

BIG 5 SPORTING GOODS Corp  
Form 10-Q  
October 29, 2014  
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**UNITED STATES**  
**SECURITIES AND EXCHANGE COMMISSION**  
**WASHINGTON, DC 20549**

**FORM 10-Q**

(Mark One)

☒ **QUARTERLY REPORT UNDER SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934**

**For the quarterly period ended September 28, 2014**

**OR**

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

**For the transition period from \_\_\_\_\_ to \_\_\_\_\_**

**Commission file number: 000-49850**

**BIG 5 SPORTING GOODS CORPORATION**  
**(Exact name of registrant as specified in its charter)**

**Delaware**  
**(State or Other Jurisdiction of Incorporation or**  
**Organization)**

**95-4388794**  
**(I.R.S. Employer Identification No.)**

**2525 East El Segundo Boulevard**

**El Segundo, California**  
**(Address of Principal Executive Offices)**

**90245**  
**(Zip Code)**

**Registrant's telephone number, including area code: (310) 536-0611**

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

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

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

Large accelerated filer ☐ Accelerated filer ☒

Non-accelerated filer ☐ (Do not check if a smaller reporting company) Smaller reporting company ☐

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

There were 22,173,745 shares of common stock, with a par value of \$0.01 per share outstanding as of October 22, 2014.

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**Table of Contents****PART I. FINANCIAL INFORMATION****Item 1. Financial Statements****BIG 5 SPORTING GOODS CORPORATION****UNAUDITED CONDENSED CONSOLIDATED BALANCE SHEETS**

(In thousands, except share amounts)

	<b>September 28, 2014</b>	<b>December 29, 2013</b>
<b>ASSETS</b>		
Current assets:		
Cash	\$ 5,641	\$ 9,400
Accounts receivable, net of allowances of \$132 and \$105, respectively	9,381	16,301
Merchandise inventories, net	307,526	300,952
Prepaid expenses	6,159	6,356
Deferred income taxes	9,855	12,000
Total current assets	338,562	345,009
Property and equipment, net	75,524	75,608
Deferred income taxes	15,671	13,564
Other assets, net of accumulated amortization of \$1,023 and \$891, respectively	3,205	3,274
Goodwill	4,433	4,433
Total assets	\$ 437,395	\$ 441,888
<b>LIABILITIES AND STOCKHOLDERS' EQUITY</b>		
Current liabilities:		
Accounts payable	\$ 93,857	\$ 104,826
Accrued expenses	61,376	69,923
Current portion of capital lease obligations	1,335	1,567
Total current liabilities	156,568	176,316
Deferred rent, less current portion	20,681	21,078
Capital lease obligations, less current portion	1,372	1,595
Long-term debt	55,381	43,018
Other long-term liabilities	9,341	9,111
Total liabilities	243,343	251,118
Commitments and contingencies		
Stockholders' equity:		

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Common stock, \$0.01 par value, authorized 50,000,000 shares; issued 24,438,505 and 24,339,537 shares, respectively; outstanding 22,190,945 and 22,297,701 shares, respectively	245	244
Additional paid-in capital	110,184	109,901
Retained earnings	111,927	106,565
Less: Treasury stock, at cost; 2,247,560 and 2,041,836 shares, respectively	(28,304)	(25,940)
Total stockholders' equity	194,052	190,770
Total liabilities and stockholders' equity	\$ 437,395	\$ 441,888

See accompanying notes to unaudited condensed consolidated financial statements.

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**Table of Contents****BIG 5 SPORTING GOODS CORPORATION****UNAUDITED CONDENSED CONSOLIDATED STATEMENTS OF OPERATIONS**

(In thousands, except per share data)

	<b>13 Weeks Ended</b>		<b>39 Weeks Ended</b>	
	<b>September 28,</b>	<b>September 29,</b>	<b>September 28,</b>	<b>September 29,</b>
	<b>2014</b>	<b>2013</b>	<b>2014</b>	<b>2013</b>
Net sales	\$ 265,115	\$ 259,121	\$ 727,528	\$ 745,286
Cost of sales	179,055	171,331	493,217	497,348
Gross profit	86,060	87,790	234,311	247,938
Selling and administrative expense	73,842	72,432	213,892	209,540
Operating income	12,218	15,358	20,419	38,398
Interest expense	386	395	1,191	1,266
Income before income taxes	11,832	14,963	19,228	37,132
Income taxes	4,366	5,825	7,167	14,376
Net income	\$ 7,466	\$ 9,138	\$ 12,061	\$ 22,756
Earnings per share:				
Basic	\$ 0.34	\$ 0.42	\$ 0.55	\$ 1.05
Diluted	\$ 0.34	\$ 0.41	\$ 0.54	\$ 1.03
Dividends per share	\$ 0.10	\$ 0.10	\$ 0.30	\$ 0.30
Weighted-average shares of common stock outstanding:				
Basic	21,926	21,933	21,964	21,700
Diluted	22,038	22,231	22,163	22,032

See accompanying notes to unaudited condensed consolidated financial statements.

**Table of Contents****BIG 5 SPORTING GOODS CORPORATION****UNAUDITED CONDENSED CONSOLIDATED STATEMENTS OF STOCKHOLDERS' EQUITY**

(In thousands, except share amounts)

	<b>Common Stock Shares</b>	<b>Common Stock Amount</b>	<b>Additional Paid-In Capital</b>	<b>Retained Earnings</b>	<b>Treasury Stock, At Cost</b>	<b>Total</b>
Balance as of December 30, 2012	21,741,248	\$ 238	\$ 102,658	\$ 87,464	\$ (25,940)	\$ 164,420
Net income				22,756		22,756
Dividends on common stock (\$0.30 per share)				(6,616)		(6,616)
Issuance of nonvested share awards	127,020	1	(1)			
Exercise of share option awards	474,345	5	4,520			4,525
Share-based compensation			1,394			1,394
Tax benefit from share-based awards activity			1,446			1,446
Forfeiture of nonvested share awards	(9,695)					
Retirement of common stock for payment of withholding tax	(41,812)		(641)			(641)
Balance as of September 29, 2013	22,291,106	\$ 244	\$ 109,376	\$ 103,604	\$ (25,940)	\$ 187,284
Balance as of December 29, 2013	22,297,701	\$ 244	\$ 109,901	\$ 106,565	\$ (25,940)	\$ 190,770
Net income				12,061		12,061
Dividends on common stock (\$0.30 per share)				(6,699)		(6,699)
Issuance of nonvested share awards	152,920	2	(2)			
Exercise of share option awards	10,525		63			63
Share-based compensation			1,451			1,451
Tax deficiency from share-based awards activity			(421)			(421)
Forfeiture of nonvested share awards	(11,550)					
Retirement of common stock for payment of withholding tax	(52,927)	(1)	(808)			(809)
Purchases of treasury stock	(205,724)				(2,364)	(2,364)
Balance as of September 28, 2014	22,190,945	\$ 245	\$ 110,184	\$ 111,927	\$ (28,304)	\$ 194,052

See accompanying notes to unaudited condensed consolidated financial statements.

**Table of Contents****BIG 5 SPORTING GOODS CORPORATION****UNAUDITED CONDENSED CONSOLIDATED STATEMENTS OF CASH FLOWS**

(In thousands)

	<b>39 Weeks Ended</b>	
	<b>September 28, 2014</b>	<b>September 29, 2013</b>
Cash flows from operating activities:		
Net income	\$ 12,061	\$ 22,756
Adjustments to reconcile net income to net cash provided by operating activities:		
Depreciation and amortization	15,947	14,890
Impairment of store assets	756	72
Share-based compensation	1,451	1,394
Excess tax benefit related to share-based awards	(184)	(1,708)
Amortization of debt issuance costs	132	190
Deferred income taxes	38	(237)
Changes in operating assets and liabilities:		
Accounts receivable, net	6,920	3,899
Merchandise inventories, net	(6,574)	(17,589)
Prepaid expenses and other assets	134	(341)
Accounts payable	4,558	6,690
Accrued expenses and other long-term liabilities	(10,157)	(4,837)
Net cash provided by operating activities	25,082	25,179
Cash flows from investing activities:		
Purchases of property and equipment	(14,727)	(12,597)
Proceeds from solar energy rebate	100	
Net cash used in investing activities	(14,627)	(12,597)
Cash flows from financing activities:		
Principal borrowings under revolving credit facility	149,649	176,602
Principal payments under revolving credit facility	(137,286)	(186,124)
Changes in book overdraft	(15,733)	(3,334)
Principal payments under capital lease obligations	(1,233)	(1,352)
Proceeds from exercise of share option awards	63	4,525
Excess tax benefit related to share-based awards	184	1,708
Purchases of treasury stock	(2,345)	(75)
Tax withholding payments for share-based compensation	(809)	(641)
Dividends paid	(6,704)	(6,595)
Net cash used in financing activities	(14,214)	(15,286)



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Net decrease in cash	(3,759)	(2,704)
Cash at beginning of period	9,400	7,635
Cash at end of period	\$ 5,641	\$ 4,931
Supplemental disclosures of non-cash investing and financing activities:		
Property and equipment acquired under capital leases	\$ 792	\$ 392
Property and equipment additions unpaid	\$ 4,077	\$ 4,948
Supplemental disclosures of cash flow information:		
Interest paid	\$ 1,096	\$ 1,070
Income taxes paid	\$ 4,558	\$ 12,122

See accompanying notes to unaudited condensed consolidated financial statements.

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**BIG 5 SPORTING GOODS CORPORATION**

**NOTES TO UNAUDITED CONDENSED CONSOLIDATED FINANCIAL STATEMENTS**

**(1) Description of Business**

*Business*

Big 5 Sporting Goods Corporation (the Company) is a leading sporting goods retailer in the western United States, operating 429 stores in 12 states as of September 28, 2014. The Company provides a full-line product offering in a traditional sporting goods store format that averages approximately 11,000 square feet. The Company's product mix includes athletic shoes, apparel and accessories, as well as a broad selection of outdoor and athletic equipment for team sports, fitness, camping, hunting, fishing, tennis, golf, winter and summer recreation and roller sports. The Company is a holding company that operates as one reportable segment through Big 5 Corp., its wholly-owned subsidiary, and Big 5 Services Corp., which is a wholly-owned subsidiary of Big 5 Corp. Big 5 Services Corp. provides a centralized operation for the issuance and administration of gift cards.

The accompanying interim unaudited condensed consolidated financial statements (Interim Financial Statements) of the Company and its wholly-owned subsidiaries have been prepared in accordance with accounting principles generally accepted in the United States of America (GAAP) for interim financial information and are presented in accordance with the requirements of Form 10-Q and Rule 10-01 of Regulation S-X. Accordingly, these Interim Financial Statements do not include all of the information and notes required by GAAP for complete financial statements. These Interim Financial Statements should be read in conjunction with the consolidated financial statements and notes thereto for the fiscal year ended December 29, 2013 included in the Company's Annual Report on Form 10-K. In the opinion of management, the Interim Financial Statements included herein contain all adjustments, including normal recurring adjustments, considered necessary to present fairly the Company's financial position, the results of operations and cash flows for the periods presented.

