SONIC
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SONIC
2020
in sight
2016 Annual Report

Seeing the Future of Sonic

As Sonic moves toward the end of the decade, with targeted milestones in terms of both average drive-in sales and profitability, a new vision for what the 2020 drive-in might look like – and how it will relate to emerging consumer trends – continues to come into focus. Part evolution, part revolution, a fusion of new technology with Sonic's drive-in delivery system and Carhop service, together with our unique all-day menu, positions us as one of the most highly differentiated concepts in the quick-service restaurant (QSR) industry. More important, it enables Sonic to build on its established service advantages as it continues to transform the future of the drive-in.

+31

The net growth in total drive-ins during the past year – the strongest pace in seven years.

+2.6%

The increase in system same-store sales for fiscal 2016 – the sixth consecutive year of positive same-store sales.

3,557

Locations Coast-to-Coast

90%

Franchise Drive-Ins

Founded in 1953 in Shawnee, Oklahoma, Sonic today franchises and operates the largest chain of drive-in restaurants in the country, with more than 3,500 Sonic Drive-Ins from coast to coast.

Unique, signature menu items are made when you order and include chicken sandwiches, popcorn chicken and chicken strips, footlong quarter pound coneys and six-inch premium beef hot dogs along with a full line-up of 100% pure beef hamburgers and cheeseburgers. Likewise, we are famous for our hand-made onion rings, tater tots and over a million drink choices, including our legendary Cherry Limeade. Customers also enjoy drive-thru service and patio dining at many Sonic locations.

To Our Shareholders

The past year represented some of our strongest sales performance, tracked on a monthly basis, and at the same time some of the most challenging customer characteristics since the Great Recession. That dichotomy virtually defined the two halves of fiscal year 2016.

Before proceeding though, let me offer a financial overview of the past year. Adjusted earnings for the year rose 17% to $1.29 per diluted share as free cash flow grew to $66 million. We prudently allocated this cash flow via strategies that help build our brand and our business, as well as rewarded shareholders for their confidence and loyalty. We again returned a significant amount of cash to shareholders in the form of share repurchases and dividends, which together totaled nearly $170 million during the year and represented an increase of 18% compared with the prior year.

+3.2%

The increase in average drive-in volume for fiscal 2016, reaching $1,284,000.

In fiscal 2017, we expect to increase shareholder returns again, including an anticipated increase in the quarterly cash dividend of 27%. From a capital structure perspective, we issued $425 million in fixed-rate securitized notes in fiscal year 2016, the proceeds of which were used to retire and refinance previous debt as well as fund further investment in the business and additional capital return to shareholders via share repurchase and dividends.

+17%

The increase in adjusted net income per diluted share for fiscal 2016, which rose to $1.29.

Despite the industrywide weakening in consumer sentiment and increasing competitive and promotional challenges during the last half of fiscal 2016, the long-term goals we established years ago are now within our reach. Our vision for Sonic's "2020 Drive-In" moves into greater clarity as we continue our march forward toward completion. We measure that journey by progress toward our drive-in performance goals. These include hitting an average unit volume of $1.5 million and an average unit profit of $200 thousand. With fiscal 2016 in the record book, we are approximately 86% and 72%, respectively, of the way toward our goals. Now, just four years out, our quest is not only in sight, our objectives are within reach.

Considering our strengthening sales over the past six years, coupled with rising average unit volumes and profits, it's understandable that our operators have had a growing appetite for expansion and new drive-in development. Development, as you know, is one of the layers of our multi-layered growth strategy; the 53 new drive-in openings during the past year were the strongest since fiscal 2010, resulting in net system growth for the second consecutive year.

Highlights of this past year's development activity include the opening of our first drive-in in Rhode Island – our 45th state, and ongoing expansion in California. During the past year, we also signed a franchisee to begin developing drive-ins in Hawaii during fiscal 2018, which will take us to our 46th state and mark our

2/3

The portion of our chain that we have upgraded with the rollout of our proprietary POPS digital menu boards.

45

The number of states where Sonic Drive-Ins are located, following our entry into in Rhode Island this past year.

first-ever offshore expansion. The pipeline for new drive-ins is strong and is approaching the level necessary to provide annual net unit growth of 2% to 3% in the coming years.

In fiscal 2016, we announced our intention to pull another strategic lever that will enhance our company's return on assets over the long term. For the past several years, franchised drive-ins have comprised almost 90% of our chain, with the remaining company-owned drive-ins functioning as a proving ground for new ideas that ensure only best practices and resources are rolled out to the entire chain.

Looking ahead, we believe we can accomplish these objectives even more efficiently with a smaller base of company-owned drive-ins, so we have begun to refranchise company-owned drive-ins to increase our total franchised base toward approximately 95% of the system by the end of fiscal 2017. We believe this initiative will improve the capital efficiency of the company and allow our franchisees to optimize performance of the refranchised drive-ins and commit to additional new store development, thus, expanding the reach of our brand.

On the technology front, we continued to phase in our Point of Personalized Service (POPS) digital menu boards during the past year – now in year three of a four-year rollout. At the close of fiscal 2016, approximately two-thirds of our system has this modernized customer interface, which will enable our Integrated Customer Engagement (ICE) strategy, transforming the way orders are placed and paid for and the customer experience in our drive-in stalls. Interactive and customer-driven, POPS elevates the ordering interchange, giving customers even more control over the pace and suggesting add-on products based on their choices. More importantly, POPS forms a hub for future technological leaps as Sonic continues to embrace mobile interaction with customers.

Extending a commitment that has underpinned our business for several years now regarding high quality ingredients and diverse, differentiated menu choices, we've had another busy year innovating new favorites for our

customers. Building on the premium side of our menu, we recently turned up the heat with our new Fiery Ultimate Chicken Sandwich and Fiery Cheeseburger. As the Ultimate Drink Stop®, our beverage lineup enjoyed the addition of our Frozen Teas and, capitalizing on the unmistakable flavor of real ice cream, our new entries into the treat category included Sweet & Salty Master Blasts and Creamery Shakes.

Of course, recognizing the continual ebb and flow between premium and value selections, we have also focused on product introductions intended to drive traffic across all dayparts. These steps evolved rapidly in April and May and have provided us with attractive and effective choices to meet the cravings of a value-oriented customer. In many ways, this was the dominant theme of the last five months of the fiscal year, and we are glad to see signs of improvement this fall from those initiatives!

During the past year, the benefits of our bench strength have come home to roost, with Claudia San Pedro, our Executive Vice President and Chief Financial Officer, celebrating her 10th anniversary with our company after moving into the CFO role in fiscal 2015. In January 2016, we added the role of President to Todd Smith, our Chief Marketing Officer. His skills in advertising, digital consumer communications, product innovation, customer insights and customer relationship management all play toward our increasing emphasis on technology. Also, John Budd was promoted to Executive Vice President and Chief Development and Strategy Officer, recognizing his leadership efforts with respect to in-store retail technologies and supply chain initiatives.

$170M

The combined amount in dollars returned to shareholders through Sonic's stock repurchases and cash dividends, up from $143 million during fiscal 2015.

On the Board, R. Neal Black, formerly Chief Executive Officer and President of Jos. A. Bank Clothiers, Inc., was elected as a director in January 2016. He filled the position formerly held by Robert M. Rosenberg, who, after 22 years of service, retired from our Board. We welcome Neal and the unique expertise and perspective he brings to the Board, and we congratulate Bob for his tireless work on behalf of Sonic since 1993!

In closing, I believe Sonic continued to make meaningful strides as a brand during the past year, and the future of our business is coming increasingly into focus. As mentioned earlier, our multi-layered growth strategies – designed to increase same-store sales, enhance operating leverage, create momentum in new drive-in development, capitalize on our unique ascending royalty rate and deploy free cash flow to grow our brand and enhance shareholder value – continue to align and gain traction in synergistic ways. As we move ahead, building a platform for an unmatched customer experience in a digital world, we recognize fiscal 2016 was neither the beginning of this process, nor the end, but a significant and satisfying waypoint on a destination toward the 2020 Drive-In. From my perspective, the view ahead is pretty amazing.

Sincerely,

Clifford Hudson
Chairman and Chief Executive Officer

Always first in line.
Then. Now. And in the future.

So how does new technology play with the Sonic format? Actually, the drive-in is uniquely positioned for one-on-one communication in a digital world.

For more than 60 years, Sonic has capitalized on mobility that began with America's newfound romance with the automobile and the open road following World War II. For all those years, Sonic's drive-in model, together with signature Carhop service, has put customers first in line. As fast-food customers, especially millennials, become more mobile, our drive-in concept – with its multiple drive-in stall format – becomes even more relevant.

With mobile ordering on the horizon, important service advantages such as personalization and customization are already embedded in Sonic's DNA. For most competitors, bottlenecks arise when customers using mobile ordering are ready to take delivery of their food. Those customers face an unexpected choice: park, enter and stand in line with other customers who are still making up their minds about what to order, or do the same at the drive-thru. For the competition, those are likely to be the only delivery points, defeating the goal of increased speed and convenience for the mobile customer.

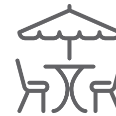
At Sonic, however, we can extend the power of first-in-line service to all customers, regardless of where their orders were placed, because our drive-in concept offers multiple points of delivery with multiple parking stalls and fast Carhop service. With an operational foundation well suited for a mobile world, we continue to build a customer experience unlike any other in QSR.

SONIC ENGAGES CUSTOMERS LIKE NO OTHER

If you are looking for a unique dining experience, highlighted by classic Carhop service, in a place where you set the pace, you need look no further than Sonic.

In car

Drive-thru



Patio

Coming soon

Digital

MANY OF SONIC'S DRIVE-INS HAVE 24 OR MORE STALLS, A DRIVE-THRU WINDOW AND POPS MENU BOARDS ON THE PATIO

Our customers always have multiple choices to ensure they are first in line. We've catered to mobility from the beginning, making Sonic fast and convenient, and we are extending that legacy in new ways as we think about mobility in a digital world.

SONIC'S GOT IT OTHERS DON'T

HEADIN' OUT

The new Sonic app conveniently allows customers to browse our menu remotely and zero in on their favorite item for later in the day.

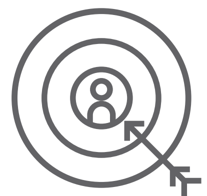
Built for a mobile world.

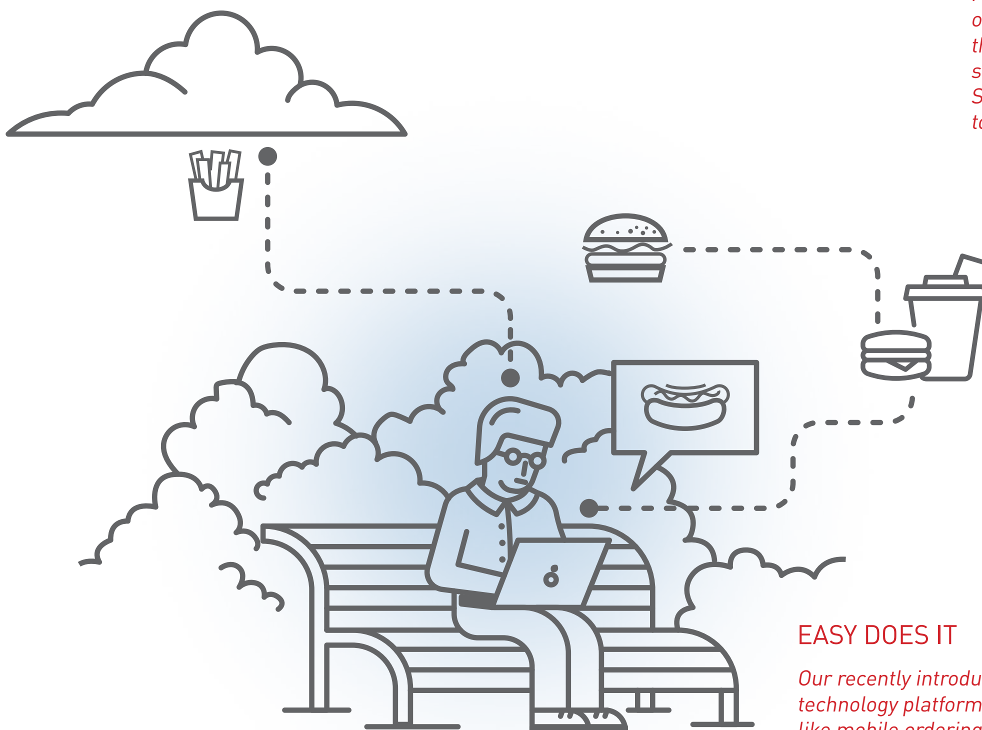
The emergence and convergence of new technology is changing the world, and with it, how restaurants interact with customers. Our technology initiatives capitalize on these trends with the rollout of our Point of Personalized Service, or POPS, which replaces static, audio-only menu boards at every drive-in stall, on the patio and at the drive-thru, with customized digital content on a touchscreen. POPS provides the hardware to support our Integrated Customer Experience, or ICE (think software), to deliver the Sonic Drive-In experience in a more interactive and engaging way. Currently, about two-thirds of the chain has been upgraded to the POPS platform, and full implementation is expected by the end of calendar 2017. This proprietary medium will allow us to deliver daypart specific content with smart upsells to every customer, with every order.

Our recently introduced Sonic mobile app was created to build on this platform, taking our drive-ins further on the path toward a digital world. While still in the early stages of its evolution, the app now allows customers to find locations, explore the menu and pay onsite. Next year, we expect to add additional new features to the app that include ordering and payment off premises, before arrival, to further unlock menu variety and customization for each order at Sonic. Sonic and our franchisees have provided additional resources for technology development, cybersecurity and an emerging Customer Relationship Management (CRM) program to reinforce our focus on the future and complement the strong national media spend that has made Sonic so successful.

BULLSEYE! SONIC'S TECHNOLOGY TARGETS MILLENNIALS

Millennials are perhaps the most mobile-oriented generation, spending more time on their smartphones than any other age group, so it makes sense to take the Sonic message directly to their devices.





EASY DOES IT

Our recently introduced mobile app builds on a strong technology platform and, with future enhancements like mobile ordering and offsite payment, it presents yet another easy way to get your Sonic on.

Pushing boundaries
with white space everywhere.

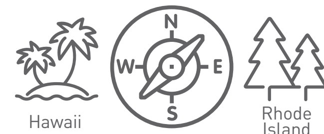
Sonic recaptured growth momentum during fiscal 2015. That resurgence became even more clear in fiscal 2016 as a total of 53 new drive-ins opened, resulting in net chain expansion of 31 for the year. The key driver for this growth – and the rising interest we've seen among franchisees in opening additional locations in new and existing markets – is a healthy return on investment with higher same-store sales, greater average unit volume and strong unit profitability. As entrepreneurs, our franchisees understand the compelling economic argument for further expansion, and many long-time operators recognize the potential of the Sonic brand through up and down markets.

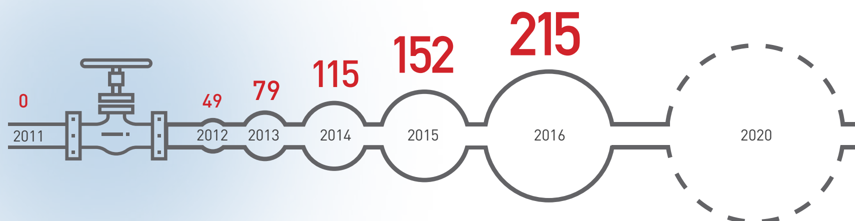
All of these positive factors have advanced over the course of the past five years, catching the attention of existing franchisees and those new to the brand. Underlying these attractive metrics, the increasing impact of our national advertising strategy continues to attract and excite customers in existing and future markets while efficiently delivering messaging that drives sales across multiple dayparts.

This progress, on so many fronts, explains why our development pipeline is at its strongest since before the Great Recession. It underscores our increasing national footprint – with recent expansion to Rhode Island, our 45th state, plans to enter Hawaii during fiscal 2018 and continued work across the country in every state. Vast stretches of the country remain ripe for ongoing development within and between existing markets as we deploy effective media strategies to bring Sonic to future fans across the USA.

FOOTPRINT EXPANDS TO 45 STATES IN 2016

Over the past 10 years, customers have enthusiastically welcomed Sonic to 13 new states, the most recent of which came this past year as we entered the state of Rhode Island. In fiscal 2018, we'll say Aloha to Hawaii!





INCREMENTAL NEW STORE COMMITMENTS ARE GROWING

The Sonic story resonates not only with customers, but also our franchisees. Coming out of the last recession in 2011, our development pipeline was empty. As we have continued to implement our multi-layered growth strategies, boosting average unit volumes and drive-in profitability, our pipeline has rebounded strongly.

COMPANY HEADING TO 95% FRANCHISE OWNED

Heavily involved with both menu innovation and expansion, our franchisees have in many ways mapped our plan for growth. Joyce Lunsford, with 10 drive-ins in Michigan, and Buddy McClain, a 30-year operator in three states and across many urban areas, reflect the diverse perspectives of our franchisees. Next year, we'll complete another round of refranchising, taking our franchise base closer to 95%.

PROMOTIONS DRIVE TRAFFIC AND OFFER INCREASED FLEXIBILITY

From the $5 Boom Box to Wing Night in America, with half-price boneless wings after 5 p.m., daypart-specific and value promotions provide flexibility to tailor offerings to meet customer tastes.

ICED COFFEE DRINKS BRIDGE DAYPARTS FOR MILLENNIALS

More and more, millennials prefer iced coffee to the hot version. Either way, Sonic has their coffee, along with about 1.3 million other drink combinations.

In a changing environment,

some things stay the same.

Down deep and underneath it all, everyone knows that consistently good-tasting food and drink, prepared with high-quality ingredients, is why restaurant customers return time after time. Selection, variety and customization also figure prominently in this decision.

