Great Cups of Coffee Company

Great Coffee at a Great Price

Financial Statements and Supplementary Data

Note: The financial notes were created to simulate current financial practices by a business. Typically financial notes are similar in appearance due to the standards in accounting. The financial notes for Great Cups of Coffee Company were adapted from the financial statements on the SEC web site for Starbucks and Caribou Coffee. These documents are public domain.

Great Cups of Coffee Company, Inc.

Statement of Earnings
(In thousands)

	2013	**2012**
Company-Operated Retail	187,000	182,360
Other Sales –Commercial Volume	12,965	11,608
Other Sales –e Marketing	35	32
Total Net Sales	**200,000**	**194,000**
Total Cost of Sales and related occupancy costs	88,078	83,420
Gross Margin	111,922	110,580
Total Operating Expenses	83,916	69,840
EBITDA	**28,006**	**28,924**
Depreciation and Amortization	13,524	15,436
Earnings from Operations	**14,482**	**13,488**
Interest Income	860	649
Interest Expense	5,606	6,575
Earnings Before Income Taxes (EBIT)	**9,736**	**7,562**
Income Taxes	3,502	3,636
Net Income	**6,234**	**3,926**

Great Cups of Coffee, Inc.

Balance Sheet
(In thousands)

Assets	**2013**	**2012**
Cash and cash equivalents	7,074	5,833
Accounts receivable	3,820	3,520
Allowance for Doubtful Accounts	(20)	(20)
Net Accounts Receivable	3,800	3,500
Inventory	22,887	20,380
Other Current Assets	8,250	7,100
Current Assets	**42,011**	**36,813**
Property, Plant, and Equipment	140,816	140,816
Less Depreciation	32,160	18,636
Property, Plant, and Equipment, net	**108,656**	**122,180**
L-T Investments	10,500	8,500
Intangible Assets	0	0
Other L-T Assets	15,213	17,720
Total Assets	**176,380**	**185,213**

Liabilities & Equity

Accounts payable	7,724	7,341
LOC Payable	8,600	9,500
Other Current Liabilities	0	0
Accrued Liabilities	5,123	4,673
Current Maturities Long Term Debt	15,000	15,000
Total Current Liabilities	**36,447**	**36,514**
Long-Term Debt - Bank	30,000	40,000
Long-Term Notes Payable - Former Owners Chicago	40,000	45,000
Total Liabilities	**106,447**	**121,514**
Shareholders' Equity		
Common Stock, par value $0.01 per share, 20,000,000 authorized; 5,000,000 issued and outstanding on December 31, 2007	50	50
Additional Paid-In Capital	4,950	4,950
Retained Earnings	64,933	58,699
Total Shareholders' Equity	**69,933**	**63,699**
Total Liabilities & Shareholders' Equity	**176,380**	**185,213**

Statement of Cash Flows
(In thousands)

	2013	2012
Cash Flows From Operating Activities		
Net Income	6,284	3,926
Depreciation	13,524	15,436
(Increase) decrease in Inventory	(2,507)	(13,500)
(Increase) in Accounts Receivable	(300)	(1,700)
(Increase) decrease in Other Current Assets	(1,150)	(100)
(Increase) decrease in Other Long Term Assets	2,507	(5,350)
Increase (decrease) in Accounts Payable	383	4,091
Increase (decrease) in Accrued Liabilities	450	2,646
Net Cash Provided by Operating Activities	**19,141**	**5,449**
Cash Flows from Investing activities		
(Increase) decrease in Property, Plant, Equipment	(105,616)	(72,616)
(Increase) decrease in LT Investments	(2,000)	4,000
(Increase) decrease in Intangible Assets	0	(33,000)
Net cash flows from investing activities	**(2,000)**	**(101,616)**
Cash Flows from Financing activities		
Increase (decrease) in LOC Payable	(900)	900
Increase (decrease) Current Maturities Long Term Debt	0	9,500
Increase (decrease)in Loan Payable Bank	(5,000)	40,000
Increase (decrease) in LT Notes Payable Former Owners	(10,000)	45,000
Net cash flows from financing activities	**(15,900)**	**95,400**
Net (decrease) increase in cash and cash equivalents	**1,241**	**(767)**
Beginning Cash	**5,833**	**6,600**
Ending Cash	**7,074**	**5,833**

GREAT CUPS COFFEE COMPANY, INC.