The operating results and cash flows of the interim periods presented herein are not necessarily indicative of the results to be expected for any other interim period or the full year.

**(2) Summary of Significant Accounting Policies**

*Consolidation*

The accompanying Interim Financial Statements include the accounts of Big 5 Sporting Goods Corporation, Big 5 Corp. and Big 5 Services Corp. Intercompany balances and transactions have been eliminated in consolidation.

*Reporting Period*

The Company follows the concept of a 52-53 week fiscal year, which ends on the Sunday nearest December 31. Fiscal year 2014 is comprised of 52 weeks and ends on December 28, 2014. Fiscal year 2013 was comprised of 52 weeks and ended on December 29, 2013. The fiscal interim periods in fiscal 2014 and 2013 are each comprised of 13 weeks.

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**BIG 5 SPORTING GOODS CORPORATION**

**NOTES TO UNAUDITED CONDENSED CONSOLIDATED FINANCIAL STATEMENTS**

**(continued)**

*Recently Issued Accounting Updates*

In April 2014, the Financial Accounting Standards Board ( FASB ) issued Accounting Standards Update ( ASU ) No. 2014-08, *Presentation of Financial Statements (Topic 205) and Property, Plant, and Equipment (Topic 360) Reporting Discontinued Operations and Disclosures of Disposals of Components of an Entity*, which includes amendments that change the requirements for reporting discontinued operations and require additional disclosures about discontinued operations. Under the new guidance, only disposals representing a strategic shift in operations that have, or will have, a major effect on the organization's operations and financial results should be presented as discontinued operations. Additionally, ASU No. 2014-08 requires expanded disclosures about discontinued operations that will provide financial statement users with more information about the assets, liabilities, income, and expenses of discontinued operations. The amendments in ASU No. 2014-08 will be applied prospectively to annual periods beginning on or after December 15, 2014, and interim periods within those years, with early adoption permitted. The Company adopted ASU No. 2014-08 in the first quarter of 2014, which did not have a material impact on the Company's Interim Financial Statements.

In May 2014, the FASB issued ASU No. 2014-09, *Revenue from Contracts with Customers (Topic 606)*, which includes amendments that create Topic 606 and supersede the revenue recognition requirements in Topic 605, *Revenue Recognition*, including most industry-specific revenue recognition guidance throughout the Industry Topics of the Codification. In addition, the amendments supersede the cost guidance in Subtopic 605-35, *Revenue Recognition Construction-Type and Production-Type Contracts*, and create new Subtopic 340-40, *Other Assets and Deferred Costs Contracts with Customers*. In summary, the core principle of Topic 606 is that an entity recognizes revenue to depict the transfer of promised goods or services to customers in an amount that reflects the consideration to which the entity expects to be entitled in exchange for those goods or services. The amendments in ASU No. 2014-09 are effective for annual reporting periods beginning after December 15, 2016, including interim periods within that reporting period. Early application is not permitted. The Company is evaluating the future impact of the issuance of ASU No. 2014-09.

In August 2014, the FASB issued ASU No. 2014-15, *Presentation of Financial Statements Going Concern (Subtopic 205-40) Disclosure of Uncertainties about an Entity's Ability to Continue as a Going Concern*, which requires entities to evaluate their ability to continue as a going concern within one year after the date that the financial statements are issued. Disclosure is required if there is substantial doubt about an entity's ability to continue as a going concern. The guidance in ASU No. 2014-15 is effective for the annual period ending after December 15, 2016, and for annual periods and interim periods thereafter, with early application permitted. The Company does not expect that the adoption of this ASU will have a material impact on the consolidated financial statements.

There have been no other recently issued accounting updates that had a material impact on the Company's Interim Financial Statements.



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**BIG 5 SPORTING GOODS CORPORATION**

**NOTES TO UNAUDITED CONDENSED CONSOLIDATED FINANCIAL STATEMENTS**

**(continued)**

*Use of Estimates*

Management has made a number of estimates and assumptions relating to the reporting of assets, liabilities and stockholders' equity and the disclosure of commitments and contingencies as of the date of the Interim Financial Statements and reported amounts of revenue and expense during the reporting period to prepare these Interim Financial Statements in conformity with GAAP. Certain items subject to such estimates and assumptions include the carrying amount of merchandise inventories, property and equipment, and goodwill; valuation allowances for receivables, sales returns and deferred income tax assets; estimates related to gift card breakage and the valuation of share-based compensation awards; and obligations related to asset retirements, litigation, self-insurance liabilities and employee benefits. Actual results could differ significantly from these estimates under different assumptions and conditions.

*Revenue Recognition*

The Company earns revenue by selling merchandise primarily through its retail stores. Revenue is recognized when merchandise is sold and delivered to the customer and is shown net of estimated returns during the relevant period. The allowance for sales returns is estimated based upon historical experience.

Cash received from the sale of gift cards is recorded as a liability, and revenue is recognized upon the redemption of the gift card or when it is determined that the likelihood of redemption is remote ( gift card breakage ) and no liability to relevant jurisdictions exists. The Company determines the gift card breakage rate based upon historical redemption patterns and recognizes gift card breakage on a straight-line basis over the estimated gift card redemption period (20 quarters as of the end of the third quarter of fiscal 2014). The Company recognized approximately \$110,000 and \$326,000 in gift card breakage revenue for the 13 and 39 weeks ended September 28, 2014, respectively, compared to approximately \$105,000 and \$314,000 in gift card breakage revenue for the 13 and 39 weeks ended September 29, 2013, respectively.

The Company records sales tax collected from its customers on a net basis, and therefore excludes it from revenue as defined in Accounting Standards Codification ( ASC ) 605, *Revenue Recognition*.

*Share-Based Compensation*

The Company accounts for its share-based compensation in accordance with ASC 718, *Compensation - Stock Compensation*. The Company recognizes compensation expense on a straight-line basis over the requisite service period using the fair-value method for share option awards, nonvested share awards and nonvested share unit awards granted with service-only conditions. See Note 10 to the Interim Financial Statements for a further discussion on share-based compensation.



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**BIG 5 SPORTING GOODS CORPORATION**

**NOTES TO UNAUDITED CONDENSED CONSOLIDATED FINANCIAL STATEMENTS**

**(continued)**

*Valuation of Merchandise Inventories, Net*

The Company's merchandise inventories are made up of finished goods and are valued at the lower of cost or market using the weighted-average cost method that approximates the first-in, first-out method. Average cost includes the direct purchase price of merchandise inventory, net of certain vendor allowances and cash discounts, in-bound freight-related expense and allocated overhead expense associated with the Company's distribution center.

Management regularly reviews inventories and records valuation reserves for damaged and defective merchandise, merchandise items with slow-moving or obsolescence exposure and merchandise that has a carrying value that exceeds market value. Because of its merchandise mix, the Company has not historically experienced significant occurrences of obsolescence.

Inventory shrinkage is accrued as a percentage of merchandise sales based on historical inventory shrinkage trends. The Company performs physical inventories of its stores at least once per year and cycle counts inventories at its distribution center throughout the year. The reserve for inventory shrinkage represents an estimate for inventory shrinkage for each store since the last physical inventory date through the reporting date.

These reserves are estimates, which could vary significantly, either favorably or unfavorably, from actual results if future economic conditions, consumer demand and competitive environments differ from expectations.

*Valuation of Long-Lived Assets*

The Company reviews long-lived assets for impairment whenever events or changes in circumstances indicate that the carrying amount of an asset may not be recoverable.

Long-lived assets are reviewed for recoverability at the lowest level in which there are identifiable cash flows (asset group), usually at the store level. Each store typically requires investments of approximately \$0.4 million in long-lived assets to be held and used, subject to recoverability testing. The carrying amount of an asset group is not considered recoverable if it exceeds the sum of the undiscounted cash flows expected to result from the use and eventual disposition of the asset group. If the asset group is determined not to be recoverable, then an impairment charge will be recognized in the amount by which the carrying amount of the asset group exceeds its fair value, determined using discounted cash flow valuation techniques, as defined in ASC 360, *Property, Plant, and Equipment*.

The Company determines the sum of the undiscounted cash flows expected to result from the asset group by projecting future revenue, gross profit and operating expense for each store under consideration for impairment. The estimates of future cash flows involve management judgment and are based upon assumptions about expected future operating performance. Assumptions used in these forecasts are consistent with internal planning, and take into consideration, among other factors, the current economic environment and future expectations, competitive factors in the various markets and inflation. The actual cash flows could differ from management's estimates due to changes in business conditions, operating performance and economic conditions.

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**BIG 5 SPORTING GOODS CORPORATION**

**NOTES TO UNAUDITED CONDENSED CONSOLIDATED FINANCIAL STATEMENTS**

**(continued)**

*Leases and Deferred Rent*

The Company accounts for its leases under the provisions of ASC 840, *Leases*.

The Company evaluates and classifies its leases as either operating or capital leases for financial reporting purposes. Operating lease commitments consist principally of leases for the Company's retail store facilities, distribution center and corporate office. Capital lease obligations consist principally of leases for some of the Company's distribution center delivery tractors, management information systems hardware and point-of-sale equipment for the Company's stores.

Certain of the leases for the Company's retail store facilities provide for payments based on future sales volumes at the leased location, which are not measurable at the inception of the lease. These contingent rents are expensed as they accrue.

Deferred rent represents the difference between rent paid and the amounts expensed for operating leases. Certain leases have scheduled rent increases, and certain leases include an initial period of free or reduced rent as an inducement to enter into the lease agreement (rent holidays). The Company recognizes rent expense for rent increases and rent holidays on a straight-line basis over the term of the underlying leases, without regard to when rent payments are made. The calculation of straight-line rent is based on the reasonably assured lease term as defined in ASC 840 and may exceed the initial non-cancelable lease term.

Landlord allowances for tenant improvements, or lease incentives, are recorded as deferred rent and amortized on a straight-line basis over the reasonably assured lease term as a component of rent expense.

**(3) Impairment of Long-Lived Assets**

For the 39 weeks ended September 28, 2014 and September 29, 2013, the Company recognized pre-tax non-cash impairment charges of \$0.8 million and \$0.1 million, respectively, related to certain underperforming stores. These impairment charges are included in selling and administrative expense in the accompanying interim unaudited condensed consolidated statements of operations.

Table of Contents**BIG 5 SPORTING GOODS CORPORATION****NOTES TO UNAUDITED CONDENSED CONSOLIDATED FINANCIAL STATEMENTS**

(continued)

**(4) Fair Value Measurements**

The carrying values of cash, accounts receivable, accounts payable and accrued expenses approximate the fair values of these instruments due to their short-term nature. The carrying amount for borrowings under the revolving credit facility approximates fair value because of the variable market interest rate charged to the Company for these borrowings. When the Company recognizes impairment on certain of its underperforming stores, the carrying values of these stores are reduced to their estimated fair values.

During the 39 weeks ended September 28, 2014 and September 29, 2013, the Company's only significant assets or liabilities measured at fair value on a nonrecurring basis subsequent to their initial recognition were certain assets subject to long-lived asset impairment. The Company classified these fair value measurements as Level 3, in accordance with ASC 820, *Fair Value Measurement*.