Sonic scores on all counts, but doubles down with an all-day selection of everything on the menu and ups the ante with complete customization on anything we offer. Competitors try to imitate Sonic's all-day menu, mostly in a limited sense – and mainly as an extended breakfast menu – but they are still constrained in the choices they can offer, and good luck with getting what you want exactly the way you want it. Actually, there's no comparison. A SuperSONIC® Breakfast Burrito, extra cheese, extra sausage, at 9:00 pm? Done! A classic crispy chicken sandwich, with jalapenos and an OREO® Cheesecake Shake for breakfast? Ditto! Other places, not so much.

Sonic's menu is built around the finest quality items available, like all-white meat chicken breasts, premium beef hot dogs and 100% pure-beef hamburger patties. Interestingly, many favorites on Sonic's menu do double duty throughout the day, switch-hitting as lunchtime items at noon and snack choices later in the day. Beyond premium products, Sonic offers easy-price selections, like our 2016 limited-time offer $5 Boom Box, which included a choice of any premium beef 6-inch hot dog, a junior deluxe cheeseburger, medium tots or fries, and medium fountain drink. So, on whichever end of the spectrum you find yourself, now and in the future, you'll find yourself at Sonic.

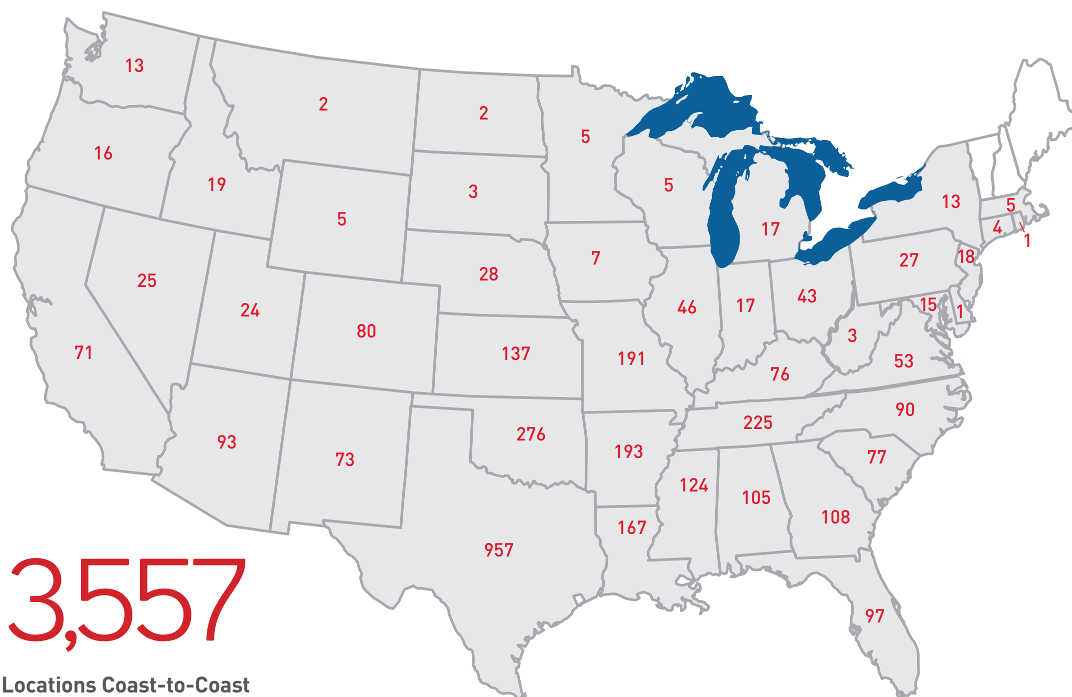
WACKY PACK STEALTHILY PROVIDES FUN WHILE ENLIGHTENING YOUNGER CUSTOMERS

Kids think it's just a fun meal with an interesting toy or game. Parents know that a learning opportunity comes on the side, engaging their child's mind in sensory and tactile ways.

CHICKEN SALES INCREASE, SOON TO OUTPACE HAMBURGER SALES

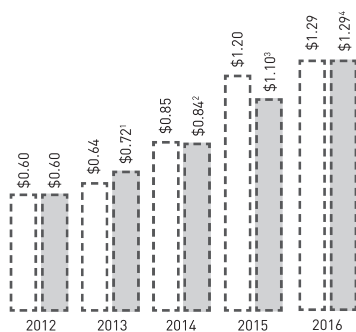
With tasty choices like the Ultimate Chicken Sandwich, it's no wonder that customers are choosing chicken more often. Already representing 10% of our total sales, we would not be surprised to see chicken sales double over the next five years.

Take a glance at Sonic



Net Income Per Diluted Share

Reported GAAP Adjusted Non-GAPP



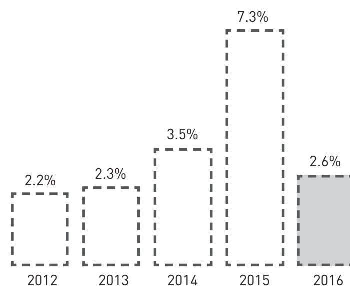
[1] Excludes $0.08, net, associated with early extinguishment of debt, a loss on closure of company drive-ins and an impairment charge for point-of-sale assets, all of which were partially offset by the benefit of a favorable resolution of tax matters.

[2] Excludes $0.01, reflecting a tax benefit from the acceptance by the IRS of a federal tax method change.

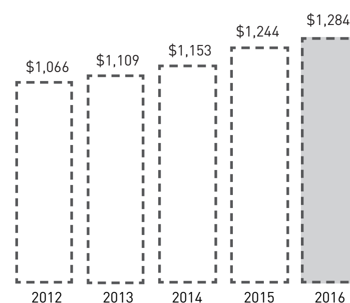
[3] Excludes $0.10, net, reflecting various changes in tax matters, including a benefit of prior-year statutory tax deduction and a change in the deferred tax valuation allowance.

[4] A number of reductions in Reported GAAP net income per diluted share totaling $0.19 per diluted share, including a release of income tax credits, the tax impact on debt extinguishment and gains on sales of Company drive-ins and real estate, were exactly offset by additions totaling $0.19 per diluted share, including a loss from early extinguishment of debt.

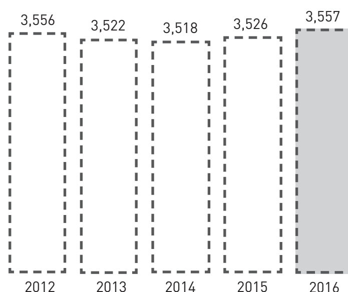
System-wide Same-store Sales



System-wide Drive-Ins Average Sales Per Drive-In (in thousands)



System-wide Drive-Ins



2016 Business Mix

90%
Franchised Drive-Ins

10%
Company Drive-Ins

Selected Financial Data

The following table sets forth selected financial data regarding the Company's financial condition and operating results. One should read the following information in conjunction with "Management's Discussion and Analysis of Financial Condition and Results of Operations" below and the Company's Consolidated Financial Statements included elsewhere in this report.

	Fiscal Year Ended August 31,				
(In thousands, except per share data)	**2016**	2015	2014	2013	2012
Income Statement Data:					
Company Drive-In sales	**$ 425,795**	$ 436,031	$ 405,363	$ 402,296	$ 404,443
Franchise Drive-Ins:					
Franchise royalties and fees	**170,319**	161,342	138,416	130,737	128,013
Lease revenue	**7,459**	5,583	4,291	4,785	6,575
Other	**2,747**	3,133	4,279	4,767	4,699
Total revenues	**606,320**	606,089	552,349	542,585	543,730
Cost of Company Drive-In sales	**356,820**	363,938	342,109	343,209	347,470
Selling, general and administrative	**82,089**	79,336	69,415	66,022	65,173
Depreciation and amortization	**44,418**	45,892	42,210	40,387	41,914
Provision for impairment of long-lived assets	**232**	1,440	114	1,776	764
Other operating (income) expense, net	**(4,691)**	(945)	(176)	1,943	(531)
Total expenses	**478,868**	489,661	453,672	453,337	454,790
Income from operations	**127,452**	116,428	98,677	89,248	88,940
Interest expense, net[(1)]	**34,948**	24,706	24,913	32,949	30,978
Income before income taxes	**92,504**	91,722	73,764	56,299	57,962
Net income-attributable to Sonic Corp.	**$ 64,067**	$ 64,485	$ 47,916	$ 36,701	$ 36,085
Income per share:					
Basic	**$ 1.32**	$ 1.23	$ 0.87	$ 0.65	$ 0.60
Diluted	**$ 1.29**	$ 1.20	$ 0.85	$ 0.64	$ 0.60
Weighted average shares used in calculation:					
Basic	**48,703**	52,572	55,164	56,384	60,078
Diluted	**49,669**	53,953	56,619	57,191	60,172
Cash dividends declared per common share[(2)]	**$ 0.44**	$ 0.27	$ 0.09	$ –	$ –
Balance Sheet Data:					
Working capital	**$ 62,994**	$ (2,383)	$ 16,201	$ 67,792	$ 26,635
Property, equipment and capital leases, net	**402,162**	421,406	441,969	399,661	443,008
Total assets	**659,995**	620,024	650,972	660,794	680,760
Obligations under capital leases (including current portion)	**21,064**	24,440	26,743	26,864	31,676
Long-term debt (including current portion)	**578,938**	438,028	437,318	447,294	481,793
Stockholders' equity (deficit)	**(75,643)**	17,433	62,675	77,464	59,247

(1) Includes net loss from early extinguishment of debt of $8.8 million and $4.4 million for fiscal years 2016 and 2013, respectively.

(2) The first quarter dividend for fiscal year 2015 was declared in the fourth quarter of fiscal year 2014.

Overview

Description of the Business. Sonic operates and franchises the largest chain of drive-in restaurants in the United States. As of August 31, 2016, the Sonic system was comprised of 3,557 drive-ins, of which 10% were Company Drive-Ins and 90% were Franchise Drive-Ins. As announced in the third quarter of fiscal year 2016, we plan to move toward an approximately 95% franchised system as part of a refranchising initiative. Sonic's signature food items include specialty drinks (such as cherry limeades and slushes), ice cream desserts, made-to-order chicken sandwiches and hamburgers, a variety of hot dogs including six-inch premium beef hot dogs and footlong quarter pound coneys, hand-made onion rings and tater tots. Sonic Drive-Ins also offer breakfast items that include a variety of breakfast burritos and serve the full menu all day. We derive our revenues primarily from Company Drive-In sales and royalties from franchisees. We also receive revenues from leasing real estate to franchisees, franchise fees, earnings from minority investments in franchise operations and other miscellaneous revenues.

Our Company Drive-In revenues and expenses are directly affected by the number and sales volumes of Company Drive-Ins. Our franchising revenues and other expenses such as depreciation, amortization and selling, general and administrative expenses are affected by the number and sales volumes of Franchise Drive-Ins. Lease revenues are generated primarily by the leasing of land and buildings for Company Drive-In operations that have been sold to franchisees.

Overview of Business Performance. System-wide same-store sales increased 2.6% during fiscal year 2016 as compared to an increase of 7.3% for fiscal year 2015. Same-store sales at Company Drive-Ins increased by 1.7% during fiscal year 2016 as compared to an increase of 6.9% for fiscal year 2015. Our continued positive same-store sales are a result of the successful implementation of initiatives, including product quality improvements and innovation, a greater emphasis on personalized service, new technology, a tiered pricing strategy and a media strategy, that have set a solid foundation for growth. All of these initiatives drive Sonic's multi-layered growth strategy, which incorporates same-store sales growth, operating leverage, deployment of cash, an ascending royalty rate and new drive-in development. Same-store sales growth is the most important layer and drives operating leverage and increased operating cash flows.

Revenues increased to $606.3 million for fiscal year 2016 from $606.1 million for fiscal year 2015, which was primarily due to an increase in Franchise Drive-In royalties of $9.9 million, partially offset by a decrease in Company Drive-In sales of $10.2 million. The decrease in Company Drive-In sales was a result of refranchising certain Company Drive-Ins, offset by an increase in sales from increased same-store sales. Restaurant margins at Company Drive-Ins were unfavorable by 30 basis points during fiscal year 2016, reflecting increased investments in employees' compensation and benefits to attract and retain employees at the drive-in level and the impact of the newly established Brand Technology Fund ("BTF"), partially offset by leverage from sales growth.

Net income and diluted earnings per share for fiscal year 2016 were $64.1 million and $1.29, respectively, as compared to net income of $64.5 million or $1.20 per diluted share for fiscal year 2015. Excluding the non GAAP adjustments further described below, net income per diluted share was $1.29 for fiscal year 2016, compared to $1.10 per diluted share in fiscal year 2015.

The following analysis of non-GAAP adjustments is intended to supplement the presentation of the Company's financial results in accordance with GAAP. We believe the exclusion of these items in evaluating the change in net income and diluted earnings per share for the periods below provides useful information to investors and management regarding the underlying business trends and the performance of our ongoing operations and is helpful for period-to-period and company-to-company comparisons, which management believes will assist investors in analyzing the financial results for the Company and predicting future performance. Numbers below are stated in thousands, except per share amounts.

	Fiscal Year Ended August 31, 2016		**Fiscal Year Ended August 31, 2015**	
	Net Income	**Diluted EPS**	**Net Income**	**Diluted EPS**
Reported – GAAP	**$ 64,067**	$ 1.29	$ 64,485	$ 1.20
Gain on sale of Company Drive-Ins	**(972)**	(0.02)	–	–
Tax impact on Company Drive-Ins sale [1]	**317**	0.00	–	–
FIN 48 release of income tax credits and deductions	**(3,038)**	(0.06)	–	–
Loss from early extinguishment of debt	**8,750**	0.18	–	–
Tax impact on debt extinguishment [2]	**(3,027)**	(0.06)	–	–
Gain on sale of real estate	**(1,875)**	(0.04)	–	–
Tax impact on real estate sale [3]	**664**	0.01	–	–
Retroactive benefit of Work Opportunity Tax Credit and resolution of tax matters	**(585)**	(0.01)	(666)	(0.01)
Federal tax benefit of prior-year statutory tax deduction	**–**	–	(3,199)	(0.06)
Change in deferred tax valuation allowance	**–**	–	(1,701)	(0.04)
Retroactive effect of federal tax law change	**–**	–	612	0.01
Adjusted - Non-GAAP	**$ 64,301**	$ 1.29	$ 59,531	$ 1.10

Management's Discussion and Analysis of Financial Condition and Results of Operations

	Fiscal Year Ended August 31, 2015		Fiscal Year Ended August 31, 2014	
	Net Income	Diluted EPS	Net Income	Diluted EPS
Reported – GAAP	$ 64,485	$ 1.20	$ 47,916	$ 0.85
Retroactive benefit of Work Opportunity Tax Credit and resolution of tax matters	(666)	(0.01)	–	–
Federal tax benefit of prior-year statutory tax deduction	(3,199)	(0.06)	–	–
Change in deferred tax valuation allowance	(1,701)	(0.04)	–	–
Retroactive effect of federal tax law change	612	0.01	–	–
Benefit from the IRS's acceptance of a federal tax method change	–	–	(484)	(0.01)
Adjusted - Non-GAAP	$ 59,531	$ 1.10	$ 47,432	$ 0.84

(1) Tax impact during the period at an adjusted effective tax rate of 32.6%.
(2) Tax impact during the period at an effective tax rate of 34.6%.
(3) Tax impact during the period at an adjusted effective tax rate of 35.4%.

The following table provides information regarding the number of Company Drive-Ins and Franchise Drive-Ins operating as of the end of the years indicated as well as the system-wide change in sales and average unit volume. System-wide information includes both Company Drive-In and Franchise Drive-In information, which we believe is useful in analyzing the growth of the brand as well as the Company's revenues, since franchisees pay royalties based on a percentage of sales.

	System-wide Performance Year Ended August 31,		
($ in thousands)	**2016**	2015	2014
Increase in total sales	**3.5%**	8.3%	3.9%
System-wide drive-ins in operation[1]:			
Total at beginning of year	**3,526**	3,518	3,522
Opened	**53**	41	40
Closed (net of re-openings)	**(22)**	(33)	(44)
Total at end of year	**3,557**	3,526	3,518
Average sales per drive-in	**$ 1,284**	$ 1,244	$ 1,153
Change in same-store sales[2]	**2.6%**	7.3%	3.5%

(1) Drive-ins that are temporarily closed for various reasons (repairs, remodeling, relocations, etc.) are not considered closed unless the Company determines that they are unlikely to reopen within a reasonable time.
(2) Represents percentage change for drive-ins open for a minimum of 15 months.

Results of Operations

Revenues. The following table sets forth the components of revenue for the reported periods and the relative change between the comparable periods.

	Revenues Year Ended August 31,		Increase	Percent Increase
($ in thousands)	**2016**	2015	(Decrease)	(Decrease)
Company Drive-In sales	**$ 425,795**	$ 436,031	$ (10,236)	(2.3)%
Franchise Drive-Ins:				
Franchise royalties	**168,691**	158,813	9,878	6.2
Franchise fees	**1,628**	2,529	(901)	(35.6)
Lease revenue	**7,459**	5,583	1,876	33.6
Other	**2,747**	3,133	(386)	(12.3)
Total revenues	**$ 606,320**	$ 606,089	$ 231	0.0 %

($ in thousands)	Revenues Year Ended August 31, 2015	2014	Increase (Decrease)	Percent Increase (Decrease)
Company Drive-In sales	$ 436,031	$ 405,363	$ 30,668	7.6%
Franchise Drive-Ins:				
Franchise royalties	158,813	137,125	21,688	15.8
Franchise fees	2,529	1,291	1,238	95.9
Lease revenue	5,583	4,291	1,292	30.1
Other	3,133	4,279	(1,146)	(26.8)
Total revenues	$ 606,089	$ 552,349	$ 53,740	9.7%

The following table reflects the changes in sales and same-store sales at Company Drive-Ins. It also presents information about average unit volumes and the number of Company Drive-Ins, which is useful in analyzing the growth of Company Drive-In sales.