NOTES TO FINANCIAL STATEMENTS

1. Summary of Significant Accounting Policies

Description of Business

Great Cups Coffee Company, Inc. is a specialty retailer of high-quality premium coffee and espresso-based beverages, foods, ice cream and coffee lifestyle items. As of December 31, 2013, the Company had 270 coffeehouses serving coffee, ice cream, and deli items located in Ohio, Chicago, and Pittsburgh

In these notes Great Cups of Coffee Company, Inc. is referred to as the "Company," "we," "us" or "our".

Use of Estimates

The preparation of financial statements in conformity with accounting principles generally accepted in the U.S. ("GAAP") requires management to make estimates and assumptions that affect reported amounts of assets, liabilities, revenues, and expenses. Actual results and outcomes may differ from these estimates, and such differences may be material to the year-end financial statements.

Fiscal Year End

The Company's fiscal year ends on December 31.

Cash and Cash Equivalents

All highly liquid investments with a maturity of three months or less at the time of purchased are considered cash equivalents.

Fair Value of Financial Instruments

The carrying values of the Company's financial instruments, which include cash and cash equivalents, approximate fair value. The Company places its cash with FDIC-insured financial institutions.

Allowance for Doubtful Accounts

Allowance for doubtful accounts is calculated based on historical experience, customer credit risk and identification of specific accounts at risk. The allowance for doubtful accounts for the years December 31, 2013 and December 31, 2012 is $20,000 and $20,000, respectively.

Inventories

Inventories are stated at the lower of cost (primarily weighted average) or market.

Property, Plant and Equipment

Property, plant and equipment are carried at cost less accumulated depreciation. Depreciation of property, plant and equipment is computed using the straight-line method over estimated useful lives, generally ranging from two to 20 years.

Deferred Financing Fees

The Company capitalized the costs incurred in acquiring its revolving credit facility and included the costs as a component of other assets. The costs are being amortized over the life of the agreement on a straight-line basis.

Impairment of Long-Lived Assets and Long-Lived Assets to Be Disposed Of

The Company reviews long-lived assets and certain identifiable intangibles for impairment whenever events or changes in circumstances indicate that the carrying amount of an asset may not be recoverable. Recoverability of assets to be held and used is measured by a comparison of the carrying amount of an asset to future undiscounted net cash flows expected to be generated by the asset. If such assets are considered to be impaired, the impairment to be recognized is measured by the amount by which the carrying amount of the assets exceeds the fair value of the assets. Assets to be disposed of are reported at the lower of the carrying amount or fair value less estimated costs to sell.

Coffeehouse Preopening and Closing Expenses

Costs incurred in connection with start-up and promotion of new coffeehouse openings are expensed as incurred. When a coffeehouse is closed, the remaining carrying amount of property and equipment, net of expected recovery value, is charged to operations. For coffeehouses under operating lease agreements, the estimated liability under the lease is also accrued.

Revenue Recognition

The Company recognizes retail coffeehouse sales for products and services when payment is tendered at the point of sale. Sales tax collected from customers is presented net of amounts expected to be remitted to various tax jurisdictions. Accordingly, sales taxes have no effect on the Company's reported net sales in the accompanying statements of operations.

Revenue from the sale of products to commercial customers is recognized when ownership and price risk of the products is legally transferred to the customer, which is generally upon the shipment of goods. Revenue includes any applicable shipping and handling costs invoiced to the customer, and the expense of such shipping and handling costs is included in cost of sales.

