as required. Among other things, our restaurant information systems provide us with the ability to:

- monitor labor utilization and sales trends on a real-time basis at each restaurant, enabling the restaurant manager to effectively manage to our established labor standards on a timely basis;
- reduce inventory shrinkage using restaurant-level inventory management and centralized standard costing systems;
- analyze sales and product mix data to help restaurant managers forecast production levels;
- monitor day-part drive-thru speed of service at each of our restaurants;
- systematically communicate human resource and payroll data to our administrative offices for efficient centralized management of labor costs and payroll processing;
- employ centralized control over price, menu and inventory management activities at the restaurant utilizing the remote management capabilities of our systems;
- take advantage of electronic commerce including our ability to place orders with suppliers and to integrate detailed invoice, receiving and product data with our inventory and accounting systems; and
- provide analyses, reporting and tools to enable all levels of management to review a wide-range of financial, product mix and operational data.

Critical information from our systems is available in near real-time to our restaurant managers, who are expected to react quickly to trends or situations in their restaurant. Our district managers also receive near real-time information from all restaurants under their control and have computer access to key operating data on a remote basis using our corporate intranet. Management personnel at all levels, from the restaurant manager through senior management, utilize key restaurant performance indicators to manage our business.

Burger King Franchise Agreements

Each of our Burger King restaurants operates under a separate franchise agreement with BKC. Our franchise agreements with BKC generally require, among other things, that all restaurants comply with specified design criteria and operate in a prescribed manner, including utilization of the standard Burger King menu. In addition, our Burger King franchise agreements generally require that our restaurants conform to BKC's current image and provide for remodeling of our restaurants during the tenth year of the agreements to conform to such current image, which may require the expenditure of considerable funds. These franchise agreements with BKC generally provide for an initial term of 20 years and currently have an initial franchise fee of $50,000. In the event that we terminate any franchise agreement and close the related BKC restaurant prior to the expiration of its term, we may be required to pay BKC an amount based on the net present value of the royalty stream that would have been realized by BKC had such franchise agreement not been terminated. Any franchise agreement, including renewals, can be extended at our discretion for an additional 20-year term, with BKC's approval, provided that, among other things, the restaurant meets the current Burger King operating and image standards and that we are not in default under the terms of the franchise agreement. The franchise agreement fee for subsequent renewals is currently $50,000. BKC may terminate any of the franchise agreements if an act of default is committed by us under these agreements and such default is not cured. Defaults under the franchise agreements include, among other things, our failure to operate such Burger King restaurant in accordance with the operating standards and specifications established by BKC (including failure to use equipment, uniforms or decor approved by BKC), our failure to sell products approved or designated by BKC, our failure to pay royalties or advertising and sales promotion contributions as required, our unauthorized sale, transfer or assignment of such franchise agreement or the related restaurant, certain events of bankruptcy or insolvency with respect to us, conduct by us or our employees that has a harmful effect on the Burger King restaurant system, conviction of us or our executive officers for certain indictable offenses, our failure to maintain a responsible credit rating or the acquisition by us of an interest in any other hamburger restaurant business. We are not in default under any of the franchise agreements with BKC.

In order to obtain a successor franchise agreement with BKC, a franchisee is typically required to make capital improvements to the restaurant to bring it up to BKC's current image standards. The cost of these improvements may vary widely depending upon the magnitude of the required changes and the degree to which we have made interim improvements to the restaurant. At December 29, 2013, we have 24 franchise agreements due to expire in 2014, 21 franchise agreements due to expire in 2015 and 19 franchise agreements due to expire in 2016. In recent years, the historical costs of improving our Burger King restaurants in connection with franchise renewals generally have ranged from $200,000 to $500,000 per restaurant. The average cost of our remodels to the 20/20 image in the past two years was approximately $300,000. The cost of capital improvements made in connection with future franchise agreement renewals may differ substantially from past franchise renewals depending on the current image requirements established from time to time by BKC.

We believe that we will be able to satisfy BKC's normal franchise agreement renewal criteria. Accordingly, we believe that renewal franchise agreements will be granted on a timely basis by BKC at the expiration of our existing franchise agreements. Historically, BKC has granted all of our requests for successor franchise agreements. However, there can be no assurance that BKC will grant these requests in the future.

We evaluate the performance of our Burger King restaurants on an ongoing basis. Such evaluation depends on many factors, among other things, including our assessment of the anticipated future operating results of the subject restaurants and the cost of required capital improvements that we would need to commit for such restaurants. If we determine that a Burger King restaurant is under-performing, or that we do not anticipate an adequate return on the capital required to renew the franchise agreement, we may elect to close such restaurant. We may also relocate (offset) a restaurant within its trade area and build a new Burger King restaurant as part of the franchise renewal process. In 2013, we closed ten restaurants, excluding one restaurant that was relocated within its trade area. We currently expect to close 15 to 20 restaurants in 2014, excluding any relocation of existing restaurants. However, based on the current operating results of these restaurants, we believe that the impact on our results of operations as a result of such restaurant closures will not be material, although there can be no assurance in this regard. Our determination to close these restaurants is subject to further evaluation and may change. We may also elect to close additional restaurants in the future.

In addition to the initial franchise fee, we generally pay BKC a monthly royalty. The royalty rate for new restaurants, including newly acquired restaurants, and for successor franchise agreements is 4.5% of sales. The royalty rate was increased from 3.5% to 4.5% of sales in 2000, and generally for restaurants in existence in 2000, becomes effective upon the renewal of the franchise agreement. Burger King royalties, as a percentage of our restaurant sales, were 4.2% in 2013 and 2012 and 4.0% in 2011. Royalty payments to BKC under new franchise agreements for the acquired BKC restaurants are at a contractual rate of 4.5%. We anticipate our Burger King royalties, as a percentage of our restaurant sales, will be 4.2% in 2014 as a result of the terms outlined above.

We also generally contribute 4% of restaurant sales from our Burger King restaurants to fund BKC's national and regional advertising. BKC engages in substantial national and regional advertising and promotional activities and other efforts to maintain and enhance the Burger King brand. From time to time we supplement BKC's marketing with our own local advertising and promotional campaigns. See “- Advertising, Products and Promotion” below.

Our franchise agreements with BKC do not give us exclusive rights to operate Burger King restaurants in any defined territory. Although we believe that BKC generally seeks to ensure that newly granted franchises do not materially adversely affect the operations of existing Burger King restaurants, we cannot assure you that franchises granted by BKC to third parties will not adversely affect any Burger King restaurants that we operate.

Except as permitted by the operating agreement, we are required to obtain BKC's consent before we acquire existing Burger King restaurants from other franchisees or develop new Burger King restaurants. BKC also has the right of first refusal to purchase any Burger King restaurant that is being offered for sale by a franchisee. However, pursuant to the operating agreement, BKC assigned the ROFR to us in 20 states and granted us franchise pre-approval to build new restaurants or acquire restaurants from franchisees until the date that we operate 1,000 restaurants. Historically, BKC has approved substantially all of our acquisitions of restaurants from other franchisees.

Advertising, Products and Promotion

BKC's marketing strategy is characterized by its HAVE IT YOUR WAY® service, TASTE IS KING® tag line, flame grilling, generous portions and competitive prices. Burger King restaurants feature flame-grilled hamburgers, the most popular of which is the Whopper® sandwich, a large, flame-grilled hamburger garnished with mayonnaise, lettuce, onions, pickles and tomatoes. The basic menu of all Burger King restaurants also includes a variety of hamburgers, chicken and other specialty sandwiches, french fries, soft drinks, salads, breakfast items, snacks, and other offerings.

BKC and its franchisees have historically spent between 4% and 5% of their respective sales on marketing, advertising and promotion to sustain high brand awareness. In 2012, BKC launched marketing initiatives to reach a more diverse consumer base and has continued to introduce a number of new and enhanced products to broaden menu offerings and drive customer traffic in all day parts.

We are generally required to contribute 4% of restaurant sales to an advertising fund utilized by BKC for its advertising, promotional programs and public relations activities. For the restaurants acquired from BKC in 2012, the franchise agreements provide for an advertising contribution of 4% of restaurant sales and local advertising investment spending of no less than 0.75% of restaurant sales in the designated market areas where the franchised restaurants are located, subject to certain other conditions and limitations. BKC's advertising programs consist of national campaigns supplemented by local advertising. BKC's advertising campaigns are generally carried on television, radio and in circulated print media (national and regional newspapers and magazines). As a percentage of our restaurant sales advertising expense was 4.5% in 2013, 4.1% in 2012 and 4.2% in 2011. For 2014 we anticipate advertising expense to range between 4.0% and 4.2% of restaurant sales.

The efficiency and quality of advertising and promotional programs can significantly affect the quick-service restaurant businesses. We believe that one of the major advantages of being a Burger King franchisee is the value of the extensive national and regional advertising and promotional programs conducted by BKC. In addition to the benefits derived from BKC's advertising spending, we sometimes supplement BKC's advertising and promotional activities with our own local advertising and promotions, including the purchase of additional television, radio and print advertising. The concentration of our Burger King restaurants in many of our markets permits us to leverage advertising in those markets. We also utilize promotional programs, such as combination value meals and discounted prices, targeted to our customers, in order to create a flexible and directed marketing program.