**(5) Accrued Expenses**

The major components of accrued expenses are as follows:

	<b>September 28, 2014</b>	<b>December 29, 2013</b>
	<b>(In thousands)</b>	
Payroll and related expense	\$ 19,101	\$ 23,240
Occupancy expense	9,670	9,392
Sales tax	7,014	10,110
Self-insurance liabilities	4,467	4,357
Advertising	2,891	5,734
Other	18,233	17,090
Accrued expenses	\$ 61,376	\$ 69,923

**(6) Long-Term Debt**

On October 18, 2010, the Company entered into a credit agreement with Wells Fargo Bank, National Association (Wells Fargo), as administrative agent, and a syndicate of other lenders, which was amended on October 31, 2011 and December 19, 2013 (as so amended, the Credit Agreement). The maturity date of the Credit Agreement is December 19, 2018.

The Credit Agreement provides for a revolving credit facility (the Credit Facility) with an aggregate committed availability of up to \$140.0 million, which amount may be increased at the Company's option up to a maximum of

\$165.0 million. The Company may also request additional increases in aggregate availability, up to a maximum of \$200.0 million, in which case the existing lenders under the Credit Agreement will have the option to increase their commitments to accommodate the requested increase. If such existing lenders do not exercise that option, the Company may (with the consent of Wells Fargo, not to be unreasonably withheld) seek other lenders willing to provide such commitments. The Credit Facility includes a \$50.0 million sublimit for issuances of letters of credit and a \$20.0 million sublimit for swingline loans.

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Table of Contents**BIG 5 SPORTING GOODS CORPORATION****NOTES TO UNAUDITED CONDENSED CONSOLIDATED FINANCIAL STATEMENTS****(continued)**

The Company may borrow under the Credit Facility from time to time, provided the amounts outstanding will not exceed the lesser of the then aggregate availability (as discussed above) and the Borrowing Base (such lesser amount being referred to as the Loan Cap). The Borrowing Base generally is comprised of the sum, at the time of calculation, of (a) 90.00% of eligible credit card receivables; plus (b) the cost of eligible inventory (other than eligible in-transit inventory), net of inventory reserves, multiplied by 90.00% of the appraised net orderly liquidation value of eligible inventory (expressed as a percentage of the cost of eligible inventory); plus (c) the lesser of (i) the cost of eligible in-transit inventory, net of inventory reserves, multiplied by 90.00% of the appraised net orderly liquidation value of eligible in-transit inventory (expressed as a percentage of the cost of eligible in-transit inventory), or (ii) \$10.0 million, minus (d) certain reserves established by Wells Fargo in its role as the Administrative Agent in its reasonable discretion.

Generally, the Company may designate specific borrowings under the Credit Facility as either base rate loans or LIBO rate loans. The applicable interest rate on the Company's borrowings is a function of the daily average, over the preceding fiscal quarter, of the excess of the Loan Cap over amounts borrowed (such amount being referred to as the Average Daily Excess Availability).

On October 31, 2011, the Company entered into a First Amendment to Credit Agreement (First Amendment) and amended certain provisions of the Credit Agreement. After the First Amendment, those loans designated as LIBO rate loans bore interest at a rate equal to the then applicable LIBO rate plus an applicable margin as shown in the table below. Those loans designated as base rate loans bore interest at a rate equal to the applicable margin for base rate loans (as shown below) plus the highest of (a) the Federal funds rate, as in effect from time to time, plus one-half of one percent (0.50%), (b) the LIBO rate, as adjusted to account for statutory reserves, plus one percent (1.00%), or (c) the rate of interest in effect for such day as publicly announced from time to time by Wells Fargo as its prime rate. The applicable margin for all loans was as set forth below as a function of Average Daily Excess Availability for the preceding fiscal quarter.

<b>Level</b>	<b>Average Daily Excess Availability</b>	<b>LIBO Rate Applicable Margin</b>	<b>Base Rate Applicable Margin</b>
<b>I</b>	Greater than or equal to \$70,000,000	1.50%	0.50%
<b>II</b>	Greater than or equal to \$40,000,000	1.75%	0.75%
<b>III</b>	Less than \$40,000,000	2.00%	1.00%

The First Amendment reduced the commitment fee assessed on the unused portion of the Credit Facility to 0.375% per annum.



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On December 19, 2013, the Company entered into a Second Amendment to Credit Agreement ( Second Amendment ) and amended certain provisions of the Credit Agreement. Following the Second Amendment, those loans designated as LIBO rate loans bear interest at a rate equal to the then applicable LIBO rate plus an applicable margin as shown in the table below. Those loans designated as base rate loans bear interest at a rate equal to the applicable margin for base rate loans (as shown below) plus the highest of (a) the Federal funds rate, as in effect from time to time, plus one-half of one percent (0.50%), (b) the LIBO rate, as adjusted to account for statutory reserves, plus one percent (1.00%), or (c) the rate of interest in effect for such day as publicly announced from time to time by Wells Fargo as its prime rate. The applicable margin for all loans is as set forth below as a function of Average Daily Excess Availability for the preceding fiscal quarter.

<b>Level</b>	<b>Average Daily Excess Availability</b>	<b>LIBO Rate Applicable Margin</b>	<b>Base Rate Applicable Margin</b>
<b>I</b>	Greater than or equal to \$100,000,000	1.25%	0.25%
<b>II</b>	Less than \$100,000,000 but greater than or equal to \$40,000,000	1.50%	0.50%
<b>III</b>	Less than \$40,000,000	1.75%	0.75%

The Second Amendment further reduced the commitment fee assessed on the unused portion of the Credit Facility to 0.25% per annum, and reduced certain fees for letters of credit.

Obligations under the Credit Facility are secured by a general lien and perfected security interest in substantially all of the Company's assets. The Credit Agreement contains covenants that require the Company to maintain a fixed charge coverage ratio of not less than 1.0:1.0 in certain circumstances, and limit the ability to, among other things, incur liens, incur additional indebtedness, transfer or dispose of assets, change the nature of the business, guarantee obligations, pay dividends or make other distributions or repurchase stock, and make advances, loans or investments. The Company may declare or pay cash dividends or repurchase stock only if, among other things, no default or event of default then exists or would arise from such dividend or repurchase of stock and, after giving effect to such dividend or repurchase, certain availability and/or fixed charge coverage ratio requirements are satisfied. The Credit Agreement contains customary events of default, including, without limitation, failure to pay when due principal amounts with respect to the Credit Facility, failure to pay any interest or other amounts under the Credit Facility for five days after becoming due, failure to comply with certain agreements or covenants contained in the Credit Agreement, failure to satisfy certain judgments against the Company, failure to pay when due (or any other default which does or may lead to the acceleration of) certain other material indebtedness in principal amount in excess of \$5.0 million, and certain insolvency and bankruptcy events.

The Company had long-term revolving credit borrowings of \$55.4 million and \$43.0 million as of September 28, 2014 and December 29, 2013, respectively. Total remaining borrowing availability, after subtracting letters of credit, was \$83.9 million and \$96.1 million as of September 28, 2014 and December 29, 2013, respectively.

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**BIG 5 SPORTING GOODS CORPORATION**

**NOTES TO UNAUDITED CONDENSED CONSOLIDATED FINANCIAL STATEMENTS**

**(continued)**

**(7) Income Taxes**

Under the asset and liability method prescribed under ASC 740, *Income Taxes*, the Company recognizes deferred tax assets and liabilities for the future tax consequences attributable to differences between financial statement carrying amounts of 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 realized or settled. The effect of a change in tax rates on deferred tax assets and liabilities is recognized in income in the period that includes the enactment date. The realizability of deferred tax assets is assessed throughout the year and a valuation allowance is recorded if necessary to reduce net deferred tax assets to the amount more likely than not to be realized. As of September 28, 2014 and December 29, 2013, there was no valuation allowance as the deferred income tax assets were more likely than not to be realized.

The Company files a consolidated federal income tax return and files tax returns in various state and local jurisdictions. The statutes of limitations for consolidated federal income tax returns are open for fiscal years 2011 and after, and state and local income tax returns are open for fiscal years 2009 and after.

Effective January 2, 2013, The American Taxpayer Relief Act of 2012 was enacted, which contained provisions that retroactively reinstated the work opportunity tax credit ( WOTC ) and the 15-year cost recovery life of qualified leasehold improvements from January 1, 2012 through December 31, 2013. As a result of this legislation, the Company applied WOTC of approximately \$0.3 million to its fiscal 2013 first quarter tax provision for amounts generated in 2012, resulting in a reduction to its estimated effective tax rate for the 2013 first quarter of 137 basis points. Also as a result of this legislation, the Company increased its 2012 federal depreciation deduction by approximately \$2.8 million, which resulted in a reduction to deferred tax assets and income taxes payable by approximately \$1.1 million in the first quarter of fiscal 2013.

As of September 28, 2014 and December 29, 2013, the Company had no unrecognized tax benefits that, if recognized, would affect the Company's effective income tax rate over the next 12 months. The Company's policy is to recognize interest accrued related to unrecognized tax benefits in interest expense and penalties in operating expense. As of September 28, 2014 and December 29, 2013, the Company had no accrued interest or penalties.



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(continued)

**(8) Earnings Per Share**

The Company calculates earnings per share in accordance with ASC 260, *Earnings Per Share*, which requires a dual presentation of basic and diluted earnings per share. Basic earnings per share is calculated by dividing net income by the weighted-average shares of common stock outstanding, reduced by shares repurchased and held in treasury, during the period. Diluted earnings per share represents basic earnings per share adjusted to include the potentially dilutive effect of outstanding share option awards, nonvested share awards and nonvested share unit awards.

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

	<b>13 Weeks Ended</b>		<b>39 Weeks Ended</b>	
	<b>September 28,</b>	<b>September 29,</b>	<b>September 28,</b>	<b>September 29,</b>
	<b>2014</b>	<b>2013</b>	<b>2014</b>	<b>2013</b>
	<b>(In thousands, except per share data)</b>			
Net income	\$ 7,466	\$ 9,138	\$ 12,061	\$ 22,756
Weighted-average shares of common stock outstanding:				
Basic	21,926	21,933	21,964	21,700
Dilutive effect of common stock equivalents arising from share option, nonvested share and nonvested share unit awards	112	298	199	332
Diluted	22,038	22,231	22,163	22,032
Basic earnings per share	\$ 0.34	\$ 0.42	\$ 0.55	\$ 1.05
Diluted earnings per share	\$ 0.34	\$ 0.41	\$ 0.54	\$ 1.03

The computation of diluted earnings per share for the 13 weeks ended September 28, 2014, the 39 weeks ended September 28, 2014, the 13 weeks ended September 29, 2013 and the 39 weeks ended September 29, 2013 does not include share option awards in the amounts of 507,259, 528,123, 474,271 and 779,443, respectively, that were outstanding and antidilutive (i.e., including such share option awards would result in higher earnings per share), since the exercise prices of these share option awards exceeded the average market price of the Company's common shares.