($ in thousands)	Company Drive-In Sales Year Ended August 31, 2016	2015	2014
Company Drive-In sales	**$ 425,795**	$ 436,031	$ 405,363
Percentage increase (decrease)	**(2.3)%**	7.6%	0.8%
Company Drive-Ins in operation[1]:			
Total at beginning of year	**387**	391	396
Opened	**1**	3	3
Sold to franchisees	**(38)**	(6)	(7)
Closed (net of re-openings)	**(5)**	(1)	(1)
Total at end of year	**345**	387	391
Average sales per Company Drive-In	**$ 1,142**	$ 1,116	$ 1,043
Change in same-store sales[2]	**1.7%**	6.9%	3.5%

(1) Drive-ins that are temporarily closed for various reasons (repairs, remodeling, relocations, etc.) are not considered closed unless the Company determines that they are unlikely to reopen within a reasonable time.

(2) Represents percentage change for drive-ins open for a minimum of 15 months.

Same-store sales for Company Drive-Ins increased 1.7% for fiscal year 2016 and 6.9% for fiscal year 2015, showing continued momentum from the Company's successful implementation of initiatives to improve product quality, service and value perception. During the fiscal fourth quarter, we experienced lower-than-expected traffic, reflecting lower consumer spending in the restaurant industry and aggressive competitive activity. Company Drive-In sales decreased $10.2 million, or 2.3%, during fiscal year 2016 compared to fiscal year 2015. The change was driven by a $17.3 million decrease related to drive-ins that were refranchised during the fiscal year, partially offset by an increase of $7.3 million in same-store sales.

For fiscal year 2015, Company Drive-In sales increased $30.7 million, or 7.6%, as compared to 2014. This improvement was primarily attributable to an increase of $27.4 million in same-store sales and $3.3 million in incremental sales from new drive-in openings.

The following table reflects the change in franchise sales, the number of Franchise Drive-Ins, average unit volumes and franchising revenues. While we do not record Franchise Drive-In sales as revenues, we believe this information is important in understanding our financial performance since these sales are the basis on which we calculate and record franchise royalties. This information is also indicative of the financial health of our franchisees.

	Franchise Information Year Ended August 31,		
($ in thousands)	**2016**	**2015**	**2014**
Franchise Drive-In sales	**$ 4,092,303**	$ 3,931,365	$ 3,627,395
Percentage increase	**4.1%**	8.4%	4.2%
Franchise Drive-Ins in operation[1]:			
Total at beginning of year	**3,139**	3,127	3,126
Opened	**52**	38	37
Acquired from the Company	**38**	6	7
Closed (net of re-openings)	**(17)**	(32)	(43)
Total at end of year	**3,212**	3,139	3,127
Average sales per Franchise Drive-In	**$ 1,301**	$ 1,261	$ 1,170
Change in same-store sales[2]	**2.7%**	7.3%	3.5%
Franchising revenues[3]	**$ 177,778**	$ 166,925	$ 142,707
Percentage increase (decrease)	**6.5%**	17.0%	5.3%
Effective royalty rate[4]	**4.12%**	4.04%	3.78%

(1) Drive-ins that are temporarily closed for various reasons (repairs, remodeling, relocations, etc.) are not considered closed unless the Company determines that they are unlikely to reopen within a reasonable time.

(2) Represents percentage change for drive-ins open for a minimum of 15 months.

(3) Consists of revenues derived from franchising activities, including royalties, franchise fees and lease revenues. See *Revenue Recognition Related to Franchise Fees and Royalties* in the Critical Accounting Policies and Estimates section of "Management's Discussion and Analysis of Financial Condition and Results of Operations" included in this Annual Report.

(4) Represents franchise royalties as a percentage of Franchise Drive-In sales.

Same-store sales for Franchise Drive-Ins increased 2.7% for fiscal year 2016 and 7.3% for fiscal year 2015, showing continued momentum from the initiatives we have implemented to improve product quality, service and value perception. During the fiscal fourth quarter, we experienced lower-than-expected traffic, reflecting lower consumer spending in the restaurant industry and aggressive competitive activity. Franchising revenues increased $10.9 million, or 6.5%, for fiscal year 2016 compared to fiscal year 2015, reflecting an increase in royalties related to positive same-store sales at Franchise Drive-Ins as well as net new unit growth and franchisee acquisitions of Company Drive-Ins. These factors also impacted the increase in the effective royalty rate compared to fiscal year 2015. Lease revenues increased compared to the prior year due to an increase in same-store sales and the addition of new leases.

Franchising revenues increased $24.2 million, or 17.0%, for fiscal year 2015 compared to fiscal year 2014. The increase in franchising revenues was driven by a license conversion increasing royalty rates for approximately 900 Franchise Drive-Ins, as well as a 7.3% increase in same-store sales. Lease revenues increased compared to the prior year due to an increase in same-store sales and the addition of 14 new leases. The effective royalty rate increased compared to fiscal year 2014 as a result of the license conversion discussed above, as well as improved same-store sales.

Other revenues decreased $0.4 million to $2.7 million in fiscal year 2016 and decreased $1.2 million to $3.1 million in fiscal year 2015 as compared to the prior year. The decrease in fiscal years 2016 and 2015 was primarily due to a decrease in minority income from investments in franchise operations.

Operating Expenses. The following table presents the overall costs of drive-in operations as a percentage of Company Drive-In sales. Other operating expenses include direct operating costs such as marketing, telephone and utilities, repair and maintenance, rent, property tax and other controllable expenses.

	Company Drive-In Margins Year Ended August 31,		Percentage Points Increase (Decrease)
	2016	2015	
Costs and expenses:			
Company Drive-Ins:			
Food and packaging	**27.7%**	27.9%	(0.2)
Payroll and other employee benefits	**35.3**	34.8	0.5
Other operating expenses	**20.8**	20.8	–
Cost of Company Drive-In sales	**83.8%**	83.5%	0.3

	Company Drive-In Margins Year Ended August 31,		Percentage Points Increase (Decrease)
	2015	2014	
Costs and expenses:			
Company Drive-Ins:			
Food and packaging	27.9%	28.7%	(0.8)
Payroll and other employee benefits	34.8	34.5	0.3
Other operating expenses	20.8	21.2	(0.4)
Cost of Company Drive-In sales	83.5%	84.4%	(0.9)

Drive-in level margins were unfavorable by 30 basis points during fiscal year 2016. Food and packaging costs were favorable by 20 basis points, which reflected favorable commodity costs offset by the impact of vendor contributions that were previously credited against food and paper costs for Company Drive-Ins that are now being remitted to the BTF. Payroll and other employee benefits were unfavorable by 50 basis points reflecting investments in improved employee compensation and benefits to attract and retain employees at the drive-in level. Other operating expenses were flat as a result of leverage from sales growth offset by the impact of the fees paid to the new BTF.

Drive-in level margins improved by 90 basis points during fiscal year 2015 reflecting leverage from improved same-store sales. Food and packaging costs were favorable by 80 basis points, which reflected lower commodity costs primarily related to dairy, as well as implementation of an inventory management tool. Payroll and other employee benefits were unfavorable by 30 basis points reflecting increased health care expenses and increased incentive compensation related to growth in same-store sales. Other operating expenses improved 40 basis points, primarily as a result of leverage from sales growth.

Selling, General and Administrative ("SG&A"). SG&A expenses increased 3.5% to $82.1 million for fiscal year 2016 as compared to fiscal year 2015, and increased 14.3% to $79.3 million during fiscal year 2015 as compared to fiscal year 2014. These increases in SG&A expense for fiscal years 2016 and 2015 were primarily related to the costs of additional headcount in support of the Company's technology and marketing initiatives.

Depreciation and Amortization. Depreciation and amortization expense decreased 3.2% to $44.4 million in fiscal year 2016. The decrease during fiscal year 2016 was primarily attributable to assets that fully depreciated in the prior fiscal year and a decrease in company assets related to Company Drive-Ins that were refranchised during the fiscal year. Depreciation and amortization expense increased 8.7% to $45.9 million in fiscal year 2015. The increase during fiscal year 2015 was primarily attributable to our increased investment in technology initiatives at Company Drive-Ins.

Provision for Impairment of Long-Lived Assets. Provision for impairment of long-lived assets decreased $1.2 million to $0.2 million in fiscal year 2016 compared to $1.4 million for fiscal year 2015 and $0.1 million for 2014. The increase in fiscal year 2015 was the result of a $1.3 million impairment charge in fiscal year 2015 for the write-off of assets associated with some lower performing drive-ins.

Other Operating Income and Expense, Net. Fiscal year 2016 reflected $4.7 million in other operating income compared to $0.9 million for fiscal year 2015 and $0.2 million for fiscal year 2014. The $3.8 million change for fiscal year 2016 was primarily the result of a $1.8 million gain related to the refranchising of Company Drive-Ins during the fiscal year as well as a gain of $1.9 million related to the sale of real estate.

Net Interest Expense. Net interest expense increased $10.2 million in fiscal year 2016 compared to a decrease of $0.2 million in fiscal year 2015 and $3.6 million in fiscal year 2014. The increase in fiscal year 2016 is driven by the $8.8 million loss from the early extinguishment of debt related to our debt transaction completed in the third quarter of fiscal year 2016 and the related increase in our long-term debt balance. See "Liquidity and Sources of Capital" and "Quantitative and Qualitative Disclosures About Market Risk" below for additional information on factors that could impact interest expense.

Income Taxes. The provision for income taxes reflects an effective tax rate of 30.7% for fiscal year 2016 compared with 29.7% for fiscal year 2015 and 35.0% for fiscal year 2014. The effective income tax rate for fiscal year 2016 was impacted by the recognition of tax benefits related to a change in uncertain tax positions from prior years and legislation that reinstated and extended the Work Opportunity Tax Credit ("WOTC"). The lower effective income tax rate for fiscal year 2015 was primarily attributable to the recognition of prior years' federal tax deductions, a decrease in the valuation allowance for the deferred tax asset related to state net operating losses and legislation that reinstated and extended the WOTC. Excluding the nonrecurring tax benefits mentioned above, the effective tax rate would have been 34.7%, 35.1% and 35.0% for fiscal years 2016, 2015 and 2014, respectively. Our tax rate may continue to vary significantly from quarter to quarter depending on the timing of stock option exercises and dispositions by option holders and as circumstances on other tax matters change.

Financial Position

Total assets increased $40.0 million, or 6.5%, to $660.0 million during fiscal year 2016 from $620.0 million at the end of fiscal year 2015. The increase during the year was driven by a $44.9 million increase in cash, which reflected cash generated from operating activities and net proceeds from the 2016 debt financing transaction, detailed below in "Liquidity and Sources of Capital," offset by purchases of treasury stock and capital expenditures. Further, there was a $7.4 million increase in debt origination costs, also related to the debt transaction and an increase of $9.2 million in current and non-current accounts and notes receivable, net, primarily due to short-term financing for refranchised drive-ins and newly constructed drive-ins sold to franchisees and an increase in receivables from system funds related to the establishment of the BTF in the third quarter of the fiscal year. Additionally, there was a decrease in net property, equipment and capital leases of $19.2 million, driven by depreciation and asset retirements, partially offset by purchases of property and equipment.

Total liabilities increased $133.0 million, or 22%, to $735.6 million during fiscal year 2016 from $602.6 million at the end of fiscal year 2015. The increase was primarily attributable to an increase in long-term debt of $149.3 million, offset by an $8.4 million decrease in current maturities of long-term debt, all related to the 2016 debt financing transaction, detailed below in "Liquidity and Sources of Capital."

Total stockholders' equity (deficit) decreased $93.1 million, or 533.9%, to a deficit of $75.6 million during fiscal year 2016 from $17.4 million at the end of fiscal year 2015. This decrease was primarily attributable to $148.3 million in purchases of common stock under our stock repurchase program and the payment of $21.3 million in dividends, partially offset by current-year earnings of $64.1 million and $9.2 million from the issuance of stock related to stock option exercises and restricted stock units ("RSUs") that vested during fiscal year 2016.

Liquidity and Sources of Capital

Operating Cash Flows. Net cash provided by operating activities decreased $20.2 million to $116.2 million for fiscal year 2016 as compared to $136.4 million in fiscal year 2015. This decrease resulted from changes in working capital related to the timing of payments and receipts for both operational and tax transactions.

Investing Cash Flows. Cash used in investing activities increased $8.8 million to $34.1 million for fiscal year 2016 compared to $25.3 million for fiscal year 2015. During fiscal year 2016, we used $46.6 million of cash for investments in property and equipment as outlined in the table below (in millions).

Brand technology investments	$ 15.5
Purchase and replacement of equipment and technology	12.4
Rebuilds, relocations and remodels of existing drive-ins	12.0
Newly constructed drive-ins leased or sold to franchisees	3.7
Newly constructed Company Drive-Ins	1.7
Acquisition of underlying real estate for drive-ins	1.3
Total investments in property and equipment	$ 46.6

These purchases increased $4.4 million in fiscal year 2016 compared to the same period last year, primarily due to additions to rebuilds, relocations and remodels of existing drive-ins and brand technology investments, offset by a decline in cash used for the acquisition of underlying real estate for drive-ins. Additionally, other cash flows used for investing increased as a result of increased notes receivable, discussed above in "Financial Position."

Financing Cash Flows. Net cash used in financing activities decreased $82.3 million to $37.2 million for fiscal year 2016 as compared to $119.5 million in fiscal year 2015. This decrease primarily relates to $140.9 million of net borrowings from the debt financing transaction and scheduled principal payments, offset by $18.4 million in debt issuance and extinguishment costs, a $30.0 million increase in purchases of treasury stock and a $14.9 million decrease in proceeds from the exercise of stock options.

During fiscal year 2013, in a private transaction, various subsidiaries of ours (the "Co-Issuers") refinanced and paid $155.0 million of the Series 2011 Senior Secured Fixed Rate Notes, Class A-2 (the "2011 Fixed Rate Notes") with the issuance of $155.0 million of Series 2013-1 Senior Secured Fixed Rate Notes, Class A-2 (the "2013 Fixed Rate Notes"), which bear interest at 3.75% per annum. The 2013 Fixed Rate Notes have an expected life of seven years, interest payable monthly, no scheduled principal amortization and an anticipated repayment date in July 2020.

On May 17, 2016, in a private transaction, the Co-Issuers issued $425.0 million of Series 2016-1 Senior Secured Fixed Rate Notes, Class A-2 (the "2016 Fixed Rate Notes"), which bears interest at 4.47% per annum. The 2016 Fixed Rate Notes have an expected life of seven years with an anticipated repayment date in May 2023.

The Co-Issuers also entered into a securitized financing facility of Series 2016-1 Senior Secured Variable Funding Notes, Class A-1 (the "2016 Variable Funding Notes" and, together with the 2016 Fixed Rate Notes, the "2016 Notes") to replace the Series 2011-1 Senior Secured Variable Funding Notes, Class A-1 (the "2011 Variable Funding Notes"). The 2016 revolving credit facility provides access to a maximum of $150.0 million of 2016 Variable Funding Notes and certain other credit instruments, including letters of credit. Interest on the 2016 Variable Funding Notes is based on the one-month London Interbank Offered Rate or Commercial Paper, depending on the funding source, plus 2.0%, per annum. An annual commitment fee of 0.5% is payable monthly on the unused portion of the 2016 Variable Funding Notes facility. The 2016 Variable Funding Notes have an expected life of five years with an anticipated repayment date in May 2021 with two one-year extension options available upon certain conditions including meeting a minimum debt service coverage ratio threshold.

We used a portion of the net proceeds from the issuance of the 2016 Fixed Rate Notes to repay our existing 2011 Fixed Rate Notes and 2011 Variable Funding Notes in full and to pay the costs associated with the securitized financing transaction, including prepayment premiums.

At August 31, 2016, the balance outstanding under the 2013 Fixed Rate Notes and the 2016 Fixed Rate Notes, including accrued interest, was $155.2 million and $424.5 million, respectively. The weighted-average interest cost of the 2013 Fixed Rate Notes and 2016 Fixed Rate Notes was 4.1% and 4.8%, respectively. The weighted-average interest cost includes the effect of the loan origination costs.

In connection with the 2016 transaction described above, we recognized an $8.8 million loss from the early extinguishment of debt during the third quarter of fiscal year 2016, which primarily consisted of a $5.9 million prepayment premium and the $2.9 million write-off of unamortized deferred loan fees remaining from the refinanced debt. This is reflected in "loss from early extinguishment of debt" on the Consolidated Statements of Income. Loan origination costs associated with the 2016 transaction totaled $12.5 million and were allocated among the 2016 Notes. Loan costs are being amortized over each note's expected life, and the unamortized balance is categorized as "debt origination costs, net" on the Consolidated Balance Sheets. For additional information on our 2013 Fixed Rate Notes and 2016 Notes, see note 9 – Debt, included in the Notes to Consolidated Financial Statements in this Annual Report.

In August 2014, our Board of Directors extended our share repurchase program, authorizing us to purchase up to $105.0 million of our outstanding shares of common stock during fiscal year 2015. In October 2014, the Company entered into an accelerated share repurchase ("ASR") agreement with a financial institution to purchase $15.0 million of the Company's common stock. In exchange for a $15.0 million up-front payment, the financial institution delivered approximately 0.6 million shares. During January 2015, the ASR purchase period concluded. The Company paid an additional $0.1 million with no additional shares delivered, resulting in an average price per share of $26.32. In February 2015, the Company entered into additional ASR agreements with a financial institution to purchase $75.0 million of the Company's common stock. In exchange for a $75.0 million up-front payment, the financial institution delivered approximately 2.1 million shares. The ASR transactions completed in July 2015 with 0.3 million additional shares delivered, resulting in an average price per share of $31.38. The Company reflected the ASR transactions as a repurchase of common stock for purposes of calculating earnings per share and as a forward contract indexed to its own common stock. The forward contract met all of the applicable criteria for equity classification.