In connection with BKC's 2011 initiatives to support the installation of digital menu boards, the introduction of new menu items and enhancements to the quality of our food preparation, we made expenditures in our restaurants of approximately $9.0 million in 2011 and $0.5 million in 2012. Beginning in 2012, BKC reduced the required advertising contribution by $5,400 per restaurant per year through 2015, for those restaurants whose expenditures included a digital menu board, and $3,000 per restaurant per year through 2015, for those restaurants whose expenditures excluded a digital menu board. At December 29, 2013 we had 284 restaurants qualifying for the $5,400 per year advertising reduction and 11 restaurants qualifying for the $3,000 per year advertising reduction. To receive the advertising reductions prospectively we must be in full compliance with our franchise agreements including being current on all payments to BKC for royalties, advertising and occupancy related charges. As of December 29, 2013 we were in compliance with our franchise agreements.

Suppliers

We are a member of a national purchasing cooperative, Restaurant Services, Inc., which we refer to as "RSI", created for the Burger King system. RSI is a non-profit independent cooperative that acts as the purchasing agent for approved distributors to the Burger King system and serves to negotiate the lowest cost for the system. We use our purchasing power to negotiate directly with certain other vendors, to obtain favorable pricing and terms for supplying our restaurants. For our restaurants, we are required to purchase all of our foodstuffs, paper goods and packaging materials from BKC-approved suppliers. We currently utilize three distributors, Maines Paper & Food Service, Inc., Reinhart Food Service L.L.C. and MBM Food Service Inc., to supply our restaurants with the majority of our foodstuffs and, as of December 29, 2013, such distributors supplied 38%, 33% and 29%, respectively, of our restaurants. We may purchase non-food items, such as kitchen utensils, equipment maintenance tools and other supplies, from any suitable source so long as such items meet BKC product uniformity standards. All BKC-approved distributors are required to purchase foodstuffs and supplies from BKC-approved manufacturers and purveyors. BKC is responsible for monitoring quality control and supervision of these manufacturers and conducts regular visits to observe the preparation of foodstuffs, and to run various tests to ensure that only quality foodstuffs are sold to its approved suppliers. In addition, BKC coordinates and supervises audits of approved suppliers and distributors to determine continuing product specification compliance and to ensure that manufacturing plant and distribution center standards are met. Although we believe that we have alternative sources of supply available to our restaurants, in the event any distributor or supplier for our restaurants was unable to service us, this could lead to a disruption of service or supply at our restaurants until a new distributor or supplier is engaged, which could have an adverse effect on our business.

Quality Assurance

Our operational focus is closely monitored to achieve a high level of customer satisfaction via speed of service, order accuracy and quality of service. Our senior management and restaurant management staffs are principally responsible for ensuring compliance with BKC's required operating procedures. We have uniform operating standards and specifications relating to the quality, preparation and selection of menu items, maintenance and cleanliness of the premises and employee conduct. In order to maintain compliance with these operating standards and specifications, we distribute to our restaurant operations management team detailed reports measuring compliance with various customer service standards and objectives, including feedback obtained directly from our customers through instructions given to them at the point of sale. The customer feedback is monitored by an independent agency and us and consists of evaluations of speed of service, quality of service, quality of our menu items and other operational objectives including the cleanliness of our restaurants. We also have our own staff that handle customer inquiries and complaints.

We operate in accordance with quality assurance and health standards mandated by federal, state and local governmental laws and regulations. These standards include food preparation rules regarding, among other things, minimum cooking times and temperatures, maximum time standards for holding prepared food, food handling guidelines and cleanliness. To maintain these standards, we conduct unscheduled inspections of our restaurants. In addition, restaurant managers conduct internal inspections for taste, quality, cleanliness and food safety on a regular basis.

Trademarks

As a franchisee of Burger King, we also have contractual rights to use certain BKC-owned trademarks, service marks and other intellectual property relating to the Burger King concept. We have no proprietary intellectual property other than the Carrols logo and trademark.

Government Regulation

Various federal, state and local laws affect our business, including various health, sanitation, fire and safety standards. Restaurants to be constructed or remodeled are subject to state and local building code and zoning requirements. In connection with the development and remodeling of our restaurants, we may incur costs to meet certain federal, state and local regulations, including regulations promulgated under the Americans with Disabilities Act.

We are subject to the federal Fair Labor Standards Act and various other federal and state laws governing such matters as:

- minimum wage requirements;
- unemployment compensation;
- overtime; and
- other working conditions and citizenship requirements.

A significant number of our food service personnel are paid at rates related to the federal, and where applicable, state minimum wage and, accordingly, increases in the minimum wage have increased and in the future will increase wage rates at our restaurants.

We are assessing the Patient Protection and Affordable Care Act (the “Act”) that requires businesses employing fifty or more full-time equivalent employees to offer health care benefits to those full-time employees beginning in January 2015, or be subject to an annual penalty. Those benefits must be provided under a health care plan which provides a certain minimum scope of health care services. The Act also limits the portion of the cost of the benefits which we can require employees to pay.

We are continuing to assess the financial impact of the Act including the provision beginning in 2015 to offer health insurance to our hourly employees who work an average of 30 hours or more per week. There are no assurances that a combination of cost management and menu price increases can accommodate all of the potential increased costs associated with these regulations.

We are also subject to various federal, state and local environmental laws, rules and regulations. We believe that we conduct our operations in substantial compliance with applicable environmental laws and regulations. Our costs for compliance with environmental laws or regulations have not had a material adverse effect on our results of operations, cash flows or financial condition in the past.

Industry and Competition

The Restaurant Market

Restaurant sales historically have closely tracked several macroeconomic indicators and we believe that “away-from-home” food consumption will increase as the economy continues to improve. Historically, unemployment has been inversely related to restaurant sales and, as the unemployment rate decreases and disposable income increases, restaurant sales have increased. In 2012, 49.5% of food dollars were spent on food away from home and is projected to surpass at-home dining in 2015 according to the U.S. Department of Agriculture.

Quick-Service Restaurants. We operate in the hamburger category of the quick-service restaurant segment of the restaurant industry. Quick-service restaurants are distinguished by high speed of service and efficiency, convenience, limited menu and service, and value pricing. According to Nation's Restaurant News, 2012 U.S. foodservice sales for the Top 100 restaurant chains were $213.7 billion. Of this amount, the hamburger category represented $71.7 billion, or 33.6%, making it the largest category of the quick-service segment.

The restaurant industry is highly competitive with respect to price, service, location and food quality. In each of our markets, our restaurants compete with a large number of national and regional restaurant chains, as well as locally owned restaurants, offering low and medium-priced fare. We also compete with convenience stores, delicatessens and prepared food counters in supermarkets, grocery stores, cafeterias and other purveyors of moderately priced and quickly prepared foods.

We believe that:

- product quality and taste;
- brand recognition;

- convenience of location;
- speed of service;
- menu variety;
- price; and
- ambiance

are the most important competitive factors in the quick-service restaurant segment and that our restaurants effectively compete in each category. We believe our largest competitors are McDonald's and Wendy's.

Employees

As of December 29, 2013, we employed approximately 17,500 persons of which approximately 160 were administrative personnel and approximately 17,340 were restaurant operations personnel. None of our employees are are unionized or covered by collective bargaining agreements. We believe that our overall relations with our employees are good.

Availability of Information

We file annual, quarterly and current reports and other information with the Securities and Exchange Commission (the "SEC"). The public may read and copy any materials we file with the SEC at the SEC's Public Reference Room at 100 F Street, NE, Washington, DC 20549. The public may obtain information on the operation of the Public Reference Room by calling the SEC at 1-800-SEC-0330. The SEC also maintains a website that contains reports, proxy and information statements and other information regarding issuers that file electronically with the SEC at www.sec.gov.

We make available through our website (www.carrols.com) our annual report on Form 10-K, quarterly reports on Form 10-Q, current reports on Form 8-K and amendments to those reports, as well as other reports relating to us that are filed or furnished to the SEC, as soon as reasonably practicable after electronically filing such material with the SEC. The reference to our website address is a textual reference only, meaning that it does not constitute incorporation by reference of the information contained on the website and should not be considered part of this document.

ITEM 1A. RISK FACTORS

You should carefully consider the risks described below, as well as other information and data included in this Annual Report on Form 10-K. Any of the following risks could materially adversely affect our business, consolidated financial condition or results of operations.

Risks Related to Our Business

Intense competition in the restaurant industry could make it more difficult to profitably expand our business and could also have a negative impact on our operating results if customers favor our competitors or we are forced to change our pricing and other marketing strategies.