Additionally, the computation of diluted earnings per share for the 13 weeks ended September 28, 2014, the 39 weeks ended September 28, 2014 and the 39 weeks ended September 29, 2013 does not include nonvested share awards and

nonvested share unit awards in the amounts of 260,691, 1,320 and 7,648 shares, respectively, that were outstanding and antidilutive, since the

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**NOTES TO UNAUDITED CONDENSED CONSOLIDATED FINANCIAL STATEMENTS**

**(continued)**

grant date fair values of these nonvested share awards and nonvested share unit awards exceeded the average market price of the Company's common shares. No nonvested share awards or nonvested share unit awards were antidilutive for the 13 weeks ended September 29, 2013.

**(9) Commitments and Contingencies**

The Company was served on the following dates with the following nine complaints, each of which was brought as a purported class action on behalf of persons who made purchases at the Company's stores in California using credit cards and were requested or required to provide personal identification information at the time of the transaction: (1) on February 22, 2011, a complaint filed in the California Superior Court in the County of Los Angeles, entitled *Maria Eugenia Saenz Valiente v. Big 5 Sporting Goods Corporation*, et al., Case No. BC455049; (2) on February 22, 2011, a complaint filed in the California Superior Court in the County of Los Angeles, entitled *Scott Mossler v. Big 5 Sporting Goods Corporation*, et al., Case No. BC455477; (3) on February 28, 2011, a complaint filed in the California Superior Court in the County of Los Angeles, entitled *Yelena Matatova v. Big 5 Sporting Goods Corporation*, et al., Case No. BC455459; (4) on March 8, 2011, a complaint filed in the California Superior Court in the County of Los Angeles, entitled *Neal T. Wiener v. Big 5 Sporting Goods Corporation*, et al., Case No. BC456300; (5) on March 22, 2011, a complaint filed in the California Superior Court in the County of San Francisco, entitled *Donna Motta v. Big 5 Sporting Goods Corporation*, et al., Case No. CGC-11-509228; (6) on March 30, 2011, a complaint filed in the California Superior Court in the County of Alameda, entitled *Steve Holmes v. Big 5 Sporting Goods Corporation*, et al., Case No. RG11563123; (7) on March 30, 2011, a complaint filed in the California Superior Court in the County of San Francisco, entitled *Robin Nelson v. Big 5 Sporting Goods Corporation*, et al., Case No. CGC-11-508829; (8) on April 8, 2011, a complaint filed in the California Superior Court in the County of San Joaquin, entitled *Pamela B. Smith v. Big 5 Sporting Goods Corporation*, et al., Case No. 39-2011-00261014-CU-BT-STK; and (9) on May 31, 2011, a complaint filed in the California Superior Court in the County of Los Angeles, entitled *Deena Gabriel v. Big 5 Sporting Goods Corporation*, et al., Case No. BC462213. On June 16, 2011, the Judicial Council of California issued an Order Assigning Coordination Trial Judge designating the California Superior Court in the County of Los Angeles as having jurisdiction to coordinate and to hear all nine of the cases as Case No. JCCP4667. On October 21, 2011, the plaintiffs collectively filed a Consolidated Amended Complaint, alleging violations of the California Civil Code, negligence, invasion of privacy and unlawful intrusion. The plaintiffs allege, among other things, that customers making purchases with credit cards at the Company's stores in California were improperly requested to provide their zip code at the time of such purchases. The plaintiffs seek, on behalf of the class members, the following: statutory penalties; attorneys' fees; expenses; restitution of property; disgorgement of profits; and injunctive relief. In an effort to negotiate a settlement of this litigation, the Company and plaintiffs engaged in Mandatory Settlement Conferences conducted by the court on February 6, 2013, February 19, 2013, April 2, 2013, September 12, 2013, and September 20, 2013, and also engaged in mediation conducted by a third party mediator on July 15, 2013. As a result of the foregoing, the parties agreed to settle the lawsuit. On March 23, 2014, the court granted preliminary approval of the settlement. The court has scheduled a hearing for November 10, 2014, to consider granting final approval of the settlement. Under the terms of the



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**NOTES TO UNAUDITED CONDENSED CONSOLIDATED FINANCIAL STATEMENTS**

**(continued)**

settlement, the Company agreed that class members who submit valid and timely claim forms will receive either a \$25 gift card (with proof of purchase) or a \$10 merchandise voucher (without proof of purchase). Additionally, the Company agreed to pay plaintiff's attorneys' fees and costs awarded by the court, enhancement payments to the class representatives and claims administrator's fees. Under the settlement, if the total amount paid by the Company for the class payout, class representative enhancement payments and claims administrator's fees is less than \$1.0 million, then the Company will issue merchandise vouchers to a charity for the balance of the deficiency in the manner provided in the settlement agreement. The Company's estimated total cost pursuant to this settlement is reflected in a legal settlement accrual recorded in the third quarter of fiscal 2013. The Company admitted no liability or wrongdoing with respect to the claims set forth in the lawsuit. Once final approval is granted, the settlement will constitute a full and complete settlement and release of all claims related to the lawsuit. Based on the terms of the settlement agreement, the Company currently believes that settlement of this litigation will not have a material negative impact on the Company's results of operations or financial condition. However, if the settlement is not finally approved by the court, the Company intends to defend this litigation vigorously. If the settlement is not finally approved by the court and this litigation is settled or resolved unfavorably to the Company, this litigation and the costs of defending it could have a material negative impact on the Company's results of operations or financial condition.

The Company is involved in various other claims and legal actions arising in the ordinary course of business. In the opinion of management, the ultimate disposition of these matters is not expected to have a material adverse effect on the Company's results of operations or financial condition.

**(10) Share-based Compensation**

At its discretion, the Company grants share option awards, nonvested share awards and nonvested share unit awards to certain employees, as defined by ASC 718, *Compensation - Stock Compensation*, under the Company's 2007 Equity and Performance Incentive Plan, as amended and restated on June 14, 2011 (the "Plan"), and accounts for its share-based compensation in accordance with ASC 718. The Company recognized \$0.5 million and \$1.5 million in share-based compensation expense for the 13 weeks and 39 weeks ended September 28, 2014, respectively, compared to \$0.5 million and \$1.4 million in share-based compensation expense for the 13 weeks and 39 weeks ended September 29, 2013, respectively.

*Share Option Awards*

Share option awards granted by the Company generally vest and become exercisable in four equal annual installments of 25% per year with a maximum life of ten years. The exercise price of share option awards is equal to the quoted market price of the Company's common stock on the date of grant. In the 39 weeks ended September 28, 2014 and September 29, 2013, the Company granted 18,000 and 30,500 share option awards, respectively. The weighted-average grant-date fair value per option for share option awards granted in the 39 weeks ended September 28, 2014 and September 29, 2013 was \$4.80 and \$8.37, respectively.



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(continued)

A summary of the status of the Company's share option awards is presented below:

	<b>Shares</b>	<b>Weighted-Average Exercise Price</b>	<b>Weighted-Average Remaining Contractual Life (In Years)</b>	<b>Aggregate Intrinsic Value</b>
Outstanding at December 29, 2013	989,130	\$ 17.83		
Granted	18,000	11.93		
Exercised	(10,525)	5.99		
Forfeited or Expired	(253,700)	24.12		
Outstanding at September 28, 2014	742,905	\$ 15.71	3.20	\$ 777,818
Exercisable at September 28, 2014	679,905	\$ 16.01	2.70	\$ 723,818
Vested and Expected to Vest at September 28, 2014	742,121	\$ 15.72	3.20	\$ 777,551

The aggregate intrinsic value in the preceding table represents the total pre-tax intrinsic value, based upon the Company's closing stock price of \$9.69 as of September 28, 2014, which would have been received by the share option award holders had all share option award holders exercised their share option awards as of that date.

The total intrinsic value of share option awards exercised for the 39 weeks ended September 28, 2014 and September 29, 2013 was approximately \$0.1 million and \$5.0 million, respectively. The total cash received from employees as a result of employee share option award exercises for the 39 weeks ended September 28, 2014 and September 29, 2013 was approximately \$63,000 and \$4.5 million, respectively. The actual tax benefit realized for the tax deduction from share option award exercises of share-based compensation awards in the 39 weeks ended September 28, 2014 and September 29, 2013 totaled \$45,000 and \$2.0 million, respectively.

The fair value of each share option award on the date of grant is estimated using the Black-Scholes method based on the following weighted-average assumptions:

**39 Weeks Ended**

	<b>September 28, 2014</b>	<b>September 29, 2013</b>
Risk-free interest rate	1.8%	1.4%
Expected term	5.8 years	6.9 years
Expected volatility	57.0%	57.5%
Expected dividend yield	3.3%	2.3%

The risk-free interest rate is based on the U.S. Treasury yield curve in effect at the time of grant for periods corresponding with the expected term of the option award; the expected term represents the weighted-average period of time that option awards granted are expected to be



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outstanding giving consideration to vesting schedules and historical participant exercise behavior; the expected volatility is based upon historical volatility of the Company's common stock; and the expected dividend yield is based upon the Company's current dividend rate and future expectations.

As of September 28, 2014, there was \$0.3 million of total unrecognized compensation expense related to nonvested share option awards granted. That expense is expected to be recognized over a weighted-average period of 2.4 years.

*Nonvested Share Awards and Nonvested Share Unit Awards*

Nonvested share awards and nonvested share unit awards granted by the Company vest from the date of grant in four equal annual installments of 25% per year. Nonvested share awards are delivered to the recipient upon their vesting. With respect to nonvested share unit awards, vested shares will be delivered to the recipient on the tenth business day of January following the year in which the recipient's service to the Company is terminated. The total fair value of nonvested share awards which vested during the 39 weeks ended September 28, 2014 and September 29, 2013 was \$2.1 million and \$1.8 million, respectively. The total fair value of nonvested share unit awards which vested during the 39 weeks ended September 28, 2014 and September 29, 2013 was \$0.1 million and \$38,000, respectively.

The Company granted 152,920 and 127,020 nonvested share awards in the 39 weeks ended September 28, 2014 and September 29, 2013, respectively. The weighted-average grant-date fair value per share of the Company's nonvested share awards granted in the 39 weeks ended September 28, 2014 and September 29, 2013 was \$15.14 and \$15.56, respectively.

The following table details the Company's nonvested share awards activity for the 39 weeks ended September 28, 2014:

	<b>Shares</b>	<b>Weighted-Average Grant-Date Fair Value</b>
Balance as of December 29, 2013	333,770	\$ 12.38
Granted	152,920	15.14
Vested	(137,615)	12.67
Forfeited	(11,550)	13.38
Balance as of September 28, 2014	337,525	\$ 13.48

To satisfy employee minimum statutory tax withholding requirements for nonvested share awards that vest, the Company withholds and retires a portion of the vesting common shares, unless an employee elects to pay cash. In the 39 weeks ended September 28, 2014, the Company withheld 52,927 common shares with a total value of \$0.8 million. This amount is presented as a cash outflow from financing activities in the accompanying interim unaudited condensed consolidated statement of cash flows.

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**NOTES TO UNAUDITED CONDENSED CONSOLIDATED FINANCIAL STATEMENTS**

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In the 39 weeks ended September 28, 2014 and September 29, 2013, the Company granted 12,000 and 12,000 nonvested share unit awards, respectively. The weighted-average grant-date fair value per share of the Company's nonvested share unit awards granted in the 39 weeks ended September 28, 2014 and September 29, 2013 was \$11.93 and \$20.29, respectively. The weighted-average grant-date fair value of nonvested share awards and nonvested share unit awards is the quoted market price of the Company's common stock on the date of grant.