Advertising

The Company expenses advertising costs as incurred. Production costs for radio and television advertising are expensed when the commercials are initially aired. Advertising expenses aggregated approximately $1.6 million and $1.6 million for the years ended December 31, 2013 and December 31, 2012.

Operating Leases and Rent Expense

Certain of the Company's lease agreements provide for scheduled rent increases during the lease term or for rental payments commencing at a date other than the date of initial occupancy. Rent expense is recorded on a straight-line basis over the initial lease term and renewal periods that are reasonably assured. The difference between rent expense and rent paid is recorded as deferred rent and is included in "accrued expenses" and "deferred rent liability" in the consolidated balance sheets. Contingent rents, including those based on a percentage of retail sales over stated levels, and rental payment increases based on a contingent future event are accrued over the respective contingency periods when the achievement of such targets or events are deemed to be probable by the Company.

Income Taxes

The Company computes income taxes under the liability method. Under this method, deferred income tax assets and liabilities are determined based on differences between the financial reporting and tax basis of assets and liabilities and are measured using the enacted tax rates and laws that will be in effect when the differences are expected to reverse.

The Company recognizes the tax benefit from an uncertain tax position only if it is more likely than not that the tax position will be sustained on examination by the taxing authorities, based on the technical merits of the position. No portion of an uncertain tax position is recognized if the position has less than a 50% likelihood of being sustained.

2. Recent Accounting Pronouncements

In June 2011, the FASB issued guidance that revises the manner in which entities present comprehensive income in their financial statements. The guidance requires entities to report the components of comprehensive income in either a single, continuous statement or two separate but consecutive statements. The guidance became effective for the Company at the beginning of the first quarter of fiscal 2012. The adoption of this new guidance resulted in a change in how the Company presents the components of comprehensive income, which is currently presented within the consolidated statements of equity.

In May 2011, the FASB issued guidance to amend the fair value measurement and disclosure requirements. The guidance requires the disclosure of quantitative information about unobservable inputs used, a description of the valuation processes used, and a qualitative discussion around the sensitivity of the measurements. The guidance became effective for the Company at the beginning of its first quarter of fiscal Year 2012. The adoption of this new guidance did not have a material impact on the Company's financial statements.

3. Inventories

Inventories consist of the following (in thousands):

	December 31, 2013	December 1, 2012
Coffee	15,923	$ 13,209
Merchandise held for sale	4,420	4,015
Supplies	2,544	3,036
	$22,887	$ 20,380

4. Property, Plant and Equipment

Property, plant and equipment consist of the following (in thousands):

	December 31, 2013	December 31, 2012
Leasehold improvements	63,367	63,367
Furniture, fixtures, and equipment	77,449	77,449
	140,816	140,816
Less accumulated depreciation and amortization	(32,160)	(18,636)
	108,656	122,180

5. Credit Facilities

Revolving Credit Facility

The company maintains an unsecured, committed, 1-year term revolving line of credit totaling $10 million from a commercial bank. Borrowings under the facility are priced at three-month LIBOR + 2% p.a. At the end of 2013 total outstandings under the facility were $8.6 million, with $8.6 million classified as Line Of Credit Payable. The commitment fee on the facility is 0.25% p.a. on any unused portion. The facility is renewed annually on January 1 for an additional one year to maintain a 1-year term. Loan covenants require the following:

A current ratio of not less than 2 to 1

Long-term Debt

In 2010 the Company borrowed from a commercial bank a secured term loan totaling $50 million to finance, in part, the acquisition of the Chicago stores. This 5-year term loan is secured by the firm's tangible long-term assets. Scheduled payments and amortization begin at the end of year 8 with principal payments at 5 million per annum. The interest rate on the facility is six-month LIBOR + 1.75% p.a. and is re-priced each year in January and July. There are no prepayment penalties on this facility. At December 31, 2012 the note had a balance $35 million, with $5 million classified in CMLTD and $30 million classified in "Long Term Debt-Bank". Covenants for the loan require a fixed charge coverage ratio of 1.50:1