The restaurant industry is highly competitive. In each of our markets, our restaurants compete with a large number of national and regional restaurant chains, as well as locally owned restaurants, offering low and medium-priced fare. We also compete with convenience stores, delicatessens and prepared food counters in grocery stores, supermarkets, cafeterias and other purveyors of moderately priced and quickly prepared food. Our largest competitors are McDonald's and Wendy's restaurants.

Due to competitive conditions, we, as well as certain of the other major quick-service restaurant chains, have offered select food items and combination meals at discounted prices. These pricing and marketing strategies have had, and in the future may have, a negative impact on our sales and earnings.

Factors applicable to the quick-service restaurant segment may adversely affect our results of operations, which may cause a decrease in earnings and revenues.

The quick-service restaurant segment is highly competitive and can be materially adversely affected by many factors, including:

- changes in local, regional or national economic conditions;
- changes in demographic trends;
- changes in consumer tastes;
- changes in traffic patterns;
- increases in fuel prices and utility costs;
- consumer concerns about health, diet and nutrition;
- increases in the number of, and particular locations of, competing restaurants;
- changes in discretionary consumer spending;
- inflation;
- increases in the cost of food, such as beef, chicken, produce and packaging;

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- increased labor costs, including healthcare, unemployment insurance and minimum wage requirements;
- the availability of experienced management and hourly-paid employees; and
- regional weather conditions.

We are highly dependent on the Burger King system and our ability to renew our franchise agreements with BKC. The failure to renew our franchise agreements or Burger King's failure to compete effectively would materially adversely affect our results of operations.

Due to the nature of franchising and our agreements with BKC, our success is, to a large extent, directly related to the success of the Burger King system including its financial condition, advertising programs, new products, overall quality of operations and the successful and consistent operation of Burger King restaurants owned by other franchisees. We cannot assure you that Burger King will be able to compete effectively with other restaurants. As a result, any failure of Burger King to compete effectively would likely have a material adverse effect on our operating results.

Under each of our franchise agreements with BKC, we are required to comply with operational programs established by BKC. For example, our franchise agreements with BKC require that our restaurants comply with specified design criteria. In addition, BKC generally has the right to require us during the tenth year of a franchise agreement to remodel our restaurants to conform to the then-current image of Burger King, which may require the expenditure of considerable funds. In addition we may not be able to avoid adopting menu price discount promotions or permanent menu price decreases instituted by BKC that may be unprofitable.

Our franchise agreements typically have a 20-year term after which BKC's consent is required to receive a successor franchise agreement. Our franchise agreements with BKC that are set to expire over the next three years are as follows: 24 in 2014, 21 in 2015 and 19 in 2016.

We cannot assure you that BKC will grant each of our future requests for successor franchise agreements, and any failure of BKC to renew our franchise agreements could adversely affect our operating results. In addition, as a condition of approval of a successor franchise agreement, BKC may require us to make capital improvements to particular restaurants to bring them up to Burger King current image standards, which may require us to incur substantial costs.

In addition, our franchise agreements with BKC do not give us exclusive rights to operate Burger King restaurants in any defined territory. Although we believe that BKC generally seeks to ensure that newly granted franchises do not materially adversely affect the operations of existing restaurants, we cannot assure you that franchises granted by BKC to third parties will not adversely affect any restaurants that we operate.

Additionally, as a franchisee, we have no control over the Burger King brand. If BKC does not adequately protect the Burger King brand and other intellectual property, our competitive position and operating results could be harmed.

Our strategy includes pursuing acquisitions of additional Burger King restaurants and we may not find Burger King restaurants that are suitable acquisition candidates or successfully operate or integrate any Burger King restaurants we may acquire.

As part of our strategy, we intend to pursue the acquisition of additional Burger King restaurants. Pursuant to the operating agreement, dated as of May 30, 2012, between BKC and Carrols LLC, BKC assigned to us its ROFR under its franchise agreements with its franchisees to purchase all of the assets of a restaurant or all or substantially all of the voting stock of the franchisee, whether direct or indirect, on the same terms proposed between such franchisee and a third party purchaser in 20 states as follows: Connecticut (except Hartford county), Delaware, Indiana, Kentucky, Maine, Maryland, Massachusetts (except for Middlesex, Norfolk and Suffolk counties), Michigan, New Hampshire, New Jersey, New York (except for Bronx, Kings, Nassau, New York, Queens, Richmond, Suffolk and Westchester counties), North Carolina, Ohio, Pennsylvania, Rhode Island, South Carolina, Vermont, Virginia, Washington DC, and West Virginia. In addition, pursuant to the operating agreement, BKC granted us, on a non-exclusive basis, franchise pre-approval to, among other things, acquire restaurants from Burger King franchisees in the DMAs until the date that we operate 1,000 Burger King restaurants. As part of the franchise pre-approval, BKC granted us pre-approval for acquisitions of restaurants from franchisees in the 20 states where we have an existing Burger King restaurant, subject to and in accordance with the terms of the operating agreement. Although we believe that opportunities for future acquisitions may be available from time to time, competition for acquisition candidates may exist or increase in the future. Consequently, there may be fewer acquisition opportunities available to us at an attractive acquisition price. There can be no assurance that we will be able to identify, acquire, manage or successfully integrate additional restaurants without substantial costs, delays or operational or financial problems. In the event we are able to acquire additional restaurants, the integration and operation of the acquired BKC restaurants may place significant demands on our management, which could adversely affect our ability to manage our existing restaurants.

We may be required to obtain additional financing to fund future acquisitions. There can be no assurance that we will be able to obtain additional financing, if necessary, on acceptable terms or at all. Both our senior credit facility and the indenture governing the $150 million of 11.25% Senior Secured Second Lien Notes due 2018 (the "Notes") contain restrictive covenants that may prevent us from incurring additional debt to acquire additional Burger King restaurants.

We are required to make substantial capital expenditures in connection with the acquisition of the acquired BKC restaurants.

The remodeling of our Burger King restaurants (including the acquired BKC restaurants) pursuant to the agreed upon remodel plan set forth in the operating agreement may be substantially costlier than we currently anticipate. In addition, we may incur substantial capital expenditures as a result of acquiring restaurants, including restaurants acquired by exercising the ROFR. If we are required to make greater than anticipated capital expenditures in connection with either or both of these activities, our business, financial condition and cash flows could be adversely affected.

We may experience difficulties in integrating restaurants acquired by us into our existing business.

The future acquisition of a significant number of restaurants will involve the integration of those acquired restaurants with our existing business. The difficulties of integration include:

- coordinating and consolidating geographically separated systems and facilities;
- integrating the management and personnel of the acquired restaurants, maintaining employee morale and retaining key employees;
- implementing our management information systems; and
- implementing operational procedures and disciplines to control costs and increase profitability.

The process of integrating operations could cause an interruption of, or loss of momentum in, the activities of our business and the loss of key personnel. The diversion of management's attention and any delays or difficulties encountered in connection with the acquisition of restaurants and integration of acquired restaurants' operations could have an adverse effect on our business, results of operations and financial condition.

Achieving the anticipated benefits of the acquisition of additional restaurants will depend in part upon whether we can integrate any acquired restaurants in an efficient and effective manner. We may not accomplish this integration process smoothly or successfully. If management is unable to successfully integrate acquired restaurants, the anticipated benefits of the acquisition may not be realized.

In our evaluation of potential acquisitions, assumptions are made as to our ability to increase sales as well as improve restaurant-level profitability particularly in the areas of food, labor and cash controls as well as other operating expenses. If we are not able to make such improvements in these operational areas as planned, the acquired restaurants' targeted profitability levels will be affected which could cause an adverse effect on our overall financial results and financial condition.

We could be adversely affected by food-borne illnesses, as well as widespread negative publicity regarding food quality, illness, injury or other health concerns.

Negative publicity about food quality, illness, injury or other health concerns (including health implications of obesity) or similar issues stemming from one restaurant or a number of restaurants could materially adversely affect us, regardless of whether they pertain to our own restaurants, other Burger King restaurants, or to restaurants owned or operated by other companies. For example, health concerns about the consumption of beef or chicken or by specific events such as the outbreak of “mad cow” disease and “avian” flu could lead to changes in consumer preferences, reduce consumption of our products and adversely affect our financial performance. These events could also reduce the available supply of beef or chicken or significantly raise the price of beef or chicken.

In addition, we cannot guarantee that our operational controls and employee training will be effective in preventing food-borne illnesses, food tampering and other food safety issues that may affect our restaurants. Food-borne illness or food tampering incidents could be caused by customers, employees or food suppliers and transporters and, therefore, could be outside of our control. Any publicity relating to health concerns or the perceived or specific outbreaks of food-borne illnesses, food tampering or other food safety issues attributed to one or more of our restaurants, could result in a significant decrease in guest traffic in all of our restaurants and could have a material adverse effect on our results of operations. In addition, similar publicity or occurrences with respect to other restaurants or restaurant chains could also decrease our guest traffic and have a similar material adverse effect on our business.

We may incur significant liability or reputational harm if claims are brought against us or the Burger King brand.