As of September 28, 2014, there was \$3.5 million and \$0.3 million of total unrecognized compensation expense related to nonvested share awards and nonvested share unit awards, respectively. That expense is expected to be recognized over a weighted-average period of 2.5 years and 2.7 years for nonvested share awards and nonvested share unit awards, respectively.

**(11) Subsequent Event**

In the fourth quarter of fiscal 2014, the Company's Board of Directors declared a quarterly cash dividend of \$0.10 per share of outstanding common stock, which will be paid on December 15, 2014 to stockholders of record as of December 1, 2014.

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**REPORT OF INDEPENDENT REGISTERED PUBLIC ACCOUNTING FIRM**

To the Board of Directors and Stockholders of

Big 5 Sporting Goods Corporation

El Segundo, California

We have reviewed the accompanying condensed consolidated balance sheet of Big 5 Sporting Goods Corporation and subsidiaries (the Corporation) as of September 28, 2014, and the related condensed consolidated statements of operations for the 13 and 39 weeks ended September 28, 2014 and September 29, 2013, and of stockholders' equity and cash flows for the 39 weeks ended September 28, 2014 and September 29, 2013. These interim financial statements are the responsibility of the Corporation's management.

We conducted our reviews in accordance with the standards of the Public Company Accounting Oversight Board (United States). A review of interim financial information consists principally of applying analytical procedures and making inquiries of persons responsible for financial and accounting matters. It is substantially less in scope than an audit conducted in accordance with the standards of the Public Company Accounting Oversight Board (United States), the objective of which is the expression of an opinion regarding the financial statements taken as a whole. Accordingly, we do not express such an opinion.

Based on our reviews, we are not aware of any material modifications that should be made to such condensed consolidated interim financial statements for them to be in conformity with accounting principles generally accepted in the United States of America.

We have previously audited, in accordance with the standards of the Public Company Accounting Oversight Board (United States), the consolidated balance sheet of Big 5 Sporting Goods Corporation and subsidiaries as of December 29, 2013, and the related consolidated statements of operations, stockholders' equity, and cash flows for the year then ended (not presented herein); and in our report dated February 26, 2014, we expressed an unqualified opinion on those consolidated financial statements. In our opinion, the information set forth in the accompanying condensed consolidated balance sheet as of December 29, 2013 is fairly stated, in all material respects, in relation to the consolidated balance sheet from which it has been derived.

/s/ DELOITTE & TOUCHE LLP

Los Angeles, California

October 29, 2014

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

The following discussion and analysis of the Big 5 Sporting Goods Corporation ( we, our, us ) financial condition and results of operations includes information with respect to our plans and strategies for our business and should be read in conjunction with our interim unaudited condensed consolidated financial statements and related notes ( Interim Financial Statements ) included herein and our consolidated financial statements and related notes, and *Management's Discussion and Analysis of Financial Condition and Results of Operations* contained in our Annual Report on Form 10-K for the fiscal year ended December 29, 2013.

**Overview**

We are a leading sporting goods retailer in the western United States, operating 429 stores in 12 states under the name Big 5 Sporting Goods as of September 28, 2014. We provide a full-line product offering in a traditional sporting goods store format that averages approximately 11,000 square feet. Our product mix includes athletic shoes, apparel and accessories, as well as a broad selection of outdoor and athletic equipment for team sports, fitness, camping, hunting, fishing, tennis, golf, winter and summer recreation and roller sports.

**Executive Summary**

Our earnings for the third quarter of fiscal 2014 compared to the third quarter of fiscal 2013 were lower, despite higher sales levels, because of reduced gross profit resulting from lower merchandise margins and higher operating costs, along with increased selling and administrative expense. Our same store sales in the third quarter of fiscal 2014 increased 1.0% compared to the same period last year, reflecting improved sales for a number of product categories including higher sales of summer-related merchandise which were aided by favorable overall weather comparisons in our primary markets year over year, partially offset by reduced demand for firearms, ammunition and related products as well as continued softness in the overall consumer environment.

Net sales for the third quarter of fiscal 2014 increased 2.3% to \$265.1 million compared to \$259.1 million for the third quarter of fiscal 2013. The increase in net sales was primarily attributable to added sales from new stores as well as an increase in same store sales of 1.0%, partially offset by a reduction in closed store sales.

Net income for the third quarter of fiscal 2014 decreased to \$7.5 million, or \$0.34 per diluted share, compared to \$9.1 million, or \$0.41 per diluted share, for the third quarter of fiscal 2013. The decrease in net income was driven primarily by reduced gross profit resulting from lower merchandise margins and higher operating costs, as well as an increase in selling and administrative expense.

Gross profit for the third quarter of fiscal 2014 represented 32.5% of net sales, compared with 33.9% in the same quarter of the prior year. The decrease in gross profit margin resulted mainly from a year-over-year decrease in merchandise margins of 47 basis points that reflected the impact of promotional activity, as well as increased store occupancy and distribution expense as a percentage of net sales.

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Selling and administrative expense for the third quarter of fiscal 2014 increased 1.9% to \$73.8 million, or 27.9% of net sales, compared to \$72.4 million, or 27.9% of net sales, for the third quarter of fiscal 2013. The increase in selling and administrative expense was primarily attributable to higher employee labor and benefit-related expense and higher store-related expense to support the increase in store count, partially offset by a decrease in legal expense reflecting a pre-tax charge for legal settlements recorded in the third quarter of fiscal 2013.

Operating income for the third quarter of fiscal 2014 decreased to \$12.2 million, or 4.6% of net sales, compared to \$15.4 million, or 6.0% of net sales, for the third quarter of fiscal 2013. The decrease in operating income primarily reflected reduced gross profit resulting from lower merchandise margins and higher operating costs, as well as an increase in selling and administrative expense.

**Results of Operations**

The results of the interim periods are not necessarily indicative of results for the entire fiscal year.

*13 Weeks Ended September 28, 2014 Compared to 13 Weeks Ended September 29, 2013*

The following table sets forth selected items from our interim unaudited condensed consolidated statements of operations by dollar and as a percentage of our net sales for the periods indicated:

	13 Weeks Ended			
	September 28, 2014		September 29, 2013	
	(In thousands, except percentages)			
Net sales	\$ 265,115	100.0%	\$ 259,121	100.0%
Cost of sales <sup>(1)</sup>	179,055	67.5	171,331	66.1
Gross profit	86,060	32.5	87,790	33.9
Selling and administrative expense <sup>(2)</sup>	73,842	27.9	72,432	27.9
Operating income	12,218	4.6	15,358	6.0
Interest expense	386	0.1	395	0.2
Income before income taxes	11,832	4.5	14,963	5.8
Income taxes	4,366	1.7	5,825	2.3
Net income	\$ 7,466	2.8%	\$ 9,138	3.5%

(1) Cost of sales includes the cost of merchandise, net of discounts or allowances earned, freight, inventory reserves, buying, distribution center expense, including depreciation and amortization, and store occupancy expense. Store occupancy expense includes rent, amortization of leasehold improvements, common area maintenance, property taxes and insurance.

(2) Selling and administrative expense includes store-related expense, other than store occupancy expense, as well as advertising, depreciation and amortization, expense associated with operating our corporate headquarters and

impairment charges, if any.

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*Net Sales.* Net sales increased by \$6.0 million, or 2.3%, to \$265.1 million in the 13 weeks ended September 28, 2014 from \$259.1 million in the comparable period last year. The change in net sales reflected the following:

Added sales from new stores reflected the opening of 20 new stores since June 30, 2013, partially offset by a reduction in closed store sales.

Same store sales increased by \$2.7 million, or 1.0%, for the 13 weeks ended September 28, 2014, versus the comparable 13-week period in the prior year. Our higher same store sales compared to the same period last year reflected improved sales for a number of product categories including higher sales of summer-related merchandise which were aided by favorable overall weather comparisons in our primary markets year over year, partially offset by reduced demand for firearms, ammunition and related products as well as continued softness in the overall consumer environment. Same store sales for a period reflect net sales from stores that operated throughout the period as well as the full corresponding prior year period.

We experienced a slight increase in customer transactions in our retail stores, and the average sale per transaction also increased slightly in the third quarter of fiscal 2014 compared to the same period last year.

Store count as of September 28, 2014 was 429 versus 420 as of September 29, 2013. We opened four new stores in the 13 weeks ended September 28, 2014, one of which was a relocation, and closed two stores, both of which were relocations. We opened five new stores, two of which were relocations, and closed one store as part of a relocation, in the 13 weeks ended September 29, 2013. For fiscal 2014, we expect to open approximately 10 net new stores.

*Gross Profit.* Gross profit decreased by \$1.7 million, or 2.0%, to \$86.1 million, or 32.5% of net sales, in the 13 weeks ended September 28, 2014 from \$87.8 million, or 33.9% of net sales, in the 13 weeks ended September 29, 2013. The change in gross profit was primarily attributable to the following:

Merchandise margins, which exclude buying, occupancy and distribution expense, decreased 47 basis points versus the third quarter last year, reflecting the impact of promotional activity.

Distribution expense increased \$1.9 million, or 62 basis points, resulting primarily from lower costs capitalized into inventory, higher employee labor and benefit-related expense and higher trucking expense.

Store occupancy expense increased by \$1.4 million, or 36 basis points, year over year in the third quarter of fiscal 2014 primarily reflecting an increase in store count and increased rent associated with store lease renewals.

Net sales increased \$6.0 million, or 2.3%, year over year in the third quarter of fiscal 2014.



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*Selling and Administrative Expense.* Selling and administrative expense increased by \$1.4 million to \$73.8 million, or 27.9% of net sales, in the 13 weeks ended September 28, 2014 from \$72.4 million, or 27.9% of net sales, in the same period last year. The increase in overall selling and administrative expense compared to the prior year was primarily attributable to higher employee labor and benefit-related expense, as well as higher operating expense to support the increase in store count. These increases were partially offset by a decrease in legal expense reflecting a pre-tax charge of \$1.0 million to provide for legal settlements recorded in the third quarter of fiscal 2013, as well as a decrease in print advertising expense.

*Interest Expense.* Interest expense remained flat at \$0.4 million in the 13 weeks ended September 28, 2014 compared to the third quarter of fiscal 2013. Interest expense reflected a decrease in average interest rates of 30 basis points to 1.8% in the third quarter of fiscal 2014 from 2.1% in the prior year. The impact of lower average interest rates was offset by an increase in average debt levels of \$22.3 million to \$57.9 million in the third quarter of fiscal 2014 from \$35.6 million in the same period last year.

*Income Taxes.* The provision for income taxes was \$4.4 million for the 13 weeks ended September 28, 2014 and \$5.8 million for the 13 weeks ended September 29, 2013. Our effective tax rate was 36.9% for the third quarter of fiscal 2014 compared with 38.9% for the third quarter of fiscal 2013. The decreased effective tax rate for the third quarter of fiscal 2014 compared to the same period in fiscal 2013 primarily resulted from income tax credits representing a larger percentage of pre-tax income for the current year.