In 2010 the company also issued a ten-year, secured $50 million term note to the sellers of the Chicago stores scheduled to be amortized over its life with principal repayments of $5 million per annum. The interest rate on this note was fixed in 2008 at the inception of the loan at 5.5% p.a. At December 31, 2012 total outstanding under the facility were $45 million, with $5 million classified as CMLTD and $40 million classified under "L-T Notes Payable-Former Owners Chicago." The security on the LT note involves a second position on the firm's tangible long-term assets. There are no covenants on this debt, but payments affect the fixed charge coverage ratio.

6. Leases

The Company leases retail coffeehouses, roasting, distribution facilities, and office space under operating leases expiring through March 2023. Most lease agreements contain renewal options and rent escalation clauses. Certain leases provide for contingent rentals based upon gross sales.

Rental expense under these lease agreements, excluding real estate taxes, common area charges and insurance, was as follows (in thousands):

	Years Ended	
	December 31, 2013	December 31, 2012

Minimum future rental payments under these agreements as of January 1, 2014, are as follows (in thousands):

2014	$ 4,472
2015	4,475
2016	4,475
2017	4,480
2018	4,482

7. Net Income Per Share

Basic net income attributable to Great Cups Coffee Company, Inc. common shareholders per share for years ended December 31, 2013 and December 31, 2012 were as follows (in thousands, except per share data):

	December 31, 2013	December 31, 2012

Common outstanding — basic	5,000	5,000
Basic net income per share	$ 1.25	$ 0.78

8. Commitments and Contingencies

From time to time, the Company is party to certain legal proceedings in the ordinary course of business. The Company does not believe that any legal proceedings to which it is currently a party will have a material adverse effect on its financial position or results of operations.

9. Segment Reporting

Segment information is prepared on the same basis that our management reviews financial information for decision making purposes. We have two reportable operating segments: retail and commercial. “Unallocated corporate” includes expenses pertaining to corporate administrative functions that support the operating segments but are not specifically attributable to or managed by any segment and are not included in the reported financial results of the operating segments. All of the segment sales are from external customers.

Retail

The Company’s retail segment represented 93.5% and 94% of total net sales for fiscal years 2013 and 2012, respectively. The retail segment operated 270 company-operated coffeehouses, ice cream stores, combo-marts, and delis located in Ohio, Illinois, and Pittsburgh.

	Ohio	Chicago	Pittsburgh
Stores	122	42	43
Combo-Marts	0	17	35

Delis	0	11	0
Total	122	70	78

Commercial

The Company's commercial segment represented 6.5% and 6% of total net sales for fiscal year 2013 and 2012, respectively. The commercial segment sells high-quality premium whole bean and ground coffee to grocery stores, office coffee and foodservice providers, hotels, and entertainment venues.

The table below presents an analysis of information by operating segment for the fiscal year 2013 (in thousands):

	Ohio	Pittsburgh	Chicago
Net Revenues			
Company Operated Retail	121,550	41,140	24,310
Other Sales –Commercial	7,410	3,502	2,088
Cost of Goods Sold – Retail	53,243	18,030	10,639
Cost of Goods Sold –Other Commercial	3,515	1,665	986
Total Cost of Goods Sold	56,758	19,695	11,625
Total Gross Margin	72,202	24,947	14,773
Commercial – Volume Sales	7,395	3,492	2,078
Commercial – e Marketing Sales	15	10	10
Cost of Goods Sold – Commercial Volume Customers	3508	1660	981
Cost of Goods Sold e-marketing	7	5	5
Gross Margin Retail	68,307	23,110	13,671
Gross Margin Commercial Volume	3,887	1,832	1,097
Gross Margin e Marketing Sales	8	5	5

Total Gross Margin Sales	72,202	24,947	14,773