We may be subject to complaints, regulatory proceedings or litigation from guests or other persons alleging food-related illness, injuries suffered in our premises or other food quality, health or operational concerns, including environmental claims. In addition, in recent years a number of restaurant companies have been subject to lawsuits, including class action lawsuits, alleging, among other things, violations of federal and state law regarding workplace and employment matters, discrimination, harassment, wrongful termination and wage, rest break, meal break and overtime compensation issues and, in the case of quick service restaurants, alleging that they have failed to disclose the health risks associated with high fat or high sodium foods and that their marketing practices have encouraged obesity. We may also be subject to litigation or other actions initiated by governmental authorities, our employees, among others, based upon these and other matters. Adverse publicity resulting from such allegations or occurrences or alleged discrimination or other operating issues stemming from one or a number of our locations could adversely affect our business, regardless of whether the allegations are true, or whether we are ultimately held liable. Any cases filed against us could materially adversely affect us if we lose such cases and have to pay substantial damages or if we settle such cases. In addition, any such cases may materially and adversely affect our operations by increasing our litigation costs and diverting our attention and resources to address such actions. In addition, if a claim is successful, our insurance coverage may not cover or be adequate to cover all liabilities or losses and we may not be able to continue to maintain such insurance, or to obtain comparable insurance at a reasonable cost, if at all. If we suffer losses, liabilities or loss of income in excess of our insurance coverage or if our insurance does not cover such loss, liability or loss of income, there could be a material adverse effect on our results of operations.

Changes in consumer taste could negatively impact our business.

We obtain a significant portion of our revenues from the sale of hamburgers and various types of sandwiches. If consumer preferences for these types of foods change, it could have a material adverse effect on our operating results. The quick-service restaurant segment is characterized by the frequent introduction of new products, often supported by substantial promotional campaigns, and is subject to changing consumer preferences, tastes, and eating and purchasing habits. Our success depends on BKC's ability to anticipate and respond to changing consumer preferences, tastes and dining and purchasing habits, as well as other factors affecting the restaurant industry, including new market entrants and demographic changes. BKC may be forced to make changes to our menu items in order to respond to changes in consumer tastes or dining patterns, and we may lose customers who do not prefer the new menu items. In recent years, numerous companies in the quick-service restaurant segments have introduced products positioned to capitalize on the growing consumer preference for food products that are, or are perceived to be, promoting good health, nutritious, low in calories and low in fat content. If BKC does not continually develop and successfully introduce new menu offerings that appeal to changing consumer preferences or if the Burger King system does not timely capitalize on new products, our operating results could suffer. In addition, any significant event that adversely affects consumption of our products, such as cost, changing tastes or health concerns, could adversely affect our financial performance.

If a significant disruption in service or supply by any of our suppliers or distributors were to occur, it could create disruptions in the operations of our restaurants, which could have a material adverse effect on our business.

Our financial performance depends on our continuing ability to offer fresh, quality food at competitive prices. If a significant disruption in service or supply by our suppliers or distributors were to occur, it could create disruptions in the operations of our restaurants, which could have a material adverse effect on us.

We are a member of a national purchasing cooperative, Restaurant Services, Inc., or "RSI," which serves as the purchasing agent for approved distributors to the Burger King system. We are required to purchase all of our foodstuffs, paper goods and packaging materials from BKC-approved suppliers. We currently utilize three distributors for our restaurants, Maines Paper & Food Service, Inc., Reinhart Food Service L.L.C. and MBM Food Service Inc., to supply our restaurants in various geographical areas. As of December 29, 2013, such distributors supplied 38%, 33% and 29%, respectively of our restaurants. Although we believe that we have alternative sources of supply, in the event any distributors or suppliers are unable to service us, this could lead to a disruption of service or supply until a new distributor or supplier is engaged, which could have an adverse effect on our business.

If labor costs increase, we may not be able to make a corresponding increase in our prices and our operating results may be adversely affected.

Wage rates for a number of our employees are at or above the federal and or state minimum wage rates. As federal and/or state minimum wage rates increase, we may need to increase not only the wage rates of our minimum wage employees but also the wages paid to the employees at wage rates which are above the minimum wage, which will increase our costs. To the extent that we are not able to raise our prices to compensate for increases in wage rates, including increases in state unemployment insurance costs or other costs including mandated health insurance, this could have a material adverse effect on our operating results. In addition, even if minimum wage rates do not increase, we may still be required to raise wage rates in order to compete for an adequate supply of labor for our restaurants.

The efficiency and quality of our competitors' advertising and promotional programs and the extent and cost of our advertising could have a material adverse effect on our results of operations and financial condition.

The success of our restaurants depends in part upon the effectiveness of the advertising campaigns and promotions by BKC. If our competitors increase spending on advertising and promotion, or the cost of television or radio advertising increases, or BKC's or our advertising and promotions are less effective than our competitors', there could be a material adverse effect on our results of operations and financial condition.

Our business is regional and we therefore face risks related to reliance on certain markets as well as risks for other unforeseen events.

At December 29, 2013, 36% of our restaurants are located in New York and Ohio and 30% of our restaurants are located in North Carolina and South Carolina. Therefore, the economic conditions, state and local government regulations, weather conditions or other conditions affecting New York, Ohio, North Carolina and South Carolina and other unforeseen events, including terrorism and other international conflicts may have a material impact on the success of our restaurants in those locations.

Many of our restaurants are located in regions that may be susceptible to severe weather conditions such as harsh winter weather. As a result, adverse weather conditions in any of these areas could damage these restaurants, result in fewer guest visits to these restaurants and otherwise have a material adverse impact on our business.

We cannot assure you that the current locations of our restaurants will continue to be economically viable or that additional locations will be acquired at reasonable costs.

The location of our restaurants has significant influence on their success. We cannot assure you that current locations will continue to be economically viable or that additional locations can be acquired at reasonable costs. In addition, the economic environment where restaurants are located could decline in the future, which could result in reduced sales in those locations. We cannot assure you that new sites will be profitable or as profitable as existing sites.

Economic downturns may adversely impact consumer spending patterns.

The U.S. economy recently underwent a significant slowdown and volatility due to uncertainties related to availability of credit, difficulties in the banking and financial services sectors, softness in the housing market, diminished market liquidity, falling consumer confidence and high unemployment rates. Our business is dependent to a significant extent on national, regional and local economic conditions, particularly those that affect our guests that frequently patronize our restaurants. In particular, where our customers' disposable income is reduced (such as by job losses, credit constraints and higher housing, tax, energy, interest or other costs) or where the perceived wealth of customers has decreased (because of circumstances such as lower residential real estate values, increased foreclosure rates, increased tax rates or other economic disruptions), our restaurants have in the past experienced, and may in the future experience, lower sales and customer traffic as customers choose lower-cost alternatives or other alternatives to dining out. The resulting decrease in our customer traffic or average sales per transaction has had an adverse effect in the past, and could in the future have a material adverse effect, on our business.

The loss of the services of our senior management could have a material adverse effect on our business, financial condition or results of operations.
Our success depends to a large extent upon the continued services of our senior management who have substantial experience in the restaurant industry. We believe that it could be difficult to replace our senior management with individuals having comparable experience. Consequently, the loss of the services of members of our senior management could have a material adverse effect on our business, financial condition or results of operations.
Government regulation could adversely affect our financial condition and results of operations.
We are subject to extensive laws and regulations relating to the development and operation of restaurants, including regulations relating to the following:

- zoning;
- requirements relating to labeling of caloric and other nutritional information on menu boards, advertising and food packaging;
- the preparation and sale of food;
- employer/employee relationships, including minimum wage requirements, overtime, working and safety conditions, and citizenship requirements;
- health care; and
- federal and state laws that prohibit discrimination and laws regulating design and operation of, and access to, facilities, such as the Americans With Disabilities Act of 1990.