**Table of Contents***39 Weeks Ended September 28, 2014 Compared to 39 Weeks Ended September 29, 2013*

The following table sets forth selected items from our interim unaudited condensed consolidated statements of operations by dollar and as a percentage of our net sales for the periods indicated:

	39 Weeks Ended			
	September 28, 2014		September 29, 2013	
	(In thousands, except percentages)			
Net sales	\$ 727,528	100.0%	\$ 745,286	100.0%
Cost of sales <sup>(1)</sup>	493,217	67.8	497,348	66.7
Gross profit	234,311	32.2	247,938	33.3
Selling and administrative expense <sup>(2)</sup>	213,892	29.4	209,540	28.1
Operating income	20,419	2.8	38,398	5.2
Interest expense	1,191	0.2	1,266	0.2
Income before income taxes	19,228	2.6	37,132	5.0
Income taxes	7,167	1.0	14,376	1.9
Net income	\$ 12,061	1.6%	\$ 22,756	3.1%

(1) Cost of sales includes the cost of merchandise, net of discounts or allowances earned, freight, inventory reserves, buying, distribution center expense, including depreciation and amortization, and store occupancy expense. Store occupancy expense includes rent, amortization of leasehold improvements, common area maintenance, property taxes and insurance.

(2) Selling and administrative expense includes store-related expense, other than store occupancy expense, as well as advertising, depreciation and amortization, expense associated with operating our corporate headquarters and impairment charges, if any.

*Net Sales.* Net sales decreased by \$17.8 million, or 2.4%, to \$727.5 million in the 39 weeks ended September 28, 2014 from \$745.3 million in the comparable period last year. The change in net sales reflected the following:

Same store sales decreased by \$27.0 million, or 3.7%, for the 39 weeks ended September 28, 2014, versus the comparable 39-week period in the prior year. Our lower same store sales compared to the same period last year reflected reduced demand for firearms, ammunition and related products as well as continued softness in our overall consumer environment, combined with lower sales of winter-related merchandise as a result of unseasonably warm and dry winter-weather conditions in our primary markets in the first quarter of fiscal 2014. Same store sales for a period reflect net sales from stores that operated throughout the period as well as the full corresponding prior year period.

Added sales from new stores reflected the opening of 23 new stores since December 30, 2012, partially offset by a reduction in closed store sales.

We experienced decreased customer transactions in our retail stores, and the average sale per transaction also declined in the 39 weeks ended September 28, 2014 compared to the same period last year.

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Store count as of September 28, 2014 was 429 versus 420 as of September 29, 2013. We opened six new stores, one of which was a relocation, and closed six stores, four of which were relocations, in the 39 weeks ended September 28, 2014. We opened eight new stores, three of which were relocations, and closed two stores, both of which were relocations, in the 39 weeks ended September 29, 2013. For fiscal 2014, we expect to open approximately 10 net new stores.

*Gross Profit.* Gross profit decreased by \$13.6 million, or 5.5%, to \$234.3 million, or 32.2% of net sales, in the 39 weeks ended September 28, 2014 from \$247.9 million, or 33.3% of net sales, in the 39 weeks ended September 29, 2013. The change in gross profit was primarily attributable to the following:

Net sales decreased \$17.8 million, or 2.4%, year over year in the 39 weeks ended September 28, 2014.

Store occupancy expense increased by \$4.0 million, or 75 basis points, year over year due primarily to the increase in store count and increased rent associated with store lease renewals.

Merchandise margins, which exclude buying, occupancy and distribution expense, decreased 32 basis points versus the 39 weeks ended September 29, 2013, when merchandise margins increased 51 basis points versus the same period in fiscal 2012.

Distribution expense decreased \$0.6 million resulting primarily from higher costs capitalized into inventory, partially offset by higher employee labor and benefit-related expense and higher trucking expense. Distribution expense increased one basis point as a percentage of net sales due to the deleveraging of expense as a result of lower net sales.

*Selling and Administrative Expense.* Selling and administrative expense increased by \$4.4 million to \$213.9 million, or 29.4% of net sales, in the 39 weeks ended September 28, 2014 from \$209.5 million, or 28.1% of net sales, in the same period last year. The year-over-year increase in selling and administrative expense as a percentage of net sales reflects lower net sales along with higher expense. The increase in overall selling and administrative expense compared to the prior year was primarily attributable to higher employee labor and benefit-related expense and higher operating expense to support the increase in store count. We also recorded a pre-tax non-cash impairment charge of \$0.8 million related to certain underperforming stores in the second quarter of fiscal 2014, as discussed in Note 3 to the Interim Financial Statements included in Part I, Item 1, *Financial Statements*, of this Quarterly Report on Form 10-Q. These increases were partially offset by a decrease in legal expense reflecting a pre-tax charge of \$1.0 million to provide for legal settlements recorded in the third quarter of fiscal 2013, as well as a decrease in print advertising expense.

*Interest Expense.* Interest expense decreased by \$0.1 million to \$1.2 million in the 39 weeks ended September 28, 2014 compared to the same period last year. Interest expense reflected a decrease in average interest rates of 30 basis points to 1.9% in the 39 weeks ended September 28, 2014 from 2.2% in the prior year. The impact of lower average interest rates was partially offset by an increase in average debt levels of \$20.2 million to \$58.5 million in the 39 weeks ended September 28, 2014 from \$38.3 million in the same period last year.



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*Income Taxes.* The provision for income taxes was \$7.2 million for the 39 weeks ended September 28, 2014 and \$14.4 million for the 39 weeks ended September 29, 2013. Our effective tax rate was 37.3% for the 39 weeks ended September 28, 2014 compared with 38.7% for the 39 weeks ended September 29, 2013. The decreased effective tax rate year over year primarily resulted from income tax credits representing a larger percentage of pre-tax income for the current year. The effective rate for the 39 weeks ended September 29, 2013 included the retroactive reinstatement of the work opportunity tax credit ( WOTC ) for 2012, which resulted from enactment of The American Taxpayer Relief Act of 2012. Reinstatement of the WOTC reduced the effective tax rate for the first quarter of fiscal 2013 by 137 basis points.

**Liquidity and Capital Resources**

Our principal liquidity requirements are for working capital, capital expenditures and cash dividends. We fund our liquidity requirements primarily through cash on hand, cash flows from operations and borrowings from our revolving credit facility. We believe our cash on hand, future cash flows from operations and borrowings from our revolving credit facility will be sufficient to fund our cash requirements for at least the next 12 months.

We ended the third quarter of fiscal 2014 with \$5.6 million of cash compared with \$4.9 million at the end of the same period in fiscal 2013. Our cash flows from operating, investing and financing activities are summarized as follows:

	<b>39 Weeks Ended</b>	
	<b>September 28, 2014</b>	<b>September 29, 2013</b>
	<b>(In thousands)</b>	
Net cash provided by (used in):		
Operating activities	\$ 25,082	\$ 25,179
Investing activities	(14,627)	(12,597)
Financing activities	(14,214)	(15,286)
Net decrease in cash	\$ (3,759)	\$ (2,704)

*Operating Activities.* Net cash provided by operating activities for the 39 weeks ended September 28, 2014 and September 29, 2013 was \$25.1 million and \$25.2 million, respectively. The slight decrease in cash flow from operating activities for the 39 weeks ended September 28, 2014 compared to the same period last year primarily reflects lower net income for the current period and lower accrued expenses for certain employee benefits and legal expense, partially offset by reduced funding of inventory purchases and decreases in credit card receivables as a result of lower net sales.

*Investing Activities.* Net cash used in investing activities for the 39 weeks ended September 28, 2014 and September 29, 2013 was \$14.6 million and \$12.6 million, respectively. Capital expenditures, excluding non-cash property and equipment acquisitions, represented all of the cash used in investing activities for both periods. The higher capital expenditures in the current year primarily reflect purchases related to the development of a new point-of-sale system and costs related to the development of an e-commerce platform.

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*Financing Activities.* Net cash used in financing activities for the 39 weeks ended September 28, 2014 and September 29, 2013 was \$14.2 million and \$15.3 million, respectively. In the first nine months of fiscal 2014, net cash was used primarily to fund dividend payments and treasury stock repurchases, partially offset by increased borrowings under our revolving credit facility. In the first nine months of fiscal 2013, net cash was used primarily to pay down borrowings under our revolving credit facility and pay dividends, partially offset by proceeds received from the exercise of employee share option awards.

As of September 28, 2014, we had revolving credit borrowings of \$55.4 million and letter of credit commitments of \$0.7 million outstanding. These balances compare to revolving credit borrowings of \$43.0 million and letter of credit commitments of \$0.9 million outstanding as of December 29, 2013 and revolving credit borrowings of \$37.9 million and letter of credit commitments of \$0.8 million outstanding as of September 29, 2013. The increase in revolving credit borrowings at the end of the third quarter of fiscal 2014 compared to the same period last year primarily reflects higher inventory levels as a result of lower-than-anticipated sales as well as increased funding of other working capital.

In fiscal 2013 and the first nine months of fiscal 2014, we paid quarterly cash dividends of \$0.10 per share of outstanding common stock, for an annual rate of \$0.40 per share. In the fourth quarter of fiscal 2014, our Board of Directors declared a quarterly cash dividend of \$0.10 per share of outstanding common stock, which will be paid on December 15, 2014 to stockholders of record as of December 1, 2014.

Periodically, we repurchase our common stock in the open market pursuant to programs approved by our Board of Directors. We may repurchase our common stock for a variety of reasons, including, among other things, our existing business conditions, our alternative cash requirements and the current market price of our stock. In fiscal 2013, we did not repurchase any shares of our common stock. In the first nine months of fiscal 2014, we repurchased 205,724 shares of common stock for \$2.4 million. Since the inception of our initial share repurchase program in May 2006 through September 28, 2014, we have repurchased a total of 2,133,350 shares for \$27.7 million, leaving a total of \$7.3 million available for share repurchases under our current share repurchase program.

*Credit Agreement.* On October 18, 2010, we entered into a credit agreement with Wells Fargo Bank, National Association ( Wells Fargo ), as administrative agent, and a syndicate of other lenders, which was amended on October 31, 2011 and December 19, 2013 (as so amended, the Credit Agreement ) as further discussed below. The maturity date of the Credit Agreement is December 19, 2018.

The Credit Agreement provides for a revolving credit facility (the Credit Facility ) with an aggregate committed availability of up to \$140.0 million, which amount may be increased at our option up to a maximum of \$165.0 million. We may also request additional increases in aggregate availability, up to a maximum of \$200.0 million, in which case the existing lenders under the Credit Agreement will have the option to increase their commitments to accommodate the requested increase. If such existing lenders do not exercise

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that option, we may (with the consent of Wells Fargo, not to be unreasonably withheld) seek other lenders willing to provide such commitments. The Credit Facility includes a \$50.0 million sublimit for issuances of letters of credit and a \$20.0 million sublimit for swingline loans. Total remaining borrowing availability under the Credit Agreement, after subtracting letters of credit, was \$83.9 million and \$96.1 million as of September 28, 2014 and December 29, 2013, respectively.