In August 2015, our Board of Directors extended our share repurchase program, authorizing us to purchase up to $145.0 million of our outstanding shares of common stock through August 31, 2016. Our Board of Directors further extended the share repurchase program effective May 2016, authorizing the purchase of up to an additional $155.0 million of our outstanding shares of common stock through August 31, 2017. During fiscal year 2016, approximately 5.2 million shares were repurchased for a total cost of $148.3 million, resulting in an average price per share of $28.48.

Share repurchases will be made from time to time in the open market or otherwise, including through an ASR program, under the terms of a Rule 10b5-1 plan, in privately negotiated transactions or in round lot or block transactions. The share repurchase program may be extended, modified, suspended or discontinued at any time.

As of August 31, 2016, our total cash balance of $88.1 million ($72.1 million of unrestricted and $16.0 million of restricted cash balances) reflected the impact of the cash generated from operating activities, stock option exercise proceeds, 2016 debt transaction proceeds and cash used for share repurchases, dividends, debt payments and capital expenditures mentioned above. We believe that existing cash, funds generated from operations and the amount available under our 2016 Variable Funding Notes will meet our needs for the foreseeable future.

In August 2014, the Company initiated a quarterly cash dividend program and paid a quarterly dividend of $0.09 per share of common stock, totaling $18.8 million, for fiscal year 2015 and paid a quarterly dividend of $0.11 per share of common stock, totaling $21.3 million, for fiscal year 2016. Subsequent to the end of the fiscal year, the Company declared a quarterly dividend of $0.14 per share of common stock to be paid to stockholders of record as of the close of business on November 9, 2016, with a payment date of November 18, 2016. The future declaration of quarterly dividends and the establishment of future record and payment dates are subject to the final determination of the Company's Board of Directors.

Off-Balance Sheet Arrangements

The Company has obligations for guarantees on certain franchisee loans, which in the aggregate are immaterial, and obligations for guarantees on certain franchisee lease agreements. Other than such guarantees and various operating leases and purchase obligations, which are disclosed below in "Contractual Obligations and Commitments" and in note 6 - Leases and note 14 – Commitments and Contingencies, included in the Notes to Consolidated Financial Statements in this Annual Report, the Company has no other material off-balance sheet arrangements.

Contractual Obligations and Commitments

In the normal course of business, Sonic enters into purchase contracts, lease agreements and borrowing arrangements. The following table presents our commitments and obligations as of August 31, 2016 (in thousands):

		Payments Due by Fiscal Year			
	Total	**Less than 1 Year (2017)**	**1 – 3 Years (2018 to 2019)**	**3 – 5 Years (2020 to 2021)**	**More than 5 Years (2022 and thereafter)**
Long-term debt[1]	**$ 728,570**	$ 26,136	$ 49,415	$ 197,957	$ 455,062
Capital leases	**26,503**	5,051	8,044	6,390	7,018
Operating leases	**117,135**	10,914	21,704	20,784	63,733
Purchase obligations[2]	**235,841**	26,066	42,392	45,738	121,645
Other[3]	**14,088**	–	–	–	–
Total	**$ 1,122,137**	$ 68,167	$ 121,555	$ 270,869	$ 647,458

(1) Includes scheduled principal and interest payments on our 2016 Notes and 2013 Fixed Rate Notes and assumes these notes will be outstanding for the expected seven-year life with anticipated repayment dates in July 2020 and May 2023, respectively.

(2) Purchase obligations primarily relate to the Company's estimated share of system-wide commitments to purchase food products. We have excluded agreements that are cancelable without penalty. These amounts require estimates and could vary due to the timing of volumes and changes in market pricing.

(3) Includes $0.6 million of unrecognized tax benefits related to uncertain tax positions and $13.5 million related to guarantees of franchisee leases and loan agreements. As we are not able to reasonably estimate the timing or amount of these payments, if any, the related balances have not been reflected in the "Payments Due by Fiscal Year" section of the table.

Impact of Inflation

We are impacted by inflation which has caused increases in our food, labor and benefits costs and has increased our operating expenses. To the extent permitted by competition and the consumer environment, increased costs are recovered through a combination of menu price increases and alternative products, efficiencies or processes, or by implementing other cost reduction procedures.

Critical Accounting Policies and Estimates

The Consolidated Financial Statements and Notes to Consolidated Financial Statements included in this document contain information that is pertinent to management's discussion and analysis. The preparation of financial statements in conformity with generally accepted accounting principles requires management to use its judgment to make estimates and assumptions that affect the reported amounts of assets and liabilities and disclosure of contingent assets and liabilities. These assumptions and estimates could have a material effect on our financial statements. We evaluate our assumptions and estimates on an ongoing basis using historical experience and various other factors that are believed to be relevant under the circumstances. Actual results may differ from these estimates under different assumptions or conditions.

We perform a periodic review of our financial reporting and disclosure practices and accounting policies to ensure that our financial reporting and disclosures provide accurate and transparent information relative to the current economic and business environment. We believe the following significant accounting policies and estimates involve a high degree of risk, judgment and/or complexity.

Accounting for Long-Lived Assets. We review Company Drive-In assets for impairment when events or circumstances indicate they might be impaired. We test for impairment using historical cash flows and other relevant facts and circumstances as the primary basis for our estimates of future cash flows. This process requires us to estimate fair values of our drive-ins by making assumptions regarding future cash flows and other factors. It is reasonably possible that our estimates of future cash flows could change resulting in the need to write down to fair value certain Company Drive-In assets.

We assess the recoverability of goodwill at least annually and more frequently if events or changes in circumstances occur indicating that the carrying amount of goodwill may not be recoverable or as a result of allocating goodwill to Company Drive-Ins that are sold. Since the Company is one reporting unit, we identify potential goodwill impairment by comparing the fair value of the Company to its carrying value. The fair value of the Company is determined using a market approach. If the carrying value of the Company exceeds fair value, a comparison of the fair value of goodwill against the carrying value of goodwill is made to determine whether goodwill has been impaired.

During the fourth quarter of fiscal year 2016, we performed our annual assessment of the recoverability of goodwill and determined that no impairment was indicated. As of the impairment testing date, the fair value of the Company significantly exceeded the carrying value. As of August 31, 2016, the Company had $76.7 million of goodwill.

Revenue Recognition Related to Franchise Fees and Royalties. Franchise fees and development fees are generally recognized upon the opening of a Franchise Drive-In or upon termination of the agreement between the Company and the franchisee. Our franchisees pay royalties based on a percentage of sales. Royalties are recognized as revenue when they are earned.

Accounting for Stock-Based Compensation. We estimate the fair value of stock options granted using the Black-Scholes option pricing model along with the assumptions shown in note 12 – Stockholders' Equity (Deficit), included in the Notes to Consolidated Financial Statements in this Annual Report. The assumptions used in computing the fair value of stock-based payments reflect our best estimates, but involve uncertainties relating to market and other conditions, many of which are outside of our control. We estimate expected volatility based on historical daily price changes of the Company's stock for a period equal to the current expected term of the options. The expected option term is the number of years the Company estimates that options will be outstanding prior to exercise considering vesting schedules and our historical exercise patterns. If other assumptions or estimates had been used, the stock-based compensation expense that was recorded could have been materially different. Furthermore, if different assumptions are used in future periods, stock-based compensation expense could be materially impacted.

Income Taxes. We estimate certain components of our provision for income taxes. These estimates include, among other items, depreciation and amortization expense allowable for tax purposes, allowable tax credits for items such as wages paid to certain employees, effective rates for state and local income taxes and the tax deductibility of certain other items.

Although we believe we have adequately accounted for our uncertain tax positions, from time to time, audits result in proposed assessments where the ultimate resolution may give rise to us owing additional taxes. We adjust our uncertain tax positions until they are resolved in light of changing facts and circumstances, such as the completion of a tax audit, expiration of a statute of limitations, the refinement of an estimate and penalty and interest accruals associated with uncertain tax positions. We believe that our tax positions comply with applicable tax law and that we have adequately provided for these matters. However, to the extent that the final tax outcome of these matters is different from the amounts recorded, such differences will impact the provision for income taxes in the period in which such determination is made.

Our estimates are based on the best available information at the time that we prepare the provision, including legislative and judicial developments. We generally file our annual income tax returns several months after our fiscal year end. Income tax returns are subject to audit by federal, state and local governments, typically several years after the returns are filed. These returns could be subject to material adjustments or differing interpretations of the tax laws. Adjustments to these estimates or returns can result in significant variability in the tax rate from period to period.

Leases. We lease the land and buildings for certain Company Drive-Ins from third parties. Rent expense for operating leases is recognized on a straight-line basis over the expected lease term, including cancelable option periods when it is deemed to be reasonably assured that we would incur an economic penalty for not exercising the options. Judgment is required to determine options expected to be exercised. Within the terms of some of our leases, there are rent holidays and/or escalations in payments over the base lease term, as well as renewal periods. The effects of the rent holidays and escalations are reflected in rent expense on a straight-line basis over the expected lease term, including cancelable option periods when appropriate. The lease term commences on the date when we have the right to control the use of lease property, which can occur before rent payments are due under the terms of the lease. Contingent rent is generally based on sales levels and is accrued at the point in time we determine that it is probable that such sales levels will be achieved.

Accounts and Notes Receivable. We charge interest on past due accounts receivable and recognize income as it is collected. Interest accrues on notes receivable based on the contractual terms of the respective notes. We monitor all accounts and notes receivable for delinquency and provide for estimated losses for specific receivables that are not likely to be collected. We assess credit risk for accounts and notes receivable of specific franchisees based on payment history, current payment patterns, the health of the franchisee's business and an assessment of the franchisee's ability to pay outstanding balances. In addition to allowances for bad debt for specific franchisee receivables, a general provision for bad debt is estimated for accounts receivable based on historical trends. Account balances generally are charged against the allowance when we believe it is probable that the receivable will not be recovered and legal remedies have been exhausted. We continually review our allowance for doubtful accounts.

New Accounting Pronouncements

For a description of new accounting pronouncements, see the "New Accounting Pronouncements" section of note 1 – Summary of Significant Accounting Policies, included in the Notes to Consolidated Financial Statements in this Annual Report.

Quantitative and Qualitative Disclosures About Market Risk

Sonic's use of debt directly exposes the Company to interest rate risk. Fixed rate debt, where the interest rate is fixed over the life of the instrument, exposes the Company to changes in market interest rates reflected in the fair value of the debt and to the risk that the Company may need to refinance maturing debt with new debt at a higher rate. Sonic is also exposed to market risk from changes in commodity prices. The Company does not utilize financial instruments for trading purposes. Sonic manages its debt portfolio to achieve an overall desired position of fixed and floating rates.

Interest Rate Risk. Our exposure to interest rate risk at August 31, 2016, was primarily based on the 2013 Fixed Rate Notes and 2016 Fixed Rate Notes with an effective rate of 3.75% and 4.47%, respectively, before amortization of debt-related costs. At August 31, 2016, the fair value of the 2013 Fixed Rate Notes and 2016 Fixed Rate Notes approximated their carrying value of $579.6 million, including accrued interest. To derive the fair value, management used market information available for public debt transactions for companies with ratings that are similar to our ratings and information gathered from brokers who trade in our notes. Management believes this fair value is a reasonable estimate. Should interest rates and/or credit spreads increase or decrease by one percentage point, the estimated fair value of the 2013 Fixed Rate Notes and 2016 Fixed Rate Notes would decrease or increase by approximately $15.0 million, respectively. The fair value estimate required significant assumptions by management.

Commodity Price Risk. The Company and its franchisees purchase certain commodities such as beef, potatoes, chicken and dairy products. These commodities are generally purchased based upon market prices established with vendors. These purchase arrangements may contain contractual features that limit the price paid by establishing price floors or caps; however, we generally do not make any long-term commitments to purchase any minimum quantities under these arrangements other than as disclosed under "Contractual Obligations and Commitments." We also do not use financial instruments to hedge commodity prices because these purchase arrangements help control the ultimate cost.

This market risk discussion contains forward-looking statements. Actual results may differ materially from this discussion based upon general market conditions and changes in financial markets.

Consolidated Balance Sheets

(In thousands, except per share amounts)	August 31, 2016	August 31, 2015
Assets		
Current assets:		
Cash and cash equivalents	**$ 72,092**	$ 27,191
Restricted cash	**15,873**	13,246
Accounts and notes receivable, net	**35,437**	31,577
Inventories	**3,321**	3,824
Prepaid expenses	**4,713**	5,544
Other current assets	**6,221**	4,056
Total current assets	**137,657**	85,438
Noncurrent restricted cash	**140**	6,524
Notes receivable, net	**12,562**	7,216
Property, equipment and capital leases, net	**402,162**	421,406
Goodwill	**76,734**	77,076
Debt origination costs, net	**14,427**	7,056
Other assets, net	**16,313**	15,308
Total assets	**$ 659,995**	$ 620,024
Liabilities and stockholders' equity (deficit)		
Current liabilities:		
Accounts payable	**$ 14,372**	$ 13,860
Franchisee deposits	**720**	870
Accrued liabilities	**51,913**	50,714
Income taxes payable	**2,568**	8,910
Current maturities of long-term debt and capital leases	**5,090**	13,467
Total current liabilities	**74,663**	87,821
Obligations under capital leases due after one year	**17,391**	20,763
Long-term debt due after one year	**577,521**	428,238
Deferred income taxes	**42,530**	43,549
Other non-current liabilities	**23,533**	22,220
Commitments and contingencies (Notes 6, 7, 13, 14)		
Stockholders' equity (deficit):		
Preferred stock, par value $.01; 1,000 shares authorized; none outstanding	**–**	–
Common stock, par value $.01; 245,000 shares authorized; 118,309 shares issued in 2016 and in 2015	**1,183**	1,183
Paid-in capital	**234,956**	232,550
Retained earnings	**894,442**	851,715
Treasury stock, at cost; 71,670 shares in 2016 and 67,249 shares in 2015	**(1,206,224)**	(1,068,015)
Total stockholders' equity (deficit)	**(75,643)**	17,433
Total liabilities and stockholders' equity (deficit)	**$ 659,995**	$ 620,024

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

Consolidated Statements of Income

(In thousands, except per share amounts)	Year Ended August 31, 2016	2015	2014
Revenues:			
Company Drive-In sales	**$ 425,795**	$ 436,031	$ 405,363
Franchise Drive-Ins:			
Franchise royalties and fees	**170,319**	161,342	138,416
Lease revenue	**7,459**	5,583	4,291
Other	**2,747**	3,133	4,279
Total revenues	**606,320**	606,089	552,349
Costs and expenses:			
Company Drive-Ins:			
Food and packaging	**118,136**	121,701	116,325
Payroll and other employee benefits	**150,260**	151,801	139,939
Other operating expenses, exclusive of depreciation and amortization included below	**88,424**	90,436	85,845
Total cost of Company Drive-In sales	**356,820**	363,938	342,109
Selling, general and administrative	**82,089**	79,336	69,415
Depreciation and amortization	**44,418**	45,892	42,210
Provision for impairment of long-lived assets	**232**	1,440	114
Other operating income, net	**(4,691)**	(945)	(176)
Total costs and expenses	**478,868**	489,661	453,672
Income from operations	**127,452**	116,428	98,677
Interest expense	**26,714**	25,114	25,382
Interest income	**(516)**	(408)	(469)
Loss from early extinguishment of debt	**8,750**	–	–
Net interest expense	**34,948**	24,706	24,913
Income before income taxes	**92,504**	91,722	73,764
Provision for income taxes	**28,437**	27,237	25,848
Net income	**$ 64,067**	$ 64,485	$ 47,916
Basic income per share	**$ 1.32**	$ 1.23	$ 0.87
Diluted income per share	**$ 1.29**	$ 1.20	$ 0.85
Cash dividends declared per common share	**$ 0.44**	$ 0.27	$ 0.09

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

Consolidated Statements of Stockholders' Equity (Deficit)

(In thousands)	Common Stock	Paid-in Capital	Retained Earnings	Treasury Stock Shares	Treasury Stock Amount	Total Stockholders' Equity (Deficit)
Balance at August 31, 2013	$ 1,183	$ 224,768	$ 758,138	62,025	$ (906,625)	$ 77,464
Net income	–	–	47,916	–	–	47,916
Cash dividends	–	–	(4,852)	–	–	(4,852)
Stock-based compensation expense	–	3,742	–	–	–	3,742
Purchase of treasury stock	–	–	–	4,080	(80,045)	(80,045)
Exercise of stock options and issuance of restricted stock	–	(4,186)	-	(1,575)	21,593	17,407
Other	–	680	-	(25)	363	1,043
Balance at August 31, 2014	$ 1,183	$ 225,004	$ 801,202	64,505	$ (964,714)	$ 62,675
Net income	–	-	64,485	–	–	64,485
Cash dividends	–	-	(13,972)	–	–	(13,972)
Stock-based compensation expense	–	3,520	–	–	–	3,520
Purchase of treasury stock	–	-	–	4,201	(123,786)	(123,786)
Exercise of stock options and issuance of restricted stock	–	(1,458)	–	(1,438)	20,190	18,732
Other	–	5,484	–	(19)	295	5,779
Balance at August 31, 2015	$ 1,183	$ 232,550	$ 851,715	67,249	$ (1,068,015)	$ 17,433
Net income	**–**	**–**	**64,067**	**–**	**–**	**64,067**
Cash dividends	**–**	**–**	**(21,340)**	**–**	**–**	**(21,340)**
Stock-based compensation expense	**–**	**3,766**	**–**	**–**	**–**	**3,766**
Purchase of treasury stock	**–**	**–**	**–**	**5,209**	**(148,345)**	**(148,345)**
Exercise of stock options and issuance of restricted stock	**–**	**(5,941)**	**–**	**(767)**	**9,783**	**3,842**
Other	**–**	**4,581**	**–**	**(21)**	**353**	**4,934**
Balance at August 31, 2016	**$ 1,183**	**$ 234,956**	**$ 894,442**	**71,670**	**$ (1,206,224)**	**$ (75,643)**

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

Consolidated Statements of Cash Flows

(In thousands)	Year Ended August 31, 2016	2015	2014
Cash flows from operating activities:			
Net income	**$ 64,067**	$ 64,485	$ 47,916
Adjustments to reconcile net income to net cash provided by operating activities:			
Depreciation and amortization	**44,418**	45,892	42,210
Stock-based compensation expense	**3,766**	3,520	3,742
Loss from early extinguishment of debt	**8,750**	–	–
Other	**270**	9,366	735
(Increase) decrease in operating assets:			
Restricted cash	**(2,829)**	(61)	(1,428)
Accounts receivable and other assets	**2,109**	2,885	(5,977)
Increase (decrease) in operating liabilities:			
Accounts payable	**380**	(1,288)	640
Accrued and other liabilities	**4,520**	10,296	7,347
Income taxes	**(9,242)**	1,267	8,363
Total adjustments	**52,142**	71,877	55,632
Net cash provided by operating activities	**116,209**	136,362	103,548
Cash flows from investing activities:			
Purchases of property and equipment	**(46,553)**	(42,153)	(79,008)
Proceeds from sale of assets	**16,206**	13,701	2,148
Other	**(3,713)**	3,132	6,337
Net cash used in investing activities	**(34,060)**	(25,320)	(70,523)
Cash flows from financing activities:			
Payments on debt	**(422,090)**	(90,290)	(9,976)
Proceeds from borrowings	**563,000**	91,000	-
Restricted cash for securitization obligations	**6,587**	151	181
Purchases of treasury stock	**(150,444)**	(120,463)	(79,786)
Proceeds from exercise of stock options	**3,842**	18,732	17,407
Payment of dividends	**(21,309)**	(18,808)	–
Debt issuance and extinguishment costs	**(18,420)**	(12)	(151)
Other	**1,586**	145	(2,902)
Net cash used in financing activities	**(37,248)**	(119,545)	(75,227)
Net increase (decrease) in cash and cash equivalents	**44,901**	(8,503)	(42,202)
Cash and cash equivalents at beginning of year	**27,191**	35,694	77,896
Cash and cash equivalents at end of year	**$ 72,092**	$ 27,191	$ 35,694
Supplemental cash flow information			
Cash paid during the year for:			
Interest	**$ 24,883**	$ 23,330	$ 23,701
Income taxes (net of refunds)	**27,821**	11,360	14,143
Non-cash investing and financing activities:			
Change in obligation to acquire treasury stock	**(2,099)**	3,323	259
Stock options exercised by stock swap	**6,396**	3,385	4,634
Accrued PP&E at period end	**3,471**	3,346	3,297
Dividend Payable	**44**	13	4,852

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

1. Summary of Significant Accounting Policies

Operations

Sonic Corp. (the "Company") operates and franchises a chain of quick-service restaurants in the United States ("U.S."). It derives its revenues primarily from Company Drive-In sales and royalty fees from franchisees. The Company also leases real estate and receives equity earnings in noncontrolling ownership in a number of Franchise Drive Ins.

Principles of Consolidation

The accompanying financial statements include the accounts of the Company, its wholly owned subsidiaries and a number of Company Drive-Ins in which a subsidiary has a controlling ownership interest. All intercompany accounts and transactions have been eliminated.

Use of Estimates

The preparation of consolidated financial statements in conformity with U.S. generally accepted accounting principles ("GAAP") requires management to make estimates and assumptions that affect the amounts reported and contingent assets and liabilities disclosed in the financial statements and accompanying notes. Actual results may differ from those estimates, and such differences may be material to the financial statements.

Reclassifications

Certain amounts reported in previous years, which are not material, have been combined and reclassified to conform to the current-year presentation.

Segment Reporting

In accordance with Accounting Standards Update ("ASU") 280, "Segment Reporting," the Company uses the management approach for determining its reportable segments. The management approach is based upon the way that management reviews performance and allocates resources. The Company's chief operating decision maker and his management team review operating results on a consolidated basis for purposes of allocating resources and evaluating the financial performance of the Sonic brand. Accordingly, the Company has determined that it has one operating segment and, therefore, one reporting segment.

Cash Equivalents

Cash equivalents consist of highly liquid investments, primarily money market accounts that mature in three months or less from date of purchase, and depository accounts.

Restricted Cash

As of August 31, 2016, the Company had restricted cash balances totaling $16.0 million for funds required to be held in trust for the benefit of senior noteholders under the Company's debt arrangements. The current portion of restricted cash of $15.9 million represents amounts to be returned to Sonic or paid to service current debt obligations. The noncurrent portion of $0.1 million represents interest reserves required to be set aside for the duration of the debt.

Accounts and Notes Receivable

The Company charges interest on past due accounts receivable and recognizes income as it is collected. Interest accrues on notes receivable based on the contractual terms of the respective note. The Company monitors all accounts and notes receivable for delinquency and provides for estimated losses for specific receivables that are not likely to be collected. The Company assesses credit risk for accounts and notes receivable of specific franchisees based on payment history, current payment patterns, the health of the franchisee's business and an assessment of the franchisee's ability to pay outstanding balances. In addition to allowances for bad debt for specific franchisee receivables, a general provision for bad debt is estimated for the Company's accounts receivable based on historical trends. Account balances generally are charged against the allowance when the Company believes that the collection is no longer reasonably assured. The Company continually reviews its allowance for doubtful accounts.

Inventories

Inventories consist principally of food and supplies that are carried at the lower of cost (first-in, first-out basis) or market.

Property, Equipment and Capital Leases

Property and equipment are recorded at cost, and leased assets under capital leases are recorded at the present value of future minimum lease payments. Depreciation of property and equipment and amortization of capital leases are computed by the straight-line method over the estimated useful lives or the lease term, including cancelable option periods when appropriate, and are combined for presentation in the financial statements.

Accounting for Long-Lived Assets

The Company reviews long-lived assets whenever events or changes in circumstances indicate that the carrying amount of an asset might not be recoverable. Assets are grouped and evaluated for impairment at the lowest level for which there are identifiable cash flows that are largely independent of the cash flows of other groups of assets, which generally represents the individual drive-in. The Company's primary test for an indicator of potential impairment is operating losses of the related drive-in. If an indication of impairment is determined to be present, the Company estimates the future cash flows expected to be generated from the use of the asset and its eventual disposal. If the sum of undiscounted future cash flows is less than the carrying amount of the asset, an impairment loss is recognized. The impairment loss is measured by comparing the fair value of the asset to its carrying amount. Fair value is typically determined to be the value of the land since drive-in buildings and improvements are single-purpose assets and have little value to market participants. The equipment associated with a drive-in can be easily relocated to another drive-in and therefore is not adjusted.

Surplus property assets are carried at the lower of depreciated cost or fair value less cost to sell. The majority of the value in surplus property is land. Fair values are estimated based upon management's assessment as well as independent market value assessments of the assets' estimated sales values.

Goodwill and Other Intangible Assets

Goodwill is determined based on an acquisition purchase price in excess of the fair value of identified assets. Intangible assets with lives restricted by contractual, legal or other means are amortized over their useful lives. The Company tests goodwill at least annually for impairment using the fair value approach on a reporting unit basis.

Since the Company is one reporting unit, potential goodwill impairment is evaluated by comparing the fair value of the Company to its carrying value. The fair value of the Company is determined using a market approach. If the carrying value of the Company exceeds fair value, a comparison of the fair value of goodwill against the carrying value of goodwill is made to determine whether goodwill has been impaired. During the fourth quarters of fiscal years 2016 and 2015, the annual assessment of the recoverability of goodwill was performed, and no impairment was indicated.

The Company's intangible assets subject to amortization consist primarily of acquired franchise agreements, intellectual property and other intangibles. Amortization expense is calculated using the straight-line method over the asset's expected useful life. See note 4 - Goodwill and Other Intangibles for additional related disclosures.

Refranchising and Closure of Company Drive-Ins

Gains and losses from the sale or closure of Company Drive-Ins are recorded as "other operating (income) expense, net" on the Consolidated Statements of Income.

Revenue Recognition, Franchise Fees and Royalties

Revenue from Company Drive-In sales is recognized when food and beverage products are sold. Company Drive-In sales are presented net of sales tax and other sales-related taxes.

The Company's gift card program serves all Sonic Drive-Ins and is administered by the Company on behalf of a system advertising fund. The Company records a liability in the period in which a gift card is sold. The gift cards do not have expiration dates. As gift cards are redeemed, the liability is reduced with revenue recognized on redemptions at Company Drive-Ins. Breakage is the amount on a gift card that is not expected to be redeemed and that the Company is not required to remit to a state under unclaimed property laws. The Company estimates breakage based upon the historical trend in redemption patterns from previously sold gift cards. The Company's policy is to recognize the breakage, using the delayed recognition method, when it is apparent that there is a remote likelihood the gift card balance will be redeemed. The Company reduces the gift card liability for the estimated breakage and uses that amount to defray the costs of operating the gift card program. There is no income recognized on unredeemed gift card balances. Costs to administer the gift card program, net of breakage, are included in the receivables from advertising funds as set forth in note 3 – Accounts and Notes Receivable. Such costs were not material in fiscal years 2016, 2015 and 2014.

Franchise fees are recognized in income when the Company has substantially performed or satisfied all material services or conditions relating to the sale of the franchise, and the fees are generally nonrefundable. Development fees are nonrefundable and are recognized in income on a pro-rata basis when the conditions for revenue recognition under the individual development agreements are met. Both franchise fees and development fees are generally recognized upon the opening of a Franchise Drive-In or upon termination of the agreement between the Company and the franchisee.

The Company's franchisees pay royalties based on a percentage of sales. Royalties are recognized as revenue when they are earned.

Advertising Costs

Costs incurred in connection with advertising and promoting the Company's products are included in other operating expenses and are expensed as incurred. Such costs amounted to $23.4 million, $24.5 million and $22.4 million in fiscal years 2016, 2015 and 2014, respectively.

Under the Company's franchise agreements, both Company Drive-Ins and Franchise Drive-Ins must contribute a minimum percentage of revenues to a national media production fund ("Sonic Brand Fund") and spend an additional minimum percentage of gross revenues on advertising, either directly or through Company-required participation in advertising cooperatives. A significant portion of the advertising cooperative contributions is remitted to the System Marketing Fund, which purchases advertising on national cable and broadcast networks and local broadcast networks and also funds other national media expenses and sponsorship opportunities. As stated in the terms of existing franchise agreements, these funds do not constitute assets of the Company, and the Company acts with limited agency in the administration of these funds. Accordingly, neither the revenues and expenses nor the assets and liabilities of the advertising cooperatives, the Sonic Brand Fund or the System Marketing Fund are included in the Company's consolidated financial statements. However, all advertising contributions by Company Drive-Ins are recorded as an expense on the Company's financial statements.

Under the Company's franchise agreements, the Company is reimbursed by the Sonic Brand Fund for costs incurred to administer the fund at an amount not to exceed 15% of the Sonic Brand Fund's gross receipts. Reimbursements from the Sonic Brand Fund are offset against selling, general and administrative expenses and totaled $5.2 million, $5.0 million and $4.4 million in fiscal years 2016, 2015 and 2014, respectively.

Technology Costs

Under the Company's franchise agreements, both Company Drive-Ins and Franchise Drive-Ins must pay a set technology fee to the Brand Technology Fund ("BTF"), which was established in the third quarter of fiscal year 2016. The BTF administers cybersecurity and other technology programs for the Sonic system. As stated in the terms of existing franchise agreements, these funds do not constitute assets of the Company, and the Company acts with limited agency in the administration of these funds. Accordingly, neither the revenues and expenses nor the assets and liabilities of the BTF are included in the Company's consolidated financial statements. However, technology fees paid by Company Drive-Ins are recorded as an expense on the Company's financial statements.

Under the Company's franchise agreements, the Company is reimbursed by the BTF for costs incurred to administer the fund at an amount not to exceed 15% of the BTF's gross receipts. Reimbursements from the BTF are offset against selling, general and administrative expenses and totaled $2.5 million in fiscal year 2016.

Operating Leases

Rent expense is recognized on a straight-line basis over the expected lease term, including cancelable option periods when it is deemed to be reasonably assured that the Company would incur an economic penalty for not exercising the options. Within the terms of some of the leases, there are rent holidays and/or escalations in payments over the base lease term, as well as renewal periods. The effects of the holidays and escalations have been reflected in rent expense on a straight-line basis over the expected lease term, which includes cancelable option periods when appropriate. The lease term commences on the date when the Company has the right to control the use of the leased property, which can occur before rent payments are due under the terms of the lease. Contingent rent is generally based on sales levels and is accrued at the point in time it is probable that such sales levels will be achieved.

Stock-Based Compensation

The Company grants incentive stock options ("ISOs"), non-qualified stock options ("NQs") and restricted stock units ("RSUs"). For grants of NQs and RSUs, the Company expects to recognize a tax benefit upon exercise of the option or vesting of the RSU. As a result, a tax benefit is recognized on the related stock-based compensation expense for these types of awards. For grants of ISOs, a tax benefit only results if the option holder has a disqualifying disposition. As a result of the limitation on the tax benefit for ISOs, the tax benefit for stock-based compensation will generally be less than the Company's overall tax rate and will vary depending on the timing of employees' exercises and sales of stock.

Stock-based compensation is measured at the grant date based on the calculated fair value of the award and is recognized as an expense on a straight-line basis over the requisite service period of the award, generally the vesting period of the grant. For additional information on stock-based compensation see note 12 - Stockholders' Equity (Deficit).

Income Taxes

Deferred tax assets and liabilities are recognized for the future tax consequences attributable to differences between the financial statement carrying amounts of existing assets and liabilities and their respective tax bases. Deferred tax assets and liabilities are measured using enacted tax rates expected to apply to taxable income in the years in which those temporary differences are expected to be recovered or settled. The effect on deferred tax assets and liabilities from a change in tax rates is recognized in income in the period that includes the enactment date.

Income tax benefits credited to equity relate to tax benefits associated with amounts that are deductible for income tax purposes but do not affect earnings. These benefits are principally generated from employee exercises of NQs, the vesting of RSUs and disqualifying dispositions of ISOs.

The threshold for recognizing the financial statement effects of a tax position is when it is more likely than not, based on the technical merits, that the position will be sustained upon examination by a taxing authority. Recognized tax positions are initially and subsequently measured as the largest amount of tax benefit that is more likely than not to be realized upon ultimate settlement with a taxing authority. Interest and penalties related to unrecognized tax benefits are included in income tax expense.

Additional information regarding the Company's unrecognized tax benefits is provided in note 11 - Income Taxes.

Fair Value Measurements

The Company's financial assets and liabilities consist of cash and cash equivalents, accounts and notes receivable, accounts payable and long-term debt. The fair value of cash and cash equivalents, accounts receivable and accounts payable approximates their carrying amounts due to the short-term nature of these assets and liabilities.

The following methods and assumptions were used by the Company in estimating fair values of its financial instruments:

- *Notes receivable* - As of August 31, 2016 and 2015, the carrying amounts of notes receivable (both current and non-current) approximate fair value due to the effect of the related allowance for doubtful accounts.
- *Long-term debt* - The Company prepares a discounted cash flow analysis for its fixed and variable rate borrowings to estimate fair value each quarter. This analysis uses Level 2 inputs from market information available for public debt transactions for companies with ratings that are similar to the Company's ratings and from information gathered from brokers who trade in the Company's notes. The fair value estimate required significant assumptions by management. Management believes this fair value is a reasonable estimate. For more information regarding the Company's long-term debt, see note 9 - Debt and note 10 - Fair Value of Financial Instruments.

Certain nonfinancial assets and liabilities are measured at fair value on a nonrecurring basis, which means these assets and liabilities are not measured at fair value on an ongoing basis but are subject to periodic impairment tests. For the Company, these items primarily include long-lived assets, goodwill and other intangible assets. Refer to sections "Accounting for Long-Lived Assets" and "Goodwill and Other Intangible Assets," discussed above, for inputs and valuation techniques used to measure the fair value of these nonfinancial assets. The fair value was based upon management's assessment as well as independent market value assessments which involved Level 2 and Level 3 inputs.

New Accounting Pronouncements

In May 2014, the Financial Accounting Standards Board ("FASB") issued ASU No. 2014-09, "Revenue from Contracts with Customers," which requires an entity to recognize revenue in an amount that reflects the consideration to which the entity expects to be entitled for the transfer of promised goods or services to customers. The standard also requires additional disclosure regarding

the nature, amount, timing and uncertainty of revenue and cash flows arising from contracts with customers. The ASU will replace most of the existing revenue recognition requirements in U.S. GAAP when it becomes effective. Further, in March 2016, the FASB issued ASU No. 2016-08, "Revenue from Contracts with Customers: Principal versus Agent Considerations (Reporting Revenue Gross versus Net)," which clarifies the guidance in ASU No. 2014-09 for evaluating when another party, along with the entity, is involved in providing a good or service to a customer. In April 2016, the FASB issued ASU No. 2016-10, "Revenue from Contracts with Customers: Identifying Performance Obligations and Licensing," which clarifies the guidance in ASU No. 2014-09 regarding assessing whether promises to transfer goods or services are distinct, and whether an entity's promise to grant a license provides a customer with a right to use or right to access the entity's intellectual property. All standards are effective for fiscal years beginning after December 15, 2017, including interim periods within that reporting period, which requires the Company to adopt the standard in fiscal year 2019. The standards are to be applied retrospectively or using a cumulative effect transition method, with early application not permitted. The Company does not believe the new revenue recognition standard will impact our recognition of sales from Company Drive-Ins and our recognition of royalty fees from franchisees. We are currently evaluating the effect that this pronouncement will have on the recognition of other transactions on the financial statements, including the initial franchise fee currently recognized upon the opening of a Franchise Drive-In, and related disclosures and have not yet selected a transition method.

In April 2015, the FASB issued ASU No. 2015-03, "Simplifying the Presentation of Debt Issuance Costs." This update requires debt issuance costs to be presented in the balance sheet as a reduction of the related liability rather than as an asset. The recognition and measurement guidance for debt issuance costs are not affected by this update. This update is effective for fiscal years beginning after December 15, 2015, including interim periods within that reporting period, and is to be applied retrospectively; early adoption is permitted. The update will be adopted in the first quarter of fiscal year 2017 and will require reclassification of debt issuance costs from other non-current assets to long-term debt within the Company's consolidated balance sheets. As of August 31, 2016, the carrying amount of unamortized debt issuance costs totaled $14.4 million. Other than this reclassification, the adoption of this ASU will not have any impact on the Company's consolidated financial statements.

In April 2015, the FASB issued ASU No. 2015-05, "Customer's Accounting for Fees Paid in a Cloud Computing Arrangement." The update provides clarification on whether a cloud computing arrangement includes a software license. If a software license is included, the customer should account for the license consistent with its accounting of other software licenses. If a software license is not included, the arrangement should be accounted for as a service contract. The update is effective for fiscal years beginning after December 15, 2015. The update will be adopted in the first quarter of fiscal year 2017 and will not have a material impact on the Company's financial statements.

In November 2015, the FASB issued ASU No. 2015-17, "Balance Sheet Classification of Deferred Taxes" as part of its simplification initiatives. The update requires that deferred tax liabilities and assets be classified as noncurrent in a classified statement of financial position. The update is effective for fiscal years beginning after December 15, 2017; however, early application is permitted. The Company adopted this standard in the first quarter of fiscal year 2016. The Company's current deferred tax asset balance of $2.2 million was classified as noncurrent and netted with noncurrent deferred tax liabilities as of November 30, 2015, and all future deferred tax asset balances will be recorded as such. No prior periods were retrospectively adjusted, as such the balance of $2.2 million remained in current assets at August 31, 2015. The reclassification did not have a material effect on our consolidated financial statements.

In February 2016, the FASB issued ASU No. 2016-02, "Leases." The new standard, which replaces existing lease guidance, requires lessees to recognize on the balance sheet a liability to make lease payments and a corresponding right-of-use asset. The guidance also requires certain qualitative and quantitative disclosures designed to assess the amount, timing and uncertainty of cash flows arising from leases. Accounting guidance for lessors is largely unchanged. The standard is effective for fiscal years beginning after December 15, 2018, which will require the Company to adopt the provisions in the first quarter of fiscal 2020, with early application permitted. This standard requires adoption based upon a modified retrospective transition approach for leases existing at, or entered into after, the beginning of the earliest comparative period presented in the financial statements, with optional practical expedients. Based on a preliminary assessment, the Company expects that most of its operating lease commitments will be subject to the new guidance and recognized as operating lease liabilities and right-of-use assets upon adoption, resulting in a significant increase in the assets and liabilities on our consolidated balance sheet. The Company is continuing its assessment, which may identify additional impacts this standard will have on its consolidated financial statements and related disclosures.

In March 2016, the FASB issued ASU No. 2016-04, "Liabilities—Extinguishments of Liabilities: Recognition of Breakage for Certain Prepaid Stored-Value Products," which is intended to eliminate current and future diversity in practice related to derecognition of prepaid stored-value product liability in a way that aligns with the new revenue recognition guidance. The update is effective for fiscal years beginning after December 15, 2017; however, early application is permitted. The adoption of the update is not expected to have a material impact on the Company's financial statements.

In March 2016, the FASB issued ASU No. 2016-09, "Compensation—Stock Compensation: Improvements to Employee Share-Based Payment Accounting," which simplifies several aspects of accounting for share-based payment transactions, including excess tax benefits, an accounting policy election for forfeitures, statutory tax withholding requirements and classification in the statements of cash flows. Upon adoption, any future excess tax benefits or deficiencies will be recorded to the provision for income taxes in the consolidated statements of operations, instead of additional paid-in capital in the consolidated balance sheets. The update is effective for fiscal years beginning after December 15, 2016; however, early application is permitted. The transition method to be applied varies depending on the area of update being adopted. The Company is currently evaluating the effect that this update will have on its financial statements and related disclosures.

In June 2016, the FASB issued ASU No. 2016-13, "Financial Instruments – Credit Losses." The update was issued to provide more decision-useful information about the expected credit losses on financial instruments. The update replaces the incurred loss impairment methodology in current GAAP with a methodology that reflects expected credit losses and requires consideration of a broader range of reasonable and supportable information to inform credit loss estimates. The update is effective for fiscal years beginning after December 15, 2019, with early adoption permitted for fiscal years beginning after December 15, 2018. The update should be adopted using a modified-retrospective approach. The Company is currently evaluating the effect that this update will have on its financial statements and related disclosures.

In August 2016, the FASB issued ASU No. 2016-15, "Statement of Cash Flows – Classification of Certain Cash Receipts and Cash Payments." The update is intended to reduce diversity in practice in how certain transactions are classified and will make eight targeted changes to how cash receipts and cash payments are presented in the statement of cash flows. The update is effective for fiscal years beginning after December 15, 2017. The new standard will require adoption on a retrospective basis unless it is impracticable to apply, in which case the amendments will apply prospectively as of the earliest date practicable. The Company is currently evaluating the effect that this update will have on its financial statements and related disclosures.

2. Earnings Per Share

The following table sets forth the computation of basic and diluted earnings per share:

	Year Ended August 31,		
	2016	**2015**	**2014**
Numerator:			
Net income	**$ 64,067**	$ 64,485	$ 47,916
Denominator:			
Weighted average common shares outstanding – basic	**48,703**	52,572	55,164
Effect of dilutive employee stock options and unvested RSUs	**966**	1,381	1,455
Weighted average common shares outstanding – diluted	**49,669**	53,953	56,619
Net income per common share – basic	**$ 1.32**	$ 1.23	$ 0.87
Net income per common share – diluted	**$ 1.29**	$ 1.20	$ 0.85
Anti-dilutive securities excluded[(1)]	**615**	342	988

(1) Anti-dilutive securities consist of stock options and unvested RSUs that were not included in the computation of diluted earnings per share because either the exercise price of the options was greater than the average market price of the common stock or the total assumed proceeds under the treasury stock method resulted in negative incremental shares and thus the inclusion would have been anti-dilutive.

3. Accounts and Notes Receivable

Accounts and notes receivable consist of the following:

	August 31,	
	2016	2015
Current Accounts and Notes Receivable:		
Royalties and other trade receivables	**$ 19,994**	$ 19,713
Notes receivable from franchisees	**5,531**	996
Receivables from system funds	**4,372**	4,965
Other	**6,507**	6,977
Accounts and notes receivable, gross	**36,404**	32,651
Allowance for doubtful accounts and notes receivable	**(967)**	(1,074)
Current accounts and notes receivable, net	**$ 35,437**	$ 31,577
Noncurrent Notes Receivable:		
Receivables from franchisees	**$ 7,170**	$ 5,676
Receivables from system funds	**5,466**	1,571
Allowance for doubtful notes receivable	**(74)**	(31)
Noncurrent notes receivable, net	**$ 12,562**	$ 7,216

The Company's receivables are primarily due from franchisees, all of whom are in the restaurant business. Substantially all of the notes receivable from franchisees are collateralized by real estate or equipment. The increase in current notes receivable from franchisees is due to short-term financing for refranchised drive-ins and newly constructed drive-ins sold to franchisees. The receivables from system funds represent transactions in the normal course of business. The increase in noncurrent receivables from system funds relates to the BTF established in the third quarter of fiscal year 2016, as discussed in note 1 – Summary of Significant Accounting Policies.

4. Goodwill and Other Intangibles

As of August 31, 2016, the Company had $76.7 million of goodwill.

The changes in the carrying amount of goodwill were as follows:

	August 31,	
	2016	2015
Balance at beginning of year	**$ 77,076**	$ 77,093
Goodwill acquired during the year	**–**	65
Goodwill disposed of related to the sale of Company Drive-Ins	**(342)**	(82)
Balance at end of year	**$ 76,734**	$ 77,076

The gross carrying amount of franchise agreements, intellectual property, franchise fees and other intangibles subject to amortization was $9.2 million and $10.4 million at August 31, 2016 and 2015, respectively. Accumulated amortization related to these intangible assets was $5.7 million and $5.9 million at August 31, 2016 and 2015, respectively. Intangible assets amortization expense was $0.9 million for each of the fiscal years ended August 31, 2016, 2015 and 2014. At August 31, 2016, the remaining weighted-average life of amortizable intangible assets was approximately 11 years. Estimated intangible assets amortization expense is $0.9 million annually for fiscal year 2017 and $0.3 million for fiscal years 2018, 2019 and 2020 and $0.2 million for fiscal year 2021.

5. Refranchising of Company Drive-Ins

During fiscal year 2016, the Company refranchised the operations of 38 Company Drive-Ins and recorded a gain of $1.8 million. The Company retained a non-controlling operating interest in 25 of these refranchised drive-ins. Gains and losses are recorded as other operating income (expenses), net on the Consolidated Statements of Income. The Company plans to refranchise other operations as part of its refranchising initiative to move toward an approximately 95%-franchised system.

6. Leases

Leasing Arrangements as a Lessor

The Company's leasing activities consist principally of leasing certain land and buildings as well as subleasing certain buildings to franchise operators. The land and building portions of all leases are classified as operating leases with lease terms expiring through August 2031. These leases include provisions for contingent rentals that may be received on the basis of a percentage of sales in excess of stipulated amounts. Income is not recognized on contingent rentals until sales exceed the stipulated amounts. Some leases contain escalation clauses over the lives of the leases. For property owned by third parties, the lease term runs concurrently with the term of the third-party lease arrangement. Most of the leases contain renewal options at the end of the initial term for periods of five years.

Future minimum rental payments receivable as of August 31, 2016, are as follows:

	Operating
Years ended August 31:	
2017	$ 7,738
2018	8,339
2019	8,890
2020	9,382
2021	8,990
Thereafter	50,709
	$ 94,048

Leasing Arrangements as a Lessee

Certain Company Drive-Ins lease land and buildings from third parties. These leases, with lease terms expiring through August 2031, include provisions for contingent rents that may be paid on the basis of a percentage of sales in excess of stipulated amounts. For the majority of leases, the land portions are classified as operating leases, and the building portions are classified as capital leases.

Future minimum rental payments required under operating leases and maturities under capital leases that have initial or remaining noncancellable lease terms in excess of one year as of August 31, 2016, are as follows:

	Operating	Capital
Years ended August 31:		
2017	$ 10,914	$ 5,051
2018	10,864	4,448
2019	10,840	3,596
2020	10,754	3,256
2021	10,030	3,134
Thereafter	63,733	7,018
Total minimum lease payments[1]	$ 117,135	26,503
Less amount representing interest averaging 6.2%		(5,439)
Present value of net minimum lease payments		21,064
Less amount due within one year		(3,673)
Amount due after one year		$ 17,391

[1] Minimum payments have not been reduced by future minimum rentals receivable under noncancellable operating and capital subleases of $16.8 million and $0.6 million, respectively. They also do not include contingent rentals which may be due under certain leases. Contingent rentals for capital leases amounted to $0.9 million, $1.0 million and $0.8 million in fiscal years 2016, 2015 and 2014, respectively.

Total rent expense for all operating leases consists of the following for the years ended August 31:

	2016	2015	2014
Minimum rentals	**$ 12,441**	$ 12,659	$ 12,449
Contingent rentals	**284**	174	161
Total rent expense	**12,725**	12,833	12,610
Less sublease rentals	**(2,372)**	(2,235)	(1,905)
Net rent expense	**$ 10,353**	$ 10,598	$ 10,705

7. Property, Equipment and Capital Leases

Property, equipment and capital leases consist of the following at August 31:

	Estimated Useful Life	2016	2015
Property, equipment and capital leases:			
Land		**$ 154,420**	$ 157,861
Buildings and improvements	8 – 25 yrs	**341,956**	343,598
Drive-In equipment	5 – 7 yrs	**132,678**	139,494
Brand technology development and other equipment	2 – 5 yrs	**110,364**	92,825
Property and equipment, at cost		**739,418**	733,778
Accumulated depreciation		**(352,390)**	(330,219)
Property and equipment, net		**387,028**	403,559
Capital leases	Life of lease	**43,991**	48,079
Accumulated amortization		**(28,857)**	(30,232)
Capital leases, net		**15,134**	17,847
Property, equipment and capital leases, net		**$ 402,162**	$ 421,406

Depreciation expense for property and equipment was $40.4 million, $41.7 million and $37.6 million for fiscal years 2016, 2015 and 2014, respectively. Land, buildings and equipment with a carrying amount of $156.6 million at August 31, 2016, were leased under operating leases to franchisees and other parties. The accumulated depreciation related to these buildings and equipment was $62.5 million at August 31, 2016. Amortization expense related to capital leases is included within "depreciation and amortization" on the Consolidated Statements of Income. As of August 31, 2016, the Company had 11 drive-ins under construction with costs to complete.

Interest incurred in connection with the construction of new drive-ins and technology projects is capitalized. Capitalized interest was $0.6 million, $0.4 million and $0.5 million for fiscal years 2016, 2015 and 2014, respectively.

8. Accrued Liabilities

Accrued liabilities consist of the following at August 31:

	2016	2015
Wages and employee benefit costs	**$ 23,416**	$ 20,501
Property taxes, sales and use taxes and employment taxes	**8,936**	9,282
Unredeemed gift cards	**10,571**	9,285
Other	**8,990**	11,646
	$ 51,913	$ 50,714

9. Debt

Long-term debt consists of the following at August 31:

	2016	2015
Class A-2 2016-1 senior secured fixed rate notes	**$ 423,938**	$ –
Class A-1 2016-1 senior secured variable funding notes	**–**	–
Class A-2 2013-1 senior secured fixed rate notes	**155,000**	155,000
Class A-2 2011-1 senior secured fixed rate notes	**–**	272,488
Class A-1 2011-1 senior secured variable funding notes	**–**	10,500
Other	**–**	40
	578,938	438,028
Less long-term debt due within one year	**(1,417)**	(9,790)
Long-term debt due after one year	**$ 577,521**	$ 428,238

At August 31, 2016, future maturities of long-term debt were $1.4 million for fiscal year 2017, no maturities for fiscal years 2018 and 2019, $155.0 million for fiscal year 2020 and no maturities for fiscal year 2021.

During fiscal year 2013, in a private transaction, various subsidiaries of the Company (the "Co-Issuers") refinanced and paid $155.0 million of the Series 2011 Senior Secured Fixed Rate Notes, Class A-2 (the "2011 Fixed Rate Notes") with the issuance of $155.0 million of Series 2013-1 Senior Secured Fixed Rate Notes, Class A-2 (the "2013 Fixed Rate Notes"), which bear interest at 3.75% per annum. The 2013 Fixed Rate Notes have an expected life of seven years, interest payable monthly, no scheduled principal amortization and an anticipated repayment date in July 2020.

On May 17, 2016, in a private transaction, the Co-Issuers issued $425.0 million of Series 2016-1 Senior Secured Fixed Rate Notes, Class A-2 (the "2016 Fixed Rate Notes"), which bear interest at 4.47% per annum. The 2016 Fixed Rate Notes have an expected life of seven years with an anticipated repayment date in May 2023.

The Co-Issuers also entered into a securitized financing facility of Series 2016-1 Senior Secured Variable Funding Notes, Class A-1 (the "2016 Variable Funding Notes" and, together with the 2016 Fixed Rate Notes, the "2016 Notes") to replace the Series 2011-1 Senior Secured Variable Funding Notes, Class A-1 (the "2011 Variable Funding Notes"). The 2016 revolving credit facility provides access to a maximum of $150.0 million of 2016 Variable Funding Notes and certain other credit instruments, including letters of credit. Interest on the 2016 Variable Funding Notes is based on the one-month London Interbank Offered Rate or Commercial Paper, depending on the funding source, plus 2.0%, per annum. An annual commitment fee of 0.5% is payable monthly on the unused portion of the 2016 Variable Funding Notes facility. The 2016 Variable Funding Notes have an expected life of five years with an anticipated repayment date in May 2021 with two one-year extension options available upon certain conditions including meeting a minimum debt service coverage ratio threshold.

Sonic used a portion of the net proceeds from the issuance of the 2016 Fixed Rate Notes to repay its existing 2011 Fixed Rate Notes and 2011 Variable Funding Notes in full and to pay the costs associated with the securitized financing transaction, including prepayment premiums.

Loan origination costs associated with the Company's 2016 transaction totaled $12.5 million and were allocated among the 2016 Notes. Loan costs are being amortized over each note's expected life, and the unamortized balance is categorized as "debt origination costs, net" on the Consolidated Balance Sheets.

In connection with the 2016 transaction described above, the Company recognized an $8.8 million loss from the early extinguishment of debt during the third quarter of fiscal year 2016, which primarily consisted of a $5.9 million prepayment premium and the $2.9 million write-off of unamortized deferred loan fees remaining from the refinanced debt.

As of August 31, 2016, the weighted-average interest cost of the 2013 Fixed Rate Notes and the 2016 Fixed Rate Notes was 4.1% and 4.8%, respectively. The weighted-average interest cost includes the effect of the loan origination costs.

While the 2013 Fixed Rate Notes and the 2016 Fixed Rate Notes are structured to provide for seven-year lives from their original issuance dates, they have legal final maturity dates of July 2043 and May 2046, respectively. The 2016 Variable Funding Notes are structured to provide for a five-year life with two one-year options available under certain conditions and with a legal final maturity date of May 2046. The Company intends to repay or refinance the 2013 Fixed Rate Notes and the 2016 Notes on or before the end of their expected lives. If the Company prepays the debt prior to the anticipated repayment date the Company may be required to pay a prepayment penalty under certain circumstances. In the event the 2013 Fixed Rate Notes and the 2016 Notes are not paid in full by the end of their expected lives, they are subject to an upward adjustment in the annual interest rate of at least 5%. In addition, principal payments will accelerate by applying all of the royalties, lease revenues and other fees securing the debt, after deducting certain expenses, until the debt is paid in full. Also, any unfunded amount under the 2016 Variable Funding Notes will become unavailable.

The Co-Issuers and Sonic Franchising LLC (the "Guarantor") are existing special purpose, bankruptcy remote, indirect subsidiaries of Sonic Corp. that hold substantially all of Sonic's franchising assets and real estate. As of August 31, 2016, assets for these combined indirect subsidiaries totaled $308.5 million, including receivables for royalties, certain Company and Franchise Drive-In real estate, intangible assets and restricted cash balances of $16.0 million. The 2013 Fixed Rate Notes and the 2016 Notes are secured by franchise fees, royalty payments and lease payments, and the repayment of the 2013 Fixed Rate Notes and the 2016 Notes is expected to be made solely from the income derived from the Co-Issuer's assets. In addition, the Guarantor, a Sonic Corp. subsidiary that acts as a franchisor, has guaranteed the obligations of the Co-Issuers under the 2013 Fixed Rate Notes and the 2016 Notes and pledged substantially all of its assets to secure those obligations.

Neither Sonic Corp., the ultimate parent of the Co-Issuers and the Guarantor, nor any other subsidiary of Sonic, guarantees or is in any way liable for the obligations of the Co-Issuers under the 2013 Fixed Rate and the 2016 Notes. The Company has, however, agreed to cause the performance of certain obligations of its subsidiaries, principally related to managing the assets included as collateral for the 2013 Fixed Rate Notes and the 2016 Notes and certain indemnity obligations relating to the transfer of the collateral assets to the Co-Issuers.

The 2013 Fixed Rate and the 2016 Notes are subject to a series of covenants and restrictions customary for transactions of this type, including (i) required actions to better secure collateral upon the occurrence of certain performance-related events, (ii) application of certain disposition proceeds as note prepayments after a set time is allowed for reinvestment, (iii) maintenance of specified reserve accounts, (iv) maintenance of certain debt service coverage ratios, (v) optional and mandatory prepayments upon change in control, (vi) indemnification payments for defective or ineffective collateral, and (vii) covenants relating to recordkeeping, access to information and similar matters. If certain covenants or restrictions are not met, the 2013 Fixed Rate Notes and the 2016 Notes are subject to customary accelerated repayment events and events of default. Although management does not anticipate an event of default or any other event of noncompliance with the provisions of the debt, if such event occurred, the unpaid amounts outstanding could become immediately due and payable.

10. Fair Value of Financial Instruments

The fair value of financial instruments is the amount at which the instrument could be exchanged in a current transaction between willing parties. The Company has no financial liabilities that are required to be measured at fair value on a recurring basis.

The Company categorizes its assets and liabilities recorded at fair value based upon the following fair value hierarchy established by FASB:

- Level 1 valuations use quoted prices in active markets for identical assets or liabilities that are accessible at the measurement date. An active market is a market in which transactions for the asset or liability occur with sufficient frequency and volume to provide pricing information on an ongoing basis.
- Level 2 valuations use inputs other than actively quoted market prices included within Level 1 that are observable for the asset or liability, either directly or indirectly. Level 2 inputs include: (a) quoted prices for similar assets or liabilities in active markets, (b) quoted prices for identical or similar assets or liabilities in markets that are not active, (c) inputs other than quoted prices that are observable for the asset or liability such as interest rates and yield curves observable at commonly quoted intervals and (d) inputs that are derived principally from or corroborated by observable market data by correlation or other means.
- Level 3 valuations use unobservable inputs for the asset or liability. Unobservable inputs are used to the extent observable inputs are not available, thereby allowing for situations in which there is little, if any, market activity for the asset or liability at the measurement date.

The Company's cash equivalents are carried at cost which approximates fair value and totaled $59.2 million and $41.1 million at August 31, 2016 and 2015, respectively. This fair value is estimated using Level 1 methods.

At August 31, 2016, the fair value of the Company's 2013 Fixed Rate Notes and 2016 Fixed Rate Notes approximated the carrying value of $579.6 million, including accrued interest. The fair value of the 2013 Fixed Rate Notes and 2016 Fixed Rate Notes is estimated using Level 2 inputs from market information available for public debt transactions for companies with ratings that are similar to the Company's ratings and from information gathered from brokers who trade in the Company's notes.

11. Income Taxes

The Company's income before the provision for income taxes is classified by source as domestic income.

The components of the provision for income taxes consist of the following for the years ended August 31:

	2016	2015	2014
Current:			
Federal	**$ 20,137**	$ 14,597	$ 16,580
State	**3,791**	3,576	3,490
	23,928	18,173	20,070
Deferred:			
Federal	**4,372**	10,592	5,328
State	**137**	(1,528)	450
	4,509	9,064	5,778
Provision for income taxes	**$ 28,437**	$ 27,237	$ 25,848

The provision for income taxes differs from the amount computed by applying the statutory federal income tax rate due to the following for the fiscal years ended August 31:

	2016	2015	2014
Amount computed by applying a tax rate of 35%	**$ 32,377**	$ 32,103	$ 25,818
State income taxes (net of federal income tax benefit)	**2,553**	1,330	2,562
Employment related and other tax credits, net	**(2,324)**	(2,096)	(1,537)
Change in uncertain tax positions	**(3,027)**	–	–
Federal tax benefit of statutory tax deduction	**–**	(4,093)	–
Other	**(1,142)**	(7)	(995)
Provision for income taxes	**$ 28,437**	$ 27,237	$ 25,848

Deferred tax assets and liabilities consist of the following at August 31:

	2016	2015
Deferred tax assets:		
Allowance for doubtful accounts and notes receivable	**$ 387**	$ 411
Leasing transactions	**3,222**	3,260
Deferred income	**2,991**	2,810
Accrued liabilities	**6,187**	5,630
Stock compensation	**2,446**	2,831
Other	**685**	541
State net operating losses	**16,303**	14,222
Total deferred tax assets	**32,221**	29,705
Valuation allowance	**(14,638)**	(12,041)
Total deferred tax assets after valuation allowance	**$ 17,583**	$ 17,664
Deferred tax liabilities:		
Prepaid expenses	**$ (1,119)**	$ (1,315)
Investment in partnerships, including differences in capitalization, depreciation and direct financing leases	**(4,125)**	(3,711)
Property, equipment and capital leases	**(31,565)**	(31,167)
Intangibles and other assets	**(21,628)**	(20,341)
Debt extinguishment	**(1,676)**	(2,515)
Total deferred tax liabilities	**(60,113)**	(59,049)
Net deferred tax liabilities	**$ (42,530)**	$ (41,385)
Net deferred tax assets and liabilities are classified as follows:		
Current	**$ –**	$ 2,164
Noncurrent	**(42,530)**	(43,549)
Total	**$ (42,530)**	$ (41,385)

State net operating loss carryforwards expire beginning in December 2016 through May 2037. Management does not believe the Company will be able to realize the state net operating loss carryforwards utilizing future income exclusive of the reversal of existing deferred tax liabilities and therefore has provided a valuation allowance of $14.6 million and $12.0 million as of August 31, 2016 and 2015, respectively.

As of August 31, 2016 and 2015, respectively, the Company had approximately $0.6 million and $3.7 million of unrecognized tax benefits, including approximately $0.3 million and $0.4 million of accrued interest and penalty. If recognized, these benefits would favorably impact the effective tax rate. The liability for unrecognized tax benefits decreased $3.0 million in fiscal year 2016. The decrease was primarily related to the favorable resolution of a federal tax audit and a statute of limitations expiration of a federal tax position. This entire change in balance impacted the Company's tax rate.

The Company recognizes estimated interest and penalties as a component of its income tax expense, net of federal benefit, as a component of "provision for income taxes" in the Consolidated Statements of Income. During the years ended August 31, 2016 and 2015, the Company recognized a net benefit of $0.1 million and net expense of $0.1 million, respectively, and negligible net expenses in fiscal year 2014.

A reconciliation of unrecognized tax benefits is as follows for fiscal years ended August 31:

	2016	2015
Balance at beginning of year	**$ 3,652**	$ 2,461
Additions based on tax positions related to the current year	**–**	254
Additions for tax positions of prior years	**725**	937
Reductions for tax positions of prior years	**(2,838)**	–
Reductions due to settlement	**(212)**	–
Reductions due to statute expiration	**(702)**	–
Balance at end of year	**$ 625**	$ 3,652

The Company or one of its subsidiaries is subject to U.S. federal income tax and income tax in multiple U.S. state jurisdictions. At August 31, 2016, the Company was subject to income tax examinations for its U.S. federal income taxes and for state and local income taxes generally after fiscal year 2012. The Company anticipates that the results of any examinations or appeals, combined with the expiration of applicable statutes of limitations and the additional accrual of interest related to unrecognized benefits on various return positions taken in years still open for examination, could result in a change to the liability for unrecognized tax benefits during the next 12 months ranging from a negligible increase to a decrease of $0.6 million depending on the timing and terms of the examination resolutions. .

12. Stockholders' Equity (Deficit)

Employee Stock Purchase Plan

The Company has an employee stock purchase plan ("ESPP") that permits eligible employees to purchase the Company's common stock at a 15% discount from the stock's fair market value. Participating employees may purchase shares of common stock each year up to the lesser of 10% of their base compensation or $25 thousand in the stock's fair market value. At August 31, 2016, 0.8 million shares were available for grant under the ESPP.

Stock-Based Compensation

The Sonic Corp. 2006 Long-Term Incentive Plan (the "2006 Plan") provides flexibility to award various forms of equity compensation, such as stock options, stock appreciation rights, performance shares, RSUs and other share-based awards. At August 31, 2016, 7.0 million shares were available for grant under the 2006 Plan. The Company grants stock options to employees with a seven-year term and a three-year vesting period and grants RSUs to employees with a minimum vesting period of three years. The Company grants stock options to its Board of Directors with a seven-year term and one-year vesting period and also grants RSUs to its Board of Directors that vest over one year. The Company's policy is to issue shares from treasury stock to satisfy stock option exercises, the vesting of RSUs and shares issued under the ESPP.

Total stock-based compensation cost recognized for fiscal years 2016, 2015 and 2014 was $3.8 million, $3.5 million and $3.7 million, respectively, net of related income tax benefits of $1.2 million, $1.0 million and $1.7 million, respectively. At August 31, 2016, the total remaining unrecognized compensation cost related to unvested stock-based arrangements was $7.1 million and is expected to be recognized over a weighted average period of 2.0 years.

The Company measures the compensation cost associated with stock option-based payments by estimating the fair value of stock options as of the grant date using the Black-Scholes option pricing model. The Company believes the valuation technique and approach utilized to develop the underlying assumptions are appropriate in calculating the fair values of the Company's stock options granted during fiscal years 2016, 2015 and 2014. Estimates of fair value are not intended to predict actual future events or the value ultimately realized by the employees who receive equity awards. The fair value of RSUs granted is equal to the Company's closing stock price on the date of the grant.

The per share weighted average fair value of stock options granted during 2016, 2015 and 2014 was $8.23, $8.83 and $6.82, respectively. In addition to the exercise and grant date prices of the awards, certain weighted average assumptions that were used to estimate the fair value of stock option grants in the respective periods are listed in the table below:

	2016	**2015**	**2014**
Expected term (years)	**5.3**	5.0	4.7
Expected volatility	**34%**	34%	37%
Risk-free interest rate	**1.4%**	1.3%	1.5%
Expected dividend yield	**1.5%**	1.2%	–%

The Company estimates expected volatility based on historical daily price changes of the Company's common stock for a period equal to the current expected term of the options. The risk-free interest rate is based on the U.S. treasury yields in effect at the time of grant corresponding with the expected term of the options. The expected option term is the number of years the Company estimates that options will be outstanding prior to exercise considering vesting schedules and historical exercise patterns.

Stock Options

A summary of stock option activity under the Company's stock-based compensation plans for the year ended August 31, 2016, is presented in the following table:

	Options	**Weighted Average Exercise Price**	**Weighted Average Remaining Contractual Life (Yrs.)**	**Aggregate Intrinsic Value**
Outstanding September 1, 2015	**2,873**	**$ 14.00**		
Granted	**494**	**29.28**		
Exercised	**(976)**	**10.49**		
Forfeited or expired	**(57)**	**27.51**		
Outstanding at August 31, 2016	**2,334**	**$ 18.37**	**3.90**	**$ 25,279**
Exercisable at August 31, 2016	**1,548**	**$ 13.23**	**2.89**	**$ 24,304**

Proceeds from the exercise of stock options for fiscal years 2016, 2015 and 2014 were $3.8 million, $18.7 million and $17.4 million, respectively. The total intrinsic value of options exercised during the years ended August 31, 2016, 2015 and 2014 was $18.9 million, 21.8 million and $13.0 million, respectively.

Restricted Stock Units

A summary of the Company's RSU activity during the year ended August 31, 2016 is presented in the following table:

	Restricted Stock Units	**Weighted Average Grant Date Fair Value**
Outstanding September 1, 2015	**66**	**$ 28.49**
Granted	**51**	**28.07**
Vested	**(13)**	**31.32**
Forfeited	**(12)**	**31.69**
Outstanding at August 31, 2016	**92**	**$ 28.90**

The aggregate fair value of RSUs that vested was $0.4 million during the fiscal year ended August 31, 2016 and $1.1 million during the fiscal years ended August 31, 2015 and 2014.

Stock Repurchase Programs

In August 2014, the Board of Directors extended the Company's share repurchase program, authorizing the Company to purchase up to $105.0 million of its outstanding shares of common stock beginning September 1, 2014 through August 31, 2015. In October 2014, the Company entered into an accelerated share repurchase ("ASR") agreement with a financial institution to purchase $15.0 million of the Company's common stock. In exchange for a $15.0 million up-front payment, the financial institution delivered approximately 0.6 million shares. During January 2015, the ASR purchase period concluded. The Company paid an additional $0.1 million with no additional shares delivered, resulting in an average price per share of $26.32. In February 2015, the Company entered into additional ASR agreements with a financial institution to purchase $75.0 million of the Company's common stock. In exchange for a $75.0 million up-front payment, the financial institution delivered approximately 2.1 million shares. The ASR transactions completed in July 2015 with 0.3 million additional shares delivered, resulting in an average price per share of $31.38. The Company reflected the ASR transactions as a repurchase of common stock for purposes of calculating earnings per share and as a forward contract indexed to its own common stock. The forward contract met all of the applicable criteria for equity classification. Including shares repurchased through the ASR transactions described above, during the fiscal year 2015, approximately 4.2 million shares were repurchased for a total cost of $123.8 million, resulting in an average price per share of $29.46.

In August 2015, the Board of Directors extended the Company's share repurchase program, authorizing the Company to purchase up to $145.0 million of its outstanding shares of common stock through August 31, 2016. The Board of Directors further extended the share repurchase program effective May 2016, authorizing the purchase of up to an additional $155.0 million of our outstanding shares of common stock through August 31, 2017. During fiscal year 2016, approximately 5.2 million shares were repurchased for a total cost of $148.3 million, resulting in an average price per share of $28.48. The total remaining amount authorized under the share repurchase program, as of August 31, 2016, was $132.9 million.

Share repurchases will be made from time to time in the open market or otherwise, including through an ASR transaction, under the terms of a Rule 10b5-1 plan, in privately negotiated transactions or in round lot or block transactions. The share repurchase program may be extended, modified, suspended or discontinued at any time. We plan to fund the share repurchase program from existing cash on hand at August 31, 2016, cash flows from operations and borrowings under our 2016 Variable Funding Notes.

Dividends

In August 2014, the Company initiated a quarterly cash dividend program and paid a quarterly dividend of $0.09 per share of common stock, totaling $18.8 million for fiscal year 2015, and paid a quarterly dividend of $0.11 per share of common stock, totaling $21.3 million for fiscal year 2016. Subsequent to the end of fiscal year 2016, the Company declared a quarterly dividend of $0.14 per share of common stock to be paid to stockholders of record as of the close of business on November 9, 2016, with a payment date of November 18, 2016. The future declaration of quarterly dividends and the establishment of future record and payment dates are subject to the final determination of the Company's Board of Directors.

13. Employee Benefit and Cash Incentive Plans

The Company sponsors a qualified defined contribution 401(k) plan for employees meeting certain eligibility requirements. Under the plan, employees are entitled to make pre-tax contributions. The Company matches an amount equal to the employee's contributions up to a maximum of 6% of the employee's salaries depending on years of service. The Company's contributions during fiscal years 2016, 2015 and 2014 were $1.8 million, $1.6 million and $1.3 million, respectively.

The Company has short-term and long-term cash incentive plans (the "Incentive Plans") that apply to certain employees, and grants of awards under the Incentive Plans are at all times subject to the approval of the Company's Board of Directors. Under certain awards pursuant to the Incentive Plans, if predetermined earnings goals are met, a predetermined percentage of the employee's salary may be paid in the form of a bonus. The Company recognized as expense incentive bonuses of $13.4 million, $12.4 million and $9.5 million during fiscal years 2016, 2015 and 2014, respectively.