In the event that legislation having a negative impact on our business is adopted, it could have a material adverse impact on us. For example, substantial increases in the minimum wage or state or Federal unemployment taxes could adversely affect our financial condition and results of operations. Local zoning or building codes or regulations can cause substantial delays in our ability to build and open new restaurants. Any failure to obtain and maintain required licenses, permits and approvals could also adversely affect our operating results.
We are continuing to assess the various provisions of the comprehensive federal health care reform law enacted in 2010, including its estimated impact on our business as provisions becomes effective. There are no assurances that a combination of cost management and menu price increases can offset all of the potential increased costs associated with these regulations.
Federal, state and local environmental regulations relating to the use, storage, discharge, emission and disposal of hazardous materials could expose us to liabilities, which could adversely affect our results of operations.
We are subject to a variety of federal, state and local environmental regulations relating to the use, storage, discharge, emission and disposal of hazardous substances or other regulated materials, release of pollutants into the air, soil and water, and the remediation of contaminated sites.
Failure to comply with environmental laws could result in the imposition of fines or penalties, restrictions on operations by governmental agencies or courts of law, as well as investigatory or remedial liabilities and claims for alleged personal injury or damages to property or natural resources. Some environmental laws impose strict, and under some circumstances joint and several, liability for costs of investigation and remediation of contaminated sites on current and prior owners or operators of the sites, as well as those entities that send regulated materials to the sites. We cannot assure you that we have been or will be at all times in complete compliance with such laws, regulations and permits. Therefore, our costs of complying with current and future environmental, health and safety laws could adversely affect our results of operations.
We are subject to all of the risks associated with leasing property subject to long-term non-cancelable leases.
The leases for our restaurant locations (except for acquired BKC restaurants sub-leased by BKC to us which have an underlying lease term of less than 20 years) generally have initial terms of 20 years, and typically provide for renewal options in five year increments as well as for rent escalations. Generally, our leases are “net” leases, which require us to pay all of the costs of insurance, taxes, maintenance and utilities. Additional sites that we lease are likely to be subject to similar long-term non-cancelable leases. We generally cannot cancel our leases. If an existing or future restaurant is not profitable, and we decide to close it, we may nonetheless be obligated to perform our monetary obligations under the applicable lease including, among other things, paying all amounts due for the balance of the lease term. In addition, as each of our leases expire, we may fail to negotiate renewals, either on commercially acceptable terms or

any terms at all, which could cause us to close restaurants in desirable locations.

An increase in food costs could adversely affect our operating results.

Our profitability and operating margins are dependent in part on our ability to anticipate and react to changes in food costs. Changes in the price or availability of certain food products could affect our ability to offer broad menu and price offerings to guests and could materially adversely affect our profitability and reputation. The type, variety, quality and price of beef, chicken, produce and cheese can be subject to change and to factors beyond our control, including weather, governmental regulation, availability and seasonality, each of which may affect our food costs or cause a disruption in our supply. For example, weather patterns in recent years have resulted in lower than normal levels of rainfall in key agricultural states such as California, impacting the price of water and the corresponding prices of food commodities grown in states facing drought conditions. Our food distributors or suppliers also may be affected by higher costs to produce and transport commodities used in our restaurants, higher minimum wage and benefit costs and other expenses that they pass through to their customers, which could result in higher costs for goods and services supplied to us. Although RSI is able to contract for certain food commodities for periods up to one year, the pricing and availability of some commodities used in our operations are not locked in for periods of longer than one week or at all. We do not currently use financial instruments to hedge our risk to market fluctuations in the price of beef, produce and other food products. We may not be able to anticipate and react to changing food costs (including anticipated increases in food costs in 2014) through menu price adjustments in the future, which could negatively impact our results of operations.

Security breaches of confidential guest information in connection with our electronic processing of credit and debit card transactions may adversely affect our business.

A significant amount of our restaurant sales are by credit or debit cards. Other restaurants and retailers have recently experienced security breaches in which credit and debit card information of their customers was compromised. We may in the future become subject to lawsuits or other proceedings for purportedly fraudulent transactions arising out of the actual or alleged theft of our guests' credit or debit card information. Any such claim or proceeding, or any adverse publicity resulting from these allegations, may have a material adverse effect on us and our restaurants.

We depend on information technology and any material failure of that technology could impair our ability to efficiently operate our business.

We rely on information systems across our operations, including, for example, point-of-sale processing in our restaurants, procurement and payment to other significant suppliers, collection of cash, and payment of other financial obligations and various other processes and procedures. Our ability to efficiently manage our business depends significantly on the reliability and capacity of these systems. The failure of these systems to operate effectively, problems with maintenance, upgrading or transitioning to replacement systems or a breach in security of these systems could cause delays in customer service and reduce efficiency in our operations. Significant capital investments might be required to remediate any problems.

Carrols is currently a guarantor under 35 Fiesta restaurant property leases and the primary lessee on five Fiesta restaurant property leases, and any default under such property leases by Fiesta may result in substantial liabilities to us.

Carrols currently is a guarantor under 35 Fiesta restaurant property leases. The Separation and Distribution Agreement, which we refer to as the "separation agreement", dated as of April 24, 2012 and entered into in connection with the spin-off among Carrols, Fiesta and us provides that the parties will cooperate and use their commercially reasonable efforts to obtain the release of such guarantees. Unless and until any such guarantees are released, Fiesta agrees to indemnify Carrols for any losses or liabilities or expenses that it may incur arising from or in connection with any such lease guarantees.

Carrols is currently a primary lessee of five Fiesta restaurants which it subleases to Fiesta. The separation agreement provides that the parties will cooperate and use their commercially reasonable efforts to cause Fiesta or a subsidiary of Fiesta to enter into a new master lease or individual leases with the lessor with respect to the Fiesta restaurants where Carrols is currently a lessee. The separation agreement provides that until such new master lease or such individual leases are entered into, (i) Carrols will perform its obligations under the master lease for the five Fiesta restaurants where it is a lessee and (ii) the parties will cooperate and use their commercially reasonable efforts to enter into with the lessor a non-disturbance agreement or similar agreement which shall provide that Fiesta or one of its subsidiaries shall become the lessee under such master lease with respect to such Fiesta restaurants and perform Carrols' obligations under such master lease in the event of a breach or default by Carrols.

Such guarantees may never be released and a new master lease with respect to the five Fiesta properties where Carrols is the primary lessee may never be entered into by Fiesta. Any losses or liabilities that may arise in connection such guarantees or the master lease where Carrols is not able to receive indemnification from Fiesta may result in substantial liabilities to us and could have a material adverse effect on our business.

We and our stockholders may be subject to substantial liabilities if the spin-off is treated as a taxable transaction.

We have received a private letter ruling from the Internal Revenue Service, which we refer to as the "IRS" to the effect that, among other things, the spin-off will qualify as a tax-free distribution for U.S. federal income tax purposes under Section 355 of the Internal Revenue Code of 1986, as amended, which we refer to as the "Code", and as part of a tax-free reorganization under Section 368(a)(1)(D) of the Code, and the transfer to Fiesta of assets and the assumption by Fiesta of liabilities in connection with the spin-off will not result in the recognition of any gain or loss for U.S. federal income tax purposes to us. Our tax advisor provided a tax opinion covering certain matters not covered in the private letter ruling. The tax opinion is not binding on the IRS or the courts.

Although a private letter ruling is generally binding on the IRS, the continuing validity of the ruling will be subject to the accuracy of factual representations and assumptions made in connection with obtaining such private letter ruling, including with respect to post-spin-off operations and conduct of the parties. Also, as part of the IRS's general policy with respect to rulings on spin-off transactions under Section 355 of the Code, the private letter ruling we obtained is based upon representations by us that certain conditions which are necessary to obtain tax-free treatment under the Code have been satisfied, rather than a determination by the IRS that these conditions have been satisfied. Failure to satisfy such necessary conditions, or any inaccuracy in any representations made by us in connection with the ruling, could invalidate the ruling.

If the spin-off does not qualify for tax-free treatment for U.S. federal income tax purposes, then, in general, we would be subject to tax as if we had sold the common stock of Fiesta in a taxable sale for its fair market value, and our stockholders would be subject to tax as if they had received a taxable distribution in an amount equal to the fair market value of Fiesta common stock distributed to them. If the transfer to Fiesta of assets and the assumption by Fiesta of liabilities in connection with the spin-off do not qualify for tax-free treatment, then, in general, we would be subject to tax as if we had sold assets to Fiesta in exchange for the financing proceeds distributed from Fiesta to us and the assumption of liabilities by Fiesta. It is expected that the amount of any such taxes to our stockholders and to us would be substantial.

The Tax Matters Agreement, which we refer to as the "tax matters agreement", dated as of April 24, 2012 and entered into by Fiesta with us in connection with the spin-off (1) governs the allocation of the tax assets and liabilities between Fiesta, and us, (2) provides for certain restrictions and indemnities in connection with the tax treatment of the spin-off and (3) addresses certain other tax related matters including, without limitation, those relating to (a) the obligations of Fiesta and us with respect to the preparation of filing of tax returns for all periods, and (b) the control of any income tax audits and any indemnities with respect thereto. In the tax matters agreement, we have agreed to indemnify Fiesta for losses and taxes imposed on Fiesta and its affiliates resulting from our breach of our representations or covenants or our undertaking not to take certain post-spin-off actions, including with respect to our stock or assets, that would be inconsistent with or cause to be untrue any material information, covenant, or representation made in connection with the private letter ruling obtained by us from the IRS or otherwise cause the spin-off or the transfer to Fiesta of assets and the assumption by Fiesta of liabilities in connection with the spin-off to be subject to tax. Further, the tax matters agreement provides that we will be responsible for 50% of the losses and taxes of Carrols Restaurant Group and our affiliates and Fiesta and its affiliates resulting from the spin-off or the related transfer of assets and assumption of liabilities that are not attributable to any such action of ours or an equivalent action by Fiesta and its affiliates.