We may borrow under the Credit Facility from time to time, provided the amounts outstanding will not exceed the lesser of the then aggregate availability (as discussed above) and the Borrowing Base (such lesser amount being referred to as the **Loan Cap** ). After giving effect to the amendments, the **Borrowing Base** generally is comprised of the sum, at the time of calculation of (a) 90.00% of our eligible credit card receivables; plus (b) the cost of our eligible inventory (other than our eligible in-transit inventory), net of inventory reserves, multiplied by 90.00% of the appraised net orderly liquidation value of eligible inventory (expressed as a percentage of the cost of eligible inventory); plus (c) the lesser of (i) the cost of our eligible in-transit inventory, net of inventory reserves, multiplied by 90.00% of the appraised net orderly liquidation value of our eligible in-transit inventory (expressed as a percentage of the cost of eligible in-transit inventory), or (ii) \$10.0 million, minus (d) certain reserves established by Wells Fargo in its role as the Administrative Agent in its reasonable discretion.

Generally, we may designate specific borrowings under the Credit Facility as either base rate loans or LIBO rate loans. Following the most recent amendment of the Credit Agreement on December 19, 2013 (the **Second Amendment** ), the applicable interest rate on our borrowings will be a function of the daily average, over the preceding fiscal quarter, of the excess of the **Loan Cap** over amounts borrowed (such amount being referred to as the **Average Daily Excess Availability** ). Those loans designated as LIBO rate loans shall bear interest at a rate equal to the then applicable LIBO rate plus an applicable margin as shown in the table below. Those loans designated as base rate loans shall bear interest at a rate equal to the applicable margin for base rate loans (as shown below) plus the highest of (a) the Federal funds rate, as in effect from time to time, plus one-half of one percent (0.50%), (b) the LIBO rate, as adjusted to account for statutory reserves, plus one percent (1.00%), or (c) the rate of interest in effect for such day as publicly announced from time to time by Wells Fargo as its **prime rate**. The applicable margin for all loans will be as set forth below as a function of **Average Daily Excess Availability** for the preceding fiscal quarter.



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Level	Average Daily Excess Availability	LIBO Rate Applicable Margin	Base Rate Applicable Margin
I	Greater than or equal to \$100,000,000	1.25%	0.25%
II	Less than \$100,000,000 but greater than		
	or equal to \$40,000,000	1.50%	0.50%
III	Less than \$40,000,000	1.75%	0.75%

Following the Second Amendment, the commitment fee assessed on the unused portion of the Credit Facility is 0.25% per annum.

Obligations under the Credit Facility are secured by a general lien and perfected security interest in substantially all of our assets. Our Credit Agreement contains covenants that require us to maintain a fixed charge coverage ratio of not less than 1.0:1.0 in certain circumstances, and limit our ability to, among other things, incur liens, incur additional indebtedness, transfer or dispose of assets, change the nature of the business, guarantee obligations, pay dividends or make other distributions or repurchase stock, and make advances, loans or investments. We may declare or pay cash dividends or repurchase stock only if, among other things, no default or event of default then exists or would arise from such dividend or repurchase of stock and, after giving effect to such dividend or repurchase, certain availability and/or fixed charge coverage ratio requirements are satisfied. The Credit Agreement contains customary events of default, including, without limitation, failure to pay when due principal amounts with respect to the Credit Facility, failure to pay any interest or other amounts under the Credit Facility for five days after becoming due, failure to comply with certain agreements or covenants contained in the Credit Agreement, failure to satisfy certain judgments against us, failure to pay when due (or any other default which does or may lead to the acceleration of) certain other material indebtedness in principal amount in excess of \$5.0 million, and certain insolvency and bankruptcy events.

*Future Capital Requirements.* We had cash on hand of \$5.6 million as of September 28, 2014. We expect capital expenditures for fiscal 2014, excluding non-cash acquisitions, to range from approximately \$24.0 million to \$26.0 million, primarily to fund the opening of new stores, store-related remodeling, distribution center equipment and computer hardware and software purchases, including amounts related to the development of a new point-of-sale system and the development of an e-commerce platform. For fiscal 2014, we expect to open approximately 10 net new stores.

We currently pay quarterly dividends, subject to declaration by our Board of Directors. In the fourth quarter of fiscal 2014, our Board of Directors declared a quarterly cash dividend of \$0.10 per share of outstanding common stock, which will be paid on December 15, 2014 to stockholders of record as of December 1, 2014.

As of September 28, 2014, a total of \$7.3 million remained available for share repurchases under our share repurchase program. We consider several factors in determining when and if we make share repurchases including, among other things, our existing business conditions, our alternative cash requirements and the market price of our stock.

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We believe we will be able to fund our cash requirements, for at least the next 12 months, from cash on hand, operating cash flows and borrowings from our revolving credit facility. However, our ability to satisfy our cash requirements depends upon our future performance, which in turn is subject to general economic conditions and regional risks, as well as financial, business and other factors affecting our operations, including factors beyond our control. There is no assurance that we will be able to generate sufficient cash flows or that we will be able to maintain our ability to borrow under our revolving credit facility.

*Off-Balance Sheet Arrangements and Contractual Obligations.* Our material off-balance sheet arrangements are operating lease obligations and letters of credit. We excluded these items from the balance sheet in accordance with accounting principles generally accepted in the United States of America.

Operating lease commitments consist principally of leases for our retail store facilities, distribution center and corporate office locations. These leases frequently include options which permit us to extend the terms beyond the initial fixed lease term. With respect to most of those leases, we intend to renegotiate those leases as they expire.

Our material contractual obligations include capital lease obligations, borrowings under our Credit Facility, certain occupancy expense related to our leased properties and other liabilities. Capital lease obligations, which include imputed interest, consist principally of leases for some of our distribution center delivery tractors, management information systems hardware and point-of-sale equipment for our stores. Our Credit Facility debt fluctuates daily depending on operating, investing and financing cash flows. Other occupancy expense includes estimated property maintenance fees and property taxes for our stores, distribution center and corporate headquarters. Other liabilities consist principally of actuarially-determined reserve estimates related to self-insurance liabilities, a contractual obligation for the surviving spouse of Robert W. Miller, our co-founder, and asset retirement obligations related to the removal and retirement of leasehold improvements for certain stores upon termination of their leases.

Issued and outstanding letters of credit were \$0.7 million as of September 28, 2014, and were related primarily to securing insurance program liabilities.

Included in the *Liquidity and Capital Resources* section of Part II, Item 7, *Management's Discussion and Analysis of Financial Condition and Results of Operations*, of our Annual Report on Form 10-K for the fiscal year ended December 29, 2013, is a discussion of our future obligations and commitments as of December 29, 2013. In the 39 weeks ended September 28, 2014, our revolving credit borrowings increased by \$12.4 million from the end of fiscal 2013. We entered into new operating lease agreements in relation to our business operations during the 39 weeks ended September 28, 2014. We do not believe that these operating leases or the increase in our revolving credit borrowings materially impact our contractual obligations or commitments presented as of December 29, 2013.

In the ordinary course of business, we enter into arrangements with vendors to purchase merchandise in advance of expected delivery. Because most of these purchase orders do not contain any termination payments or other penalties if cancelled, they are not included as outstanding contractual obligations.

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### **Critical Accounting Estimates**

As discussed in Part II, Item 7, *Management's Discussion and Analysis of Financial Condition and Results of Operations*, of our Annual Report on Form 10-K for the fiscal year ended December 29, 2013, we consider our estimates on inventory valuation, long-lived assets and self-insurance liabilities to be the most critical in understanding the judgments that are involved in preparing our consolidated financial statements. There have been no significant changes to these estimates in the 39 weeks ended September 28, 2014.

### **Seasonality and Impact of Inflation**

We experience seasonal fluctuations in our net sales and operating results. In the fourth fiscal quarter, which includes the holiday selling season, we normally experience higher inventory purchase volumes and increased expense for staffing and advertising. Seasonality influences our buying patterns which directly impacts our merchandise and accounts payable levels and cash flows. We purchase merchandise for seasonal activities in advance of a season. If we miscalculate the demand for our products generally or for our product mix during the fourth fiscal quarter, our net sales can decline, which can harm our financial performance. A significant shortfall from expected fourth fiscal quarter net sales can negatively impact our annual operating results.

In fiscal 2013 and 2014, we experienced minor inflation in the purchase cost, including transportation expense, of certain products. We continue to evolve our product mix to include more branded merchandise that we believe gives us added flexibility to adjust selling prices for purchase cost increases. If we are unable to adjust our selling prices for purchase cost increases then our merchandise margins will decline, which will adversely impact our operating results. We do not believe that inflation had a material impact on our operating results for the reporting periods.

### **Recently Issued Accounting Updates**

See Note 2 to the Interim Financial Statements included in Part I, Item 1, *Financial Statements*, of this Quarterly Report on Form 10-Q.

### **Forward-Looking Statements**

This document includes certain forward-looking statements within the meaning of the Private Securities Litigation Reform Act of 1995. Such forward-looking statements relate to, among other things, our financial condition, our results of operations, our growth strategy and the business of our company generally. In some cases, you can identify such statements by terminology such as *may*, *could*, *project*, *estimate*, *potential*, *continue*, *should*, *anticipates*, *believes*, *intends* or other such terminology. These forward-looking statements involve known and unknown risks, uncertainties and other factors that may cause our actual results in future periods to differ materially from forecasted results. These risks and uncertainties include, among other things, continued or worsening weakness in the consumer spending environment and the U.S. financial and credit markets,

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fluctuations in consumer holiday spending patterns, breach of data security or other unauthorized disclosure of sensitive personal or confidential information, the competitive environment in the sporting goods industry in general and in our specific market areas, inflation, product availability and growth opportunities, changes in the current market for (or regulation of) firearms, ammunition and related products, seasonal fluctuations, weather conditions, changes in cost of goods, operating expense fluctuations, higher-than-expected costs related to the development of an e-commerce platform, delay in completing the e-commerce platform, lower-than-expected profitability of the e-commerce platform or cannibalization of sales from our existing store base which could occur as a result of operating our e-commerce platform, litigation risks, disruption in product flow, changes in interest rates, credit availability, higher expense associated with sources of credit resulting from uncertainty in financial markets and economic conditions in general. Those and other risks and uncertainties are more fully described in Part II, Item 1A, *Risk Factors*, in this report and in Part I, Item 1A, *Risk Factors*, in our Annual Report on Form 10-K and other filings with the United States Securities and Exchange Commission. We caution that the risk factors set forth in this report are not exclusive. In addition, we conduct our business in a highly competitive and rapidly changing environment. Accordingly, new risk factors may arise. It is not possible for management to predict all such risk factors, nor to assess the impact of all such risk factors on our business or the extent to which any individual risk factor, or combination of factors, may cause results to differ materially from those contained in any forward-looking statement. We undertake no obligation to revise or update any forward-looking statement that may be made from time to time by us or on our behalf.