14. Commitments and Contingencies

Litigation

The Company is involved in various legal proceedings and has certain unresolved claims pending. Based on the information currently available, management believes that all claims currently pending are either covered by insurance or would not have a material adverse effect on the Company's business, operating results or financial condition.

Note Repurchase Agreement

On December 20, 2013, the Company extended a note purchase agreement to a bank that serves to guarantee the repayment of a franchisee loan, with a term through 2018, and also benefits the franchisee with a lower financing rate. In the event of default by the franchisee, the Company would purchase the franchisee loan from the bank, thereby becoming the note holder and providing an avenue of recourse with the franchisee. The Company recorded a liability for this guarantee which was based on the Company's estimate of fair value. As of August 31, 2016, the balance of the franchisee's loan was $5.8 million.

Lease Commitments

The Company has obligations under various operating lease agreements with third-party lessors related to the real estate for certain Company Drive-In operations that were sold to franchisees. Under these agreements, which expire through 2029, the Company remains secondarily liable for the lease payments for which it was responsible as the original lessee. As of August 31, 2016, the amount remaining under these guaranteed lease obligations totaled $7.4 million. At this time, the Company does not anticipate any material defaults under the foregoing leases; therefore, no liability has been provided.

Purchase Obligations

At August 31, 2016, the Company had purchase obligations of approximately $235.8 million which primarily related to its estimated share of system-wide commitments for food products. The Company has excluded agreements that are cancelable without penalty.

15. Selected Quarterly Financial Data (Unaudited)

	First Quarter		Second Quarter		Third Quarter		Fourth Quarter	
	2016	**2015**	**2016**	**2015**	**2016**	**2015**	**2016**	**2015**
Total revenues	**$ 145,803**	$ 139,856	**$ 133,160**	$ 126,219	**$ 165,239**	$ 164,748	**$ 162,118**	$ 175,266
Income from operations	**26,045**	22,538	**22,212**	16,991	**38,880**	36,370	**40,315**	40,529
Net income[1]	**$ 12,458**	$ 10,085	**$ 10,819**	$ 7,662	**$ 15,353**	$ 20,442	**$ 25,437**	$ 26,296
Basic income per share[2]	**$ 0.25**	$ 0.19	**$ 0.22**	$ 0.14	**$ 0.32**	$ 0.39	**$ 0.54**	$ 0.51
Diluted income per share[2]	**$ 0.24**	$ 0.18	**$ 0.22**	$ 0.14	**$ 0.31**	$ 0.38	**$ 0.53**	$ 0.50

(1) For fiscal year 2016, includes the after tax gain on the sale of real estate of $1.2 million and a tax benefit of $0.6 million from the retroactive reinstatement of the Work Opportunity Tax Credit and resolution of income tax matters in the second quarter, the $5.7 million after tax loss from early extinguishment of debt in the third quarter and the after tax gain on the sale of Company Drive-Ins of $0.7 million and the FIN 48 release of income tax credits and deductions of $3.0 million in the fourth quarter. For fiscal year 2015, includes a tax benefit of $0.7 million from the retroactive reinstatement of the Work Opportunity Tax Credit and resolution of income tax matters in the second quarter, a federal tax benefit of $1.7 million from the recognition of a prior-year statutory tax deduction and a tax expense of $0.6 million from the retroactive effect of federal tax law change during the third quarter and a federal tax benefit of $1.5 million from the recognition of a prior-year statutory tax deduction and $1.7 million from a change in deferred tax valuation allowance during the fourth quarter.

(2) The sum of per share data may not agree to annual amounts due to rounding.

Report of Independent Registered Public Accounting Firm

The Board of Directors and Stockholders
Sonic Corp.:

We have audited the accompanying consolidated balance sheets of Sonic Corp. and subsidiaries as of August 31, 2016 and 2015, and the related consolidated statements of income, stockholders' equity (deficit), and cash flows for each of the years in the three-year period ended August 31, 2016. These consolidated financial statements and the financial statement schedule are the responsibility of the Company's management. Our responsibility is to express an opinion on these consolidated financial statements and the financial statement schedule based on our audits.

We conducted our audits in accordance with the standards of the Public Company Accounting Oversight Board (United States). Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements. An audit also includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation. We believe that our audits provide a reasonable basis for our opinion.

In our opinion, the consolidated financial statements referred to above present fairly, in all material respects, the financial position of Sonic Corp. and subsidiaries as of August 31, 2016 and 2015, and the results of their operations and their cash flows for each of the years in the three-year period ended August 31, 2016, in conformity with U.S. generally accepted accounting principles. Also, in our opinion, the related financial statement schedule, when considered in relation to the basic consolidated financial statements taken as a whole, presents fairly, in all material respects, the information set forth therein.

We also have audited, in accordance with the standards of the Public Company Accounting Oversight Board (United States), Sonic Corp.'s internal control over financial reporting as of August 31, 2016, based on criteria established in Internal Control – Integrated Framework (2013) issued by the Committee of Sponsoring Organizations of the Treadway Commission (COSO), and our report dated October 31, 2016, expressed an unqualified opinion on the effectiveness of Sonic Corp.'s internal control over financial reporting.

(signed) KPMG LLP

Oklahoma City, Oklahoma
October 31, 2016

Management's Report on Internal Control Over Financial Reporting

The management of the Company is responsible for establishing and maintaining adequate internal control over financial reporting. The Company's internal control system was designed to provide reasonable assurance to the Company's management and Board of Directors regarding the preparation and fair presentation of published financial statements. All internal control systems, no matter how well designed, have inherent limitations. Therefore, even those systems determined to be effective can provide only reasonable assurance with respect to financial statement preparation and presentation.

The Company's management assessed the effectiveness of the Company's internal control over financial reporting as of August 31, 2016. In making this assessment, it used the criteria set forth by the Committee of Sponsoring Organizations of the Treadway Commission in Internal Control - Integrated Framework - 2013. Based on our assessment, we believe that, as of August 31, 2016, the Company's internal control over financial reporting is effective based on those criteria.

The Company's independent registered public accounting firm that audited the 2016 financial statements included in this annual report has issued an attestation report on the Company's internal control over financial reporting. The report appears on the following page.

Report of Independent Registered Public Accounting Firm

The Board of Directors and Stockholders
Sonic Corp.:

We have audited Sonic Corp.'s internal control over financial reporting as of August 31, 2016, based on criteria established in Internal Control – Integrated Framework (2013) issued by the Committee of Sponsoring Organizations of the Treadway Commission (COSO). Sonic Corp.'s management is responsible for maintaining effective internal control over financial reporting and for its assessment of the effectiveness of internal control over financial reporting, included in the accompanying Management's Report on Internal Control over Financial Reporting. Our responsibility is to express an opinion on Sonic Corp.'s internal control over financial reporting based on our audit.

We conducted our audit in accordance with the standards of the Public Company Accounting Oversight Board (United States). Those standards require that we plan and perform the audit to obtain reasonable assurance about whether effective internal control over financial reporting was maintained in all material respects. Our audit included obtaining an understanding of internal control over financial reporting, assessing the risk that a material weakness exists, and testing and evaluating the design and operating effectiveness of internal control based on the assessed risk. Our audit also included performing such other procedures as we considered necessary in the circumstances. We believe that our audit provides a reasonable basis for our opinion.

A company's internal control over financial reporting is a process designed to provide reasonable assurance regarding the reliability of financial reporting and the preparation of financial statements for external purposes in accordance with generally accepted accounting principles. A company's internal control over financial reporting includes those policies and procedures that (1) pertain to the maintenance of records that, in reasonable detail, accurately and fairly reflect the transactions and dispositions of the assets of the company; (2) provide reasonable assurance that transactions are recorded as necessary to permit preparation of financial statements in accordance with generally accepted accounting principles, and that receipts and expenditures of the company are being made only in accordance with authorizations of management and directors of the company; and (3) provide reasonable assurance regarding prevention or timely detection of unauthorized acquisition, use, or disposition of the company's assets that could have a material effect on the financial statements.

Because of its inherent limitations, internal control over financial reporting may not prevent or detect misstatements. Also, projections of any evaluation of effectiveness to future periods are subject to the risk that controls may become inadequate because of changes in conditions, or that the degree of compliance with the policies or procedures may deteriorate.

In our opinion, Sonic Corp. maintained, in all material respects, effective internal control over financial reporting as of August 31, 2016, based on criteria established in Internal Control – Integrated Framework (2013) issued by COSO.

We also have audited, in accordance with the standards of the Public Company Accounting Oversight Board (United States), the consolidated balance sheets of Sonic Corp. and subsidiaries as of August 31, 2016 and 2015 and the related consolidated statements of income, stockholders' equity (deficit), and cash flows for each of the years in the three-year period ended August 31, 2016, and our report dated October 31, 2016 expressed an unqualified opinion on those consolidated financial statements.

(signed) KPMG LLP

Oklahoma City, Oklahoma
October 31, 2016

Directors and Officers

Board of Directors

Clifford Hudson
Chairman and Chief Executive Officer
Sonic Corp.

Tony D. Bartel [2]
Chief Operating Officer
GameStop Corp.

R. Neal Black [3]
Former Chief Executive Officer
and President
Jos. A. Bank Clothiers, Inc.

Lauren R. Hobart [3]
Executive Vice President
and Chief Marketing Officer
Dick's Sporting Goods, Inc.

Kate S. Lavelle [1, 2]
Former Executive Vice President
and Chief Financial Officer
Dunkin' Brands, Inc.

J. Larry Nichols [1, 2, 4]
Chairman Emeritus
Devon Energy Corporation

Federico F. Peña [1, 3]
Senior Advisor
Colorado Impact Fund

Frank E. Richardson [1, 2]
Chairman
F. E. Richardson & Co., Inc.

Jeffrey H. Schutz [1, 3]
Managing Director
Centennial Ventures

Kathryn L. Taylor [2]
Leadership Council Chair
Impact Tulsa

Susan E. Thronson [3]
Former Senior Vice President,
Global Marketing
Marriott International, Inc.

[1] Member of the Nominating and Corporate Governance Committee
[2] Member of the Audit Committee
[3] Member of the Compensation Committee
[4] Lead Independent Director

Officers

Clifford Hudson
Chairman and Chief Executive Officer

Todd W. Smith
President and Chief Marketing Officer

Claudia S. San Pedro
Executive Vice President
and Chief Financial Officer

John H. Budd III
Executive Vice President and
Chief Development and Strategy Officer

Harold A. Ceron
President of Sonic Restaurants, Inc.
(the Company's restaurant-operating
subsidiary)

Paige S. Bass
Senior Vice President and General Counsel

Andrew G. Ritger, Jr.
Senior Vice President of Development

E. Edward Saroch
Senior Vice President of Franchise Relations

Anita K. Vanderveer
Senior Vice President of People

David Abney
Vice President of Quality Assurance

Lori I. Abou-Habib
Vice President of Local Relationship Marketing

Larry G. Archibald
Vice President of Brand Technology

Justin W. Ashby
Vice President of Design and Construction

Tanishia M. Beacham
Vice President of Franchise Operations

Sarah E. Beddoe
Vice President of National Marketing

K. Wayne Brayton
Vice President of Facilities

Michelle E. Britten
Vice President and
Chief Accounting Officer

R. Douglas Cook
Vice President of Enterprise Architecture
and Integration

Carolyn C. Cummins
Vice President of Compliance
and Corporate Secretary

Mark W. Davis
Vice President of Cybersecurity
and Enterprise Systems

Jon C. Dorch
Vice President of Integrated
Customer Engagement

John J. Doyle
Vice President of Retail Systems Management

Christopher R. Graves
Vice President and Real Estate Counsel

Jacques A. Grondin
Vice President of New Franchisees

Rochelle L. Guinn
Vice President of Human Resources
Compliance and Technology

Lisa Hammond
Vice President of Program Management Office

Ralph F. Heim
Vice President of Media
and Integrated Marketing

Corey R. Horsch
Vice President of Investor Relations
and Treasurer

M. Anne Hughes
Vice President of Internal Audit

Bobby L. Jones
Vice President of POS Implementation

Johnny D. Jones
Vice President of Development
and Real Estate

William I. Klearman
Vice President of Retail Technology

Robert D. Moorhead
Vice President of CRM Loyalty
and Brand Insights

Diane L. Prem
Vice President of Operations Services

Matthew J. Schein
Vice President of Operations Technology

Jeffrey D. Semler
Vice President of Customer Experience

Dail A. Smith
Vice President of Operations
Sonic Restaurants, Inc.

C. Nelson Taylor
Vice President of Food Safety
and Equipment

Scott B. Uehlein
Vice President of Product Innovation
and Development

Michele A. Varian
Vice President of Supply Chain and Purchasing

Christina D. Vaughan
Vice President of Franchise Operations

Barbara A. Williams
Vice President of Performance Analysis

Charles B. Woods
Vice President of Tax

Christine O. Woodworth
Vice President of Public Relations

Corporate Information

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Oklahoma City, Oklahoma 73104
405-225-5000

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www.sonicdrivein.com

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Computershare
211 Quality Circle, Suite 210
College Station, Texas 77845, United States
800-884-4225
web.queries@computershare.com
www.computershare.com/investor

Independent Registered Public Accounting Firm
KPMG LLP
Oklahoma City, Oklahoma

Annual Meeting
Our 2017 Annual Meeting of Shareholders will be held at 1:30 p.m. Central Standard Time on January 19, 2017, at our corporate offices, 4th Floor, 300 Johnny Bench Drive, Oklahoma City, Oklahoma.

Annual Report on Form 10-K
A copy of our annual report on Form 10-K for the year ended August 31, 2016, as filed with the Securities and Exchange Commission ("SEC"), may be obtained without charge upon written request to Claudia S. San Pedro, Executive Vice President and Chief Financial Officer, at our corporate offices. In addition, we make available free of charge through our website at sonicdrivein.com annual reports on Form 10-K, quarterly reports on Form 10-Q, current reports on Form 8-K and all amendments to those reports filed with or furnished to the SEC. The reports are available as soon as reasonably practical after we electronically file such material with the SEC, and may be found on our website under "Investors."

Forward-Looking Statements
This annual report contains forward-looking statements within the meaning of the federal securities laws. Forward-looking statements reflect management's expectations regarding future events and operating performance and speak only as of the date thereof. These forward-looking statements involve a number of risks and uncertainties. Factors that could cause actual results to differ materially from those expressed in, or underlying, these forward-looking statements are detailed in the Company's annual and quarterly report filings with the SEC. The Company undertakes no obligation to publicly release revisions to these forward-looking statements to reflect events or circumstances after the date hereof or to reflect the occurrence of unforeseen events, except as required to be reported under the rules and regulations of the SEC.

Stock Market Information
Our common stock trades on the NASDAQ Global Select Market under the symbol SONC. At November 21, 2016, we had approximately 22,500 shareholders, including beneficial owners holding shares in nominee or "street" name.

The table below sets forth our high and low sales prices for the Company's common stock and cash dividends paid during each fiscal quarter within the two most recent fiscal years.

Fiscal Year Ended August 31, 2016

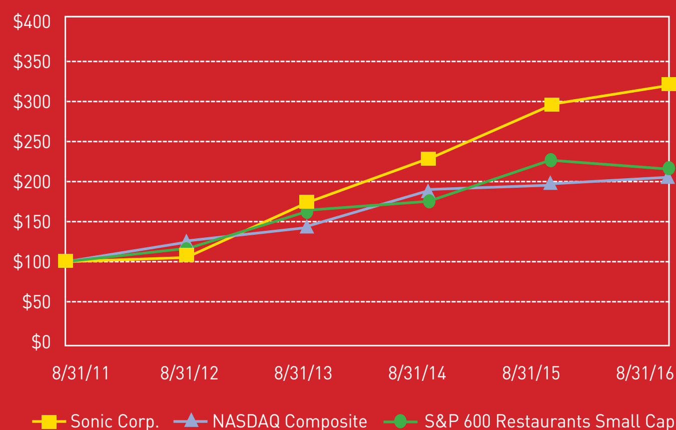
	High	Low	Dividends Per Common Share
First Quarter	$ 29.99	$ 22.72	$ 0.11
Second Quarter	$ 33.18	$ 24.91	$ 0.11
Third Quarter	$ 36.34	$ 28.80	$ 0.11
Fourth Quarter	$ 30.91	$ 26.17	$ 0.11

Fiscal Year Ended August 31, 2015

	High	Low	Dividends Per Common Share
First Quarter	$ 27.88	$ 21.10	$ 0.09
Second Quarter	$ 33.15	$ 25.91	$ 0.09
Third Quarter	$ 36.73	$ 28.53	$ 0.09
Fourth Quarter	$ 34.23	$ 24.86	$ 0.09

During the fourth quarter of 2014, the Company initiated a cash dividend program, and a quarterly dividend of $0.09 per common share was paid during fiscal year 2015. The Company increased the quarterly rate to $0.11 per common share effective with the payment made in the first quarter of fiscal year 2016. The Company again increased the quarterly rate to $0.14 per common share effective with the payment made in the first quarter of fiscal year 2017. Future payments of dividends will be considered by the Company's Board of Directors after reviewing, among other factors, returns to shareholders, profitability expectations and financing needs.

Comparison of Five-Year Cumulative Total Return
The graph below matches Sonic Corp.'s cumulative five-year total return on common stock with the cumulative total returns of the NASDAQ Composite index and the S&P 600 Restaurants Small Cap index. The graph tracks the performance of a $100 investment in our common stock and in each index (with the reinvestment of all dividends) from 8/31/2011 to 8/31/2016.



The Future of Sonic Drive-In looks amazing, right?

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Oklahoma City, OK 73104

sonicdrivein.com