The tax matters agreement also provides that Fiesta will indemnify us for losses and taxes imposed on Carrols Restaurant Group and our affiliates resulting from the spin-off or the related transfer of assets and assumption of liabilities that are attributable to any such action by Fiesta and its affiliates. However, in such a case, we would be directly liable to the IRS for any such resulting taxes and would need to seek indemnification from Fiesta.

We have agreed to certain restrictions in order to comply with U.S. federal income tax requirements for a tax-free spin-off and may not be able to engage in acquisitions with related parties and other strategic transactions that may otherwise be in our best interests.

Current U.S. federal tax law that applies to spin-offs generally creates a presumption that the spin-off would be taxable to us (but not to our stockholders) if we engage in, or enter into an agreement to engage in, a plan or series of related transactions that would result in the acquisition of a 50% or greater interest (by vote or by value) in our stock ownership during the four-year period beginning on the date that begins two years before the spin-off, unless it is established that the transaction is not pursuant to a plan related to the spin-off. United States Treasury Regulations generally provide that whether an acquisition of our stock and a spin-off are part of a plan is determined based on all of the facts and circumstances, including specific factors listed in the regulations. In addition, the regulations provide certain “safe harbors” for acquisitions of our stock that are not considered to be part of a plan related to the spin-off.

There are other restrictions imposed on us under current U.S. federal tax law for spin-offs and with which we will need to comply in order to preserve the favorable tax treatment of the distribution, such as limitations on sales or redemptions of our common stock for cash or other property following the spin-off.

In the tax matters agreement with Fiesta, we accepted that, among other things, we will not take any actions that would result in any tax being imposed on us as a result of the spin-off. Further, for the two-year period following the spin-off, we agreed not to: (1) enter into, approve, agree to enter into, or substantially negotiate any transaction or series of transactions (in whatever form) resulting in a greater than 45% change in ownership of the vote or value of our equity or the equity of the surviving or successor entity, (2) merge, consolidate, liquidate, or partially liquidate Carrols Restaurant Group or any of the entities conducting the business relied upon in the IRS ruling as the "active business" of Carrols Restaurant Group, (3) permit the termination, sale, or transfer of, or a material change in, the business relied upon in the IRS ruling as the "active business" of Carrols Restaurant Group or the sale, issuance, or other disposition of the equity of the entities conducting such business,

(4) sell or otherwise dispose of assets in a way that would adversely affect tax-free status, (5) repurchase any of our stock except in circumstances permitted by IRS guidelines, or (6) take any actions inconsistent with the representations or covenants in the IRS ruling request, inconsistent with the ruling or tax opinion, or that would be reasonably likely to otherwise jeopardize tax-free status.
We will, however, be permitted to take certain actions otherwise prohibited by the tax matters agreement if we provide Fiesta with an opinion of tax counsel or private letter ruling from the IRS, reasonably acceptable to Fiesta, to the effect that these actions will not affect the tax-free nature of the spin-off. These restrictions could substantially limit our strategic and operational flexibility, including our ability to finance our operations by issuing equity securities, make acquisitions using equity securities, repurchase our equity securities, raise money by selling assets, or enter into business combination transactions.

The terms of the spin-off of Fiesta may reduce the likelihood of any potential change of control or unsolicited acquisition proposal that you might consider favorable.
The terms of the spin-off of Fiesta could delay or prevent a change of control that you may favor. An acquisition or issuance of our common stock could trigger the application of Section 355(e) of the Code, which would result in the imposition of a substantial federal income tax liability on us. Further, under the tax matters agreement that we and Carrols entered into with Fiesta in connection with the spin-off, we are required to indemnify Fiesta for any resulting tax imposed on it or its affiliates in connection with such an acquisition or issuance. This tax liability and indemnity obligation might discourage, delay or prevent a change of control that you may consider favorable.
Risks Related to Our Common Stock
The market price of our common stock may be highly volatile or may decline regardless of our operating performance.
The trading price of our common stock may fluctuate substantially. The price of our common stock that will prevail in the market may be higher or lower than the price you pay, depending on many factors, some of which are beyond our control. Broad market and industry factors may adversely affect the market price of our common stock, regardless of our actual operating performance. The fluctuations could cause a loss of all or part of an investment in our common stock. Factors that could cause fluctuation in the trading price of our common stock may include, but are not limited to the following:

- price and volume fluctuations in the overall stock market from time to time;
- significant volatility in the market price and trading volume of companies generally or restaurant companies;
- actual or anticipated variations in the earnings or operating results of our company or our competitors;
- actual or anticipated changes in financial estimates by us or by any securities analysts who might cover our stock or the stock of other companies in our industry;
- market conditions or trends in our industry and the economy as a whole;
- announcements by us or our competitors of significant acquisitions, strategic partnerships or divestitures and our ability to complete any such transaction;
- announcements of investigations or regulatory scrutiny of our operations or lawsuits filed against us;
- capital commitments;
- changes in accounting principles;
- additions or departures of key personnel;
- sales of our common stock, including sales of large blocks of our common stock or sales by our directors and officers; and
- the trading price of our common stock might also decline in reaction to events that affect BKC.

In addition, if the market for restaurant company stocks or the stock market in general experiences loss of investor confidence, the trading price of our common stock could decline for reasons unrelated to our business, results of operations or financial condition. The trading price of our common stock might also decline in reaction to events that affect other companies in our industry or related industries even if these events do not directly affect us.

In the past, following periods of volatility in the market price of a company's securities, class action securities litigation has often been brought against that company. Due to the potential volatility of our stock price, we may therefore be the target of securities litigation in the future. Securities litigation could result in substantial costs and divert management's attention and resources from our business, and could also require us to make substantial payments to satisfy judgments or to settle litigation.

The concentrated ownership of our capital stock by insiders will likely limit our stockholders' ability to influence corporate matters.

Our executive officers, directors and BKC together beneficially own approximately 33.3% of our outstanding common stock as of February 27, 2014 (assuming conversion of the Series A Preferred Stock). In addition, due to the issuance of Series A Preferred Stock to BKC in connection with our 2012 acquisition, BKC beneficially owns approximately 28.4% of our common stock as of February 27, 2014 (assuming conversion of the Series A Preferred Stock). In addition, our executive officers and directors (excluding directors affiliated with BKC) together beneficially own approximately 6.8% of our common stock outstanding as of February 27, 2014 (excluding conversion of the Series A Preferred Stock). As a result, our executive officers, directors and BKC, if they act as a group, will be able to significantly influence matters that require approval by our stockholders, including the election of directors and approval of significant corporate transactions such as mergers and acquisitions. The directors will have the authority to make decisions affecting our capital structure, including the issuance of additional debt and the declaration of dividends. BKC may also have interests that differ from yours and may vote in a way with which you disagree and which may be adverse to your interests. Corporate action might be taken even if other stockholders oppose them. This concentration of ownership might also have the effect of delaying or preventing a change of control of us that other stockholders may view as beneficial, could deprive our stockholders of an opportunity to receive a premium for their common stock as part of a sale of our company and might ultimately depress the market price of our common stock.

We do not expect to pay any cash dividends for the foreseeable future, and the indenture governing the Notes and the senior credit facility limit our ability to pay dividends to our stockholders.

We do not anticipate that we will pay any cash dividends to holders of our common stock in the foreseeable future. The absence of a dividend on our common stock may increase the volatility of the market price of our common stock or make it more likely that the market price of our common stock will decrease in the event of adverse economic conditions or adverse developments affecting our company. Additionally, the indenture governing the Notes and our senior credit facility limit, and the debt instruments that we may enter into in the future may limit our ability to pay dividends to our stockholders.

If securities analysts do not publish research or reports about our business or if they downgrade our stock, the price of our stock could decline.

The trading market for our common stock will rely in part on the research and reports that industry or financial analysts publish about us or our business. We cannot assure you that these analysts will publish research or reports about us or that any analysts that do so will not discontinue publishing research or reports about us in the future. If one or more analysts who cover us downgrade our stock, our stock price could decline rapidly. If analysts do not publish reports about us or if one or more analysts cease coverage of our stock, we could lose visibility in the market, which in turn could cause our stock price to decline.

Provisions in our restated certificate of incorporation and amended and restated bylaws, as amended, or Delaware law might discourage, delay or prevent a change of control of our company or changes in our management and, therefore, depress the trading price of our common stock.

Delaware corporate law and our restated certificate of incorporation and amended and restated bylaws, as amended, contain provisions that could discourage, delay or prevent a change in control of our company or changes in our management that the stockholders of our company may deem advantageous. These provisions:

- require that special meetings of our stockholders be called only by our board of directors or certain of our officers, thus prohibiting our stockholders from calling special meetings;
- deny holders of our common stock cumulative voting rights in the election of directors, meaning that stockholders owning a majority of our outstanding shares of common stock will be able to elect all of our directors;
- authorize the issuance of “blank check” preferred stock that our board could issue to dilute the voting and economic rights of our common stock and to discourage a takeover attempt;
- provide that approval of our board of directors or a supermajority of stockholders is necessary to make, alter or repeal our amended and restated bylaws and that approval of a supermajority of stockholders is necessary to amend, alter or change certain provisions of our restated certificate of incorporation;

- establish advance notice requirements for stockholder nominations for election to our board or for proposing matters that can be acted upon by stockholders at stockholder meetings;
- divide our board into three classes of directors, with each class serving a staggered 3-year term, which generally increases the difficulty of replacing a majority of the directors;
- provide that directors only may be removed for cause by a majority of the board or by a supermajority of our stockholders; and

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- require that any action required or permitted to be taken by our stockholders must be effected at a duly called annual or special meeting of stockholders and may not be effected by any consent in writing.