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**Item 3. Quantitative and Qualitative Disclosures About Market Risk**

We are subject to risks resulting from interest rate fluctuations since interest on our borrowings under our Credit Facility is based on variable rates. We enter into borrowings under our Credit Facility principally for working capital, capital expenditures and general corporate purposes. We routinely evaluate the best use of our cash on hand and manage financial statement exposure to interest rate fluctuations by managing our level of indebtedness and the interest base rate options on such indebtedness. We do not utilize derivative instruments and do not engage in foreign currency transactions or hedging activities to manage our interest rate risk. If the interest rate on our debt was to change 1.0% as compared to the rate as of September 28, 2014, our interest expense would change approximately \$0.6 million on an annual basis based on the outstanding balance of borrowings under our Credit Facility as of September 28, 2014.

Inflationary factors and changes in foreign currency rates can increase the purchase cost of our products. We are evolving our product mix to include more branded merchandise that we believe will give us added flexibility to adjust selling prices for purchase cost increases. If we are unable to adjust our selling prices for purchase cost increases then our merchandise margins will decline, which will adversely impact our operating results. All of our stores are located in the United States, and all imported merchandise is purchased in U.S. dollars. We do not believe that inflation had a material impact on our operating results for the reporting periods.

**Item 4. Controls and Procedures**

*Evaluation of Disclosure Controls and Procedures*

We conducted an evaluation, under the supervision and with the participation of our Chief Executive Officer ( CEO ) and Chief Financial Officer ( CFO ), of the effectiveness of the design and operation of our disclosure controls and procedures (as such term is defined in Rules 13a-15(e) and 15d-15(e) under the Securities Exchange Act of 1934, as amended (the Exchange Act )) as of the end of the period covered by this report. Based on such evaluation, our CEO and CFO have concluded that, as of the end of such period, our disclosure controls and procedures are effective, at a reasonable assurance level, in recording, processing, summarizing and reporting, on a timely basis, information required to be disclosed by us in the reports that we file or submit under the Exchange Act and are effective in ensuring that information required to be disclosed by us in the reports that we file or submit under the Exchange Act is accumulated and communicated to our management, including our CEO and CFO, as appropriate to allow timely decisions regarding required disclosure.

*Changes in Internal Control Over Financial Reporting*

During the fiscal quarter ended September 28, 2014, no changes occurred with respect to our internal control over financial reporting that materially affected, or are reasonably likely to materially affect, internal control over financial reporting.

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**PART II. OTHER INFORMATION**

**Item 1. Legal Proceedings**

The Company was served on the following dates with the following nine complaints, each of which was brought as a purported class action on behalf of persons who made purchases at the Company's stores in California using credit cards and were requested or required to provide personal identification information at the time of the transaction: (1) on February 22, 2011, a complaint filed in the California Superior Court in the County of Los Angeles, entitled *Maria Eugenia Saenz Valiente v. Big 5 Sporting Goods Corporation*, et al., Case No. BC455049; (2) on February 22, 2011, a complaint filed in the California Superior Court in the County of Los Angeles, entitled *Scott Mossler v. Big 5 Sporting Goods Corporation*, et al., Case No. BC455477; (3) on February 28, 2011, a complaint filed in the California Superior Court in the County of Los Angeles, entitled *Yelena Matatova v. Big 5 Sporting Goods Corporation*, et al., Case No. BC455459; (4) on March 8, 2011, a complaint filed in the California Superior Court in the County of Los Angeles, entitled *Neal T. Wiener v. Big 5 Sporting Goods Corporation*, et al., Case No. BC456300; (5) on March 22, 2011, a complaint filed in the California Superior Court in the County of San Francisco, entitled *Donna Motta v. Big 5 Sporting Goods Corporation*, et al., Case No. CGC-11-509228; (6) on March 30, 2011, a complaint filed in the California Superior Court in the County of Alameda, entitled *Steve Holmes v. Big 5 Sporting Goods Corporation*, et al., Case No. RG11563123; (7) on March 30, 2011, a complaint filed in the California Superior Court in the County of San Francisco, entitled *Robin Nelson v. Big 5 Sporting Goods Corporation*, et al., Case No. CGC-11-508829; (8) on April 8, 2011, a complaint filed in the California Superior Court in the County of San Joaquin, entitled *Pamela B. Smith v. Big 5 Sporting Goods Corporation*, et al., Case No. 39-2011-00261014-CU-BT-STK; and (9) on May 31, 2011, a complaint filed in the California Superior Court in the County of Los Angeles, entitled *Deena Gabriel v. Big 5 Sporting Goods Corporation*, et al., Case No. BC462213. On June 16, 2011, the Judicial Council of California issued an Order Assigning Coordination Trial Judge designating the California Superior Court in the County of Los Angeles as having jurisdiction to coordinate and to hear all nine of the cases as Case No. JCCP4667. On October 21, 2011, the plaintiffs collectively filed a Consolidated Amended Complaint, alleging violations of the California Civil Code, negligence, invasion of privacy and unlawful intrusion. The plaintiffs allege, among other things, that customers making purchases with credit cards at the Company's stores in California were improperly requested to provide their zip code at the time of such purchases. The plaintiffs seek, on behalf of the class members, the following: statutory penalties; attorneys' fees; expenses; restitution of property; disgorgement of profits; and injunctive relief. In an effort to negotiate a settlement of this litigation, the Company and plaintiffs engaged in Mandatory Settlement Conferences conducted by the court on February 6, 2013, February 19, 2013, April 2, 2013, September 12, 2013, and September 20, 2013, and also engaged in mediation conducted by a third party mediator on July 15, 2013. As a result of the foregoing, the parties agreed to settle the lawsuit. On March 23, 2014, the court granted preliminary approval of the settlement. The court has scheduled a hearing for November 10, 2014, to consider granting final approval of the settlement. Under the terms of the settlement, the Company agreed that class members who submit valid and timely claim forms will receive either a \$25 gift card (with proof of purchase) or a \$10 merchandise voucher (without proof of purchase). Additionally, the

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Company agreed to pay plaintiff's attorneys' fees and costs awarded by the court, enhancement payments to the class representatives and claims administrator's fees. Under the settlement, if the total amount paid by the Company for the class payout, class representative enhancement payments and claims administrator's fees is less than \$1.0 million, then the Company will issue merchandise vouchers to a charity for the balance of the deficiency in the manner provided in the settlement agreement. The Company's estimated total cost pursuant to this settlement is reflected in a legal settlement accrual recorded in the third quarter of fiscal 2013. The Company admitted no liability or wrongdoing with respect to the claims set forth in the lawsuit. Once final approval is granted, the settlement will constitute a full and complete settlement and release of all claims related to the lawsuit. Based on the terms of the settlement agreement, the Company currently believes that settlement of this litigation will not have a material negative impact on the Company's results of operations or financial condition. However, if the settlement is not finally approved by the court, the Company intends to defend this litigation vigorously. If the settlement is not finally approved by the court and this litigation is settled or resolved unfavorably to the Company, this litigation and the costs of defending it could have a material negative impact on the Company's results of operations or financial condition.

The Company is involved in various other claims and legal actions arising in the ordinary course of business. In the opinion of management, the ultimate disposition of these matters is not expected to have a material adverse effect on the Company's results of operations or financial condition.

## **Item 1A. Risk Factors**

There have been no material changes to the risk factors identified in Part I, Item 1A, *Risk Factors*, of the Company's Annual Report on Form 10-K for the fiscal year ended December 29, 2013.

**Table of Contents****Item 2. Unregistered Sales of Equity Securities and Use of Proceeds**

The following tabular summary reflects the Company's share repurchase activity during the quarter ended September 28, 2014:

**ISSUER PURCHASES OF EQUITY SECURITIES <sup>(1) (2)</sup>**

<i>Period</i>	<i>Total Number of Shares Purchased</i>	<i>Average Price Paid per Share</i>	<i>Total Number of Shares Purchased as Part of Publicly Announced Plans or Programs</i>	<i>Maximum Number (or Approximate Dollar Value) of Shares that May Yet Be Purchased Under the Plans or Programs <sup>(3)</sup></i>
June 30 – July 27		\$		\$ 8,429,000
July 28 – August 24	48,200	\$ 10.04	48,200	\$ 7,945,000
August 25 – September 28	66,000	\$ 10.23	66,000	\$ 7,270,000
Total	114,200		114,200	\$ 7,270,000

- (1) All shares were purchased under the Company's current share repurchase program, which was announced on November 1, 2007 and authorizes the repurchase of the Company's common stock totaling \$20.0 million. Under the authorization, the Company may purchase shares from time to time in the open market or in privately negotiated transactions in compliance with the applicable rules and regulations of the SEC. However, the timing and amount of such purchases, if any, would be at the discretion of management and would depend upon market conditions and other considerations. Since the inception of the initial share repurchase program in May 2006 through September 28, 2014, the Company has repurchased a total of 2,133,350 shares for \$27.7 million, leaving a total of \$7.3 million available for share repurchases under the current share repurchase program.
- (2) The Company's dividends and stock repurchases are generally funded by distributions from its subsidiary, Big 5 Corp. The Company's Credit Agreement contains covenants that require it to maintain a fixed charge coverage ratio of not less than 1.0:1.0 in certain circumstances, and limit the ability to, among other things, pay dividends or repurchase stock. The Company may declare or pay cash dividends or repurchase stock only if, among other things, no default or event of default then exists or would arise from such dividend or repurchase of stock and, after giving effect to such dividend or repurchase, certain availability and/or fixed charge coverage ratio requirements are satisfied. See Part I, Item 2, *Management's Discussion and Analysis of Financial Condition and Results of Operations – Liquidity and Capital Resources*, for a further discussion of the Credit Agreement.
- (3) This amount reflects the dollar value of shares remaining available to repurchase under previously announced plans.





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**Item 3. Defaults Upon Senior Securities**

None.

**Item 4. Mine Safety Disclosures**

None.

**Item 5. Other Information**

None.

**Item 6. Exhibits**

(a) Exhibits

<b>Exhibit Number</b>	<b>Description of Document</b>
15.1	Independent Auditors Awareness Letter Regarding Interim Financial Statements.
31.1	Rule 13a-14(a) Certification of Chief Executive Officer.
31.2	Rule 13a-14(a) Certification of Chief Financial Officer.
32.1	Section 1350 Certification of Chief Executive Officer.
32.2	Section 1350 Certification of Chief Financial Officer.
101.INS	XBRL Instance Document.
101.SCH	XBRL Taxonomy Extension Schema Document.
101.CAL	XBRL Taxonomy Calculation Linkbase Document.
101.DEF	XBRL Taxonomy Definition Linkbase Document.
101.LAB	XBRL Taxonomy Label Linkbase Document.
101.PRE	XBRL Taxonomy Presentation Linkbase Document.

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**SIGNATURES**

Pursuant to the requirements of the Securities Exchange Act of 1934, the registrant has duly caused this report to be signed on its behalf by the undersigned thereunto duly authorized.

**BIG 5 SPORTING GOODS CORPORATION,**  
a Delaware corporation

Date: October 29, 2014

By: */s/ Steven G. Miller*  
*Steven G. Miller*  
*Chairman of the Board of Directors,*  
*President and Chief Executive Officer*

Date: October 29, 2014

By: */s/ Barry D. Emerson*  
*Barry D. Emerson*  
*Senior Vice President,*  
*Chief Financial Officer and Treasurer*  
*(Principal Financial and*  
*Accounting Officer)*

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