Risks Related to Our Indebtedness

Our substantial indebtedness could adversely affect our financial condition.

As a result of our substantial indebtedness, a significant portion of our cash flow will be required to pay interest and principal on our outstanding indebtedness, and we may not generate sufficient cash flow from operations, or have future borrowings available under our senior credit facility, to enable us to repay our indebtedness, including the Notes, or to fund other liquidity needs. As of December 29, 2013, we had approximately $160.5 million of total indebtedness outstanding (consisting of $150.0 million of Notes, $1.2 million of lease financing obligations and $9.3 million of capital leases and other debt) and $12.4 million of borrowing availability under our senior credit facility (after reserving $7.6 million for letters of credit issued under our senior credit facility), which would effectively rank senior to the Notes.

Our substantial indebtedness could have important consequences to our stockholders. For example, it could:

- make it more difficult for us to satisfy our obligations with respect to the Notes and our other debt;
- increase our vulnerability to general adverse economic and industry conditions;
- require us to dedicate a substantial portion of our cash flow from operations to payments on our indebtedness and related interest, including indebtedness we may incur in the future, thereby reducing the availability of our cash flow to fund working capital, capital expenditures (including restaurant remodeling obligations under the operating agreement) and other general corporate purposes;
- restrict our ability to acquire additional restaurants;
- limit our flexibility in planning for, or reacting to, changes in our business and the industry in which we operate;
- increase our cost of borrowing;
- place us at a competitive disadvantage compared to our competitors that may have less debt; and
- limit our ability to obtain additional financing for working capital, capital expenditures, acquisitions, debt service requirements or general corporate purposes.

We expect to use cash flow from operations to meet our current and future financial obligations, including funding our operations, debt service and capital expenditures. Our ability to make these payments depends on our future performance, which will be affected by financial, business, economic and other factors, many of which we cannot control. Our business may not generate sufficient cash flow from operations in the future, which could result in our being unable to repay indebtedness, or to fund other liquidity needs. If we do not have enough money, we may be forced to reduce or delay our business activities and capital expenditures (including our restaurant remodeling obligations under the operating agreement), sell assets, obtain additional debt or equity capital or restructure or refinance all or a portion of our debt, including our senior credit facility and the Notes, on or before maturity. We cannot make any assurances that we will be able to accomplish any of these alternatives on terms acceptable to us, or at all. In addition, the terms of existing or future indebtedness, including the agreements for our senior credit facility, may limit our ability to pursue any of these alternatives.

Despite current indebtedness levels and restrictive covenants, we may still be able to incur more debt or make certain restricted payments, which could further exacerbate the risks described above.

We and our subsidiaries may be able to incur additional debt in the future, including debt that may be secured on a first lien basis or pari passu with the Notes. Although our senior credit facility and the indenture governing the Notes contains restrictions on our ability to incur indebtedness, those restrictions are subject to a number of exceptions. In addition, if we are able to designate some of our restricted subsidiaries under the indenture governing the Notes as unrestricted subsidiaries, those unrestricted subsidiaries would be permitted to borrow beyond the limitations specified in the indenture governing the Notes and engage in other activities in which restricted subsidiaries may not engage. We may also consider investments in joint ventures or acquisitions, which may increase our indebtedness. Moreover, although our senior credit facility and the indenture governing the Notes contains restrictions on our ability to make restricted payments, including the declaration and payment of dividends, we are able to make such restricted payments under certain circumstances. Adding new debt to current debt levels or making restricted payments could intensify the related risks that we and our subsidiaries now face.

The agreements governing our debt agreements restrict our ability to engage in some business and financial transactions and contain certain other restrictive terms.

Our debt agreements, such as the indenture governing the notes and the agreement governing our senior credit facility, restrict our ability in certain circumstances to, among other things:

- incur additional debt;

- pay dividends and make other distributions on, redeem or repurchase, capital stock;
- make investments or other restricted payments;
- enter into transactions with affiliates;
- engage in sale and leaseback transactions;
- sell all, or substantially all, of our assets;
- create liens on assets to secure debt; or
- effect a consolidation or merger.

Additionally, our senior credit facility requires cash collateralization of $20.0 million, the entire amount committed under the facility, whether drawn or undrawn, until such time as our lease adjusted leverage ratio (as defined in the senior credit facility) is less than 6.00x for two consecutive fiscal quarters.

These covenants limit our operational flexibility and could prevent us from taking advantage of business opportunities as they arise, growing our business or competing effectively. In addition, our senior credit facility requires us to maintain specified financial ratios and satisfy other financial condition tests, although we are not required to be in compliance with such ratios as long as the senior credit facility is cash collateralized. Our ability to meet these financial ratios and tests can be affected by events beyond our control, and we cannot assure you that we will meet these tests.

A breach of any of these covenants or other provisions in our debt agreements could result in an event of default, which if not cured or waived, could result in such debt becoming immediately due and payable. This, in turn, could cause our other debt to become due and payable as a result of cross-acceleration provisions contained in the agreements governing such other debt. In the event that some or all of our debt is accelerated and becomes immediately due and payable, we may not have the funds to repay, or the ability to refinance, such debt. In addition, in the event that the Notes become immediately due and payable, the holders of the Notes would not be entitled to receive any payment in respect of the notes until all of our senior debt has been paid in full.

We may not have the funds necessary to satisfy all of our obligations under our senior credit facility, the Notes or other indebtedness in connection with certain change of control events.

Upon the occurrence of specific kinds of change of control events, the indenture governing the Notes requires us to make an offer to repurchase all outstanding Notes at 101% of the principal amount thereof, plus accrued and unpaid interest (and additional interest, if any) to the date of repurchase. However, it is possible that we will not have sufficient funds, or the ability to raise sufficient funds, at the time of the change of control to make the required repurchase of the Notes. In addition, restrictions under our senior credit facility may not allow us to repurchase the Notes upon a change of control. If we could not refinance such debt or otherwise obtain a waiver from the holders of such debt, we would be prohibited from repurchasing the Notes, which would constitute an event of default under the indenture. Certain important corporate events, such as leveraged recapitalizations that would increase the level of our indebtedness, would not constitute a “Change of Control” under the indenture.

In addition, our senior credit facility provides that certain change of control events constitute an event of default under such senior credit facility. Such an event of default entitles the lenders thereunder to, among other things, cause all outstanding debt obligations under the senior credit facility to become due and payable and to proceed against the collateral securing such senior credit facility. Any event of default or acceleration of the senior credit facility will likely also cause a default under the terms of our other indebtedness.

ITEM 1B. UNRESOLVED STAFF COMMENTS

None.

ITEM 2. PROPERTIES

As of December 29, 2013, we owned eight and leased 556 Burger King restaurant properties including six restaurants located in mall shopping centers, two restaurants located on military bases and twenty-two co-branded locations.

We typically enter into leases (including renewal options) ranging from 20 to 40 years. The average remaining term for all leases, including options, was approximately 20.5 years at December 29, 2013. Generally, we have been able to renew leases, upon or prior to their expiration, at the prevailing market rates, although there can be no assurance that this will continue to occur.

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Most of our Burger King restaurant leases are coterminous with the related franchise agreements. We believe that we generally will be able to renew at commercially reasonable rates the leases whose terms expire prior to the expiration of that location's Burger King franchise agreement, although there can be no assurance that this will occur.

Most leases require us to pay utility and water charges and real estate taxes. Certain leases also require contingent rentals based upon a percentage of gross sales of the particular restaurant that exceed specified minimums. In some of our mall locations, we are also required to pay certain other charges such as a pro rata share of the mall's common area maintenance costs, insurance and security costs.

In addition to the restaurant locations set forth under Item 1. “Business-Restaurant Locations”, we own a building with approximately 25,300 square feet at 968 James Street, Syracuse, New York, which houses our executive offices and most of our administrative operations for our Burger King restaurants. We also lease seven small regional offices that support the management of our Burger King restaurants.

ITEM 3. LEGAL PROCEEDINGS

On August 21, 2012 Alan Vituli, our former chairman and chief executive officer, filed an action in the Superior Court of the State of Delaware against us and Carrols. On October 1, 2013 Mr. Vituli filed an amended and supplemental complaint (the "Amended Complaint") which, among other things, added Fiesta Restaurant Group, now an independent public company, but our indirect wholly-owned subsidiary for the time period at issue in the Amended Complaint, as a defendant. The Amended Complaint alleges, among other things, breach of Mr. Vituli's employment agreement with us, fraud, and fraudulent inducement in connection with Mr. Vituli’s departure as chief executive officer, chairman, and director of Carrols Restaurant Group and Carrols and as non-executive chairman and director of Fiesta Restaurant Group, that he was wrongfully deprived of observer rights on the board of directors of Carrols Restaurant Group after his departure from such board and that he was underpaid a portion of his bonus for fiscal 2011. The relief sought by Mr. Vituli includes damages of $3.55 million in the aggregate, unspecified consequential and punitive damages, attorney’s fees and costs and various requests for declaratory judgment. We believe that that all of the claims raised by Mr. Vituli are without merit. We will vigorously contest and defend against this action and Mr. Vituli’s claims.

We are a party to various other litigation matters incidental to the conduct of our business. We do not believe that the outcome of any of these other matters will have a material adverse effect on our consolidated financial statements.

ITEM 4. MINE SAFETY DISCLOSURES

None.

PART II

ITEM 5. MARKET FOR THE REGISTRANT'S COMMON EQUITY, RELATED STOCKHOLDER MATTERS AND ISSUER PURCHASES OF EQUITY SECURITIES

Our common stock trades on The NASDAQ Global Market under the symbol “TAST”. On February 27, 2014, there were 23,711,096 shares of our common stock outstanding held by 765 holders of record. The number of record holders was determined from the records of our transfer agent and does not include beneficial owners of our common stock whose shares are held in the names of various securities brokers, dealers, and registered clearing agencies. The closing price of our common stock on February 27, 2014 was $6.52. The closing price of our common stock on May 7, 2012, the date of the spin-off, was $15.08. The closing price of our common stock on May 8, 2012, the date following the spin-off, was $4.44.

The following table sets forth the range of high and low closing prices of our common stock for the periods indicated, as reported by The NASDAQ Global Market and after May 7, 2012, reflects the spin-off of FIesta Restaurant Group:

	Common Stock Price (1)	
	High	Low
Year Ended December 29, 2013		
First Quarter	$6.40	$5.00
Second Quarter	6.64	4.71
Third Quarter	6.89	6.01
Fourth Quarter	6.70	5.34
Year Ended December 30, 2012		
First Quarter	$15.42	$11.02
Second Quarter	15.51	4.44
Third Quarter	6.17	5.18
Fourth Quarter	6.65	5.92

(1) Stock prices prior to the second quarter of 2012 were before the spin-off of Fiesta Restaurant Group, Inc.

Dividends

We did not pay any cash dividends during the fiscal years 2013 or 2012.We currently intend to continue to retain all available funds to fund the development and growth of our business and do not anticipate paying any cash dividends on our common stock in the foreseeable future. In addition, we are a holding company and conduct all of our operations through our direct and indirect subsidiaries. As a result, for us to pay dividends, we need to rely on dividends or distributions to us from Carrols and indirectly from subsidiaries of Carrols. The indenture governing the Notes and our senior credit facility limits, and debt instruments that we and our subsidiaries may enter into in the future may limit, our ability to pay dividends to our stockholders.

Stock Performance Graph

The following graph compares from December 31, 2008 the cumulative total stockholder return on our common stock over the cumulative total returns of The NASDAQ Composite Index and a peer group, The S&P SmallCap 600 Restaurants Index. We have elected to use the S&P SmallCap 600 Restaurant Index in compiling our stock performance graph because we believe the S&P SmallCap 600 Restaurant Index represents a comparison to competitors with similar market capitalization as us. The following graph is based on the closing price of our common stock from December 31, 2008 through December 31, 2013.

* $100 invested on 12/31/2008 in stock or index, including reinvestment of dividends.

	12/31/08	12/31/09	12/31/10	12/31/11	12/31/12	12/31/13
Carrols Restaurant Group, Inc.	$100.00	$261.85	$274.81	$428.52	$795.14	$878.91
NASDAQ Composite	$100.00	$144.84	$170.58	$171.34	$200.03	$283.43
S&P SmallCap 600 Restaurants	$100.00	$136.39	$185.18	$184.71	$221.49	$357.09

ITEM 6. SELECTED FINANCIAL DATA

The information in the following table should be read together with "Financial Statements and Supplementary Data," and “Management’s Discussion and Analysis of Financial Condition and Results of Operations” included elsewhere in this Form 10-K. Reported amounts below present the historical operating results and cash flows of Fiesta for periods prior to May 7, 2012 as discontinued operations. On May 30, 2012, we acquired 278 restaurants from BKC. The results of operations of the acquired BKC restaurants are included in our consolidated operating results from May 31, 2012, the day following the closing of the 2012 acquisition. These historical results are not necessarily indicative of the results to be expected in the future. Our fiscal years ended January 2, 2011, January 1, 2012, December 30, 2012 and December 29, 2013 each contained 52 weeks. Our fiscal year ended January 3, 2010 contained 53 weeks.

	Year Ended January 3, 2010	January 2, 2011	January 1, 2012	December 30, 2012	December 29, 2013
	(In thousands of dollars, except share and per share data)				
Statements of operations data:					
Restaurant sales	$384,020	$357,073	$347,518	$539,608	$663,483
Costs and expenses:					
Cost of sales	105,376	105,399	103,860	172,698	201,532
Restaurant wages and related expenses (1)	119,321	112,534	109,155	169,857	208,404
Restaurant rent expense	23,981	23,169	22,665	37,883	47,198
Other restaurant operating expenses (1)	57,377	54,602	53,389	88,883	106,508
Advertising expense	16,213	14,966	14,424	22,257	29,615
General and administrative (1)(2)	20,561	19,210	20,982	36,085	37,228
Depreciation and amortization	14,714	15,354	16,058	26,321	33,594
Impairment and other lease charges	487	709	1,293	977	4,462
Other expense (income) (3)	79	(444)	(720)	(717)	17
Total operating expenses	358,109	345,499	341,106	554,244	668,558
Income (loss) from operations	25,911	11,574	6,412	(14,636)	(5,075)
Interest expense	8,907	8,957	7,353	12,764	18,841
Loss on extinguishment of debt	—	—	1,244	1,509	—
Income (loss) from continuing operations before income taxes	17,004	2,617	(2,185)	(28,909)	(23,916)
Provision (benefit) for income taxes	5,930	807	(1,661)	(10,093)	(10,397)
Net income (loss) from continuing operations	11,074	1,810	(524)	(18,816)	(13,519)
Income (loss) from discontinued operations, net of income taxes	10,761	10,106	11,742	(72)	—
Net income (loss)	$21,835	$11,916	$11,218	$(18,888)	$(13,519)
Per share data:					
Basic net income (loss) per share:					
Continuing operations	$0.51	$0.08	$(0.02)	$(0.83)	$(0.59)
Discontinued operations	$0.50	$0.47	$0.54	$—	$—
Diluted net income (loss) per share:					
Continuing operations	$0.51	$0.08	$(0.02)	$(0.83)	$(0.59)
Discontinued operations	$0.49	$0.46	$0.54	$—	$—
Weighted average shares used in computing net income (loss) per share:					
Basic	21,594,366	21,620,550	21,677,837	22,580,468	22,958,963
Diluted	21,768,683	21,835,417	21,677,837	22,580,468	22,958,963

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	Year Ended January 3, 2010	January 2, 2011	January 1, 2012	December 30, 2012	December 29, 2013
	(In thousands of dollars, except restaurant weekly sales data)				
Other financial data:					
Net cash provided from operating activities	$46,409	$32,260	$33,448	$18,207	$21,581
Total capital expenditures	20,817	13,649	27,771	37,642	50,486
Net cash used for investing activities	17,459	12,626	25,961	65,908	50,486
Net cash provided from (used for) financing activities	(29,276)	(19,621)	2,943	69,301	(1,083)
Operating Data:					
Restaurants (at end of period)	312	305	298	572	564
Average number of restaurants	313.2	307.3	301.2	457.0	563.8
Average annual sales per restaurant (4)	1,226,117	1,161,969	1,153,778	1,180,761	1,176,806
Adjusted EBITDA (5)	41,980	28,537	25,448	24,972	34,271
Adjusted Restaurant-Level EBITDA (5)	61,752	46,403	44,025	52,415	70,226
Change in comparable restaurant sales (6)	(2.6)%	(4.3)%	(1.4)%	7.1 %	1.0 %
Balance sheet data (at end of period):					
Total assets	$439,977	$426,302	$458,392	$346,256	$329,481
Working capital	(40,170)	(39,646)	(11,620)	7,478	(21,974)
Debt:					
Senior and senior subordinated debt	271,900	252,250	267,375	150,000	150,000
Capital leases	1,193	1,202	1,144	10,295	9,336
Lease financing obligations	9,999	10,061	10,064	1,197	1,200
Total debt	$283,092	$263,513	$278,583	$161,492	$160,536
Stockholders' equity	$31,404	$44